"International Investment or Capital Flows — FDI & FPI"

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Introduction:—

Capital is a vital ingredient for economic growth, but since most nations cannot meet their total capital requirements from internal resources alone, they turn to foreign investors. International capital flows are the financial side of International Trade. FDI (Foreign direct investment) and FPI (Foreign Portfolio/Institutional investment) are two of the most common routes for investors to invest in an overseas economy.

Meaning:— FDI implies investment by foreign investors directly in the productive assets of another nation. FPI means investing in financial assets, such as stocks and bonds of entities located in another country.

FDI & FPI are both important sources of funding for most economies.

Foreign Capital Can be used to develop infrastructure, set up manufacturing facilities and service hubs, and invest in other productive assets such as machinery and equipment, which contributes to economic growth and stimulates employment.

A marvellous advantage of both FDI and FPI is that the receiving country need not repay the debt like in the case of External Commercial Borrowings (foreign Loans). Both are thus described as non-debt creating, and hence involve no payment obligations. Their own servicing depends on future growth of the economy. This is why most developing countries prefer FDI and FPI compared to other forms of foreign capital like ECBs.

When making foreign investments, investors have to consider economic factors as well as other risk factors, such as political instability and currency exchange risk. These factors

Can be used to decide if an investment Should be direct or through a portfolio.

Differences:- FDI and FPI are similar in some respects but very different in others. Given below are *some of the key differences between the two.

1) Foreign direct investment (FDI) involves establishing a direct business interest in a foreign Country, such as buying or establishing a manufacturing business, building warehouses, or buying buildings. On the other hand, Foreign Portfolio investment (FPI) refers to investing in the financial assets of a foreign country, such as stocks or bonds available on an exchange. It is indirect investment.

2) FDI Creates Productive assets and brings in long-term Capital for an economy. FPI doesnot aid Productive asset creation directly. It is just a financial investment. Its destination Period is small.

3) FDI includes having control over

The business invested in and being able to manage it directly, but it also involves more risk, Work and Commitment. Unlike direct investment, Portfolio investment does not offer Control over the business entity in which the investment is made.

4) Direct Investment is seen as a long term investment in the Country's economy, While Portfolio investment Can be viewed as a Short-term move to make money. As with any equity investment, foreign Portfolio investors usually expect to quickly realize a profit on their investments.

5) Foreign Portfolio investments are more accessible for the average investor than direct investments because they require much less investment Capital and research.

6) One of the most important distinctions between Portfolio and direct investment to have emerged in the era of

globalization is that Portfolio investment Can be much more volatile. Changes in the investment environment in a Country Can lead to Swift changes in Portfolio investment. In Contrast, FDI is more difficult to pull out or sell off as it implies a Controlling stake and thus stable.

Conclusion:—

If FDI is Certain, long term and less fluctuating, FPI is Speculative, highly volatile and Un-predictive. Hence, FDI is superior to FPI from the angle of a developing Country like India.