



MARKETS IN MOTION

developments that matter in financial markets

Emerging Markets Attract Global Investors

“Capital flows aid growth by providing external capital to sustain an excess of investment over domestic savings. By affording the opportunity of using the world market, an open capital account permits both savers and investors to diversify their portfolios to maximize returns and minimize risks.”

Dr Duvvuri Subbarao, Governor, Reserve Bank of India

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For details, contact:
Ms Meena Kulkarni
Tel: +91 22 6731 8842
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Introduction

Emerging markets, which have been growing much faster than advanced economies, are increasingly being seen as more fundamentally safe investment destinations. The pattern of inflows in the first half of 2010 points to further momentum in net foreign investment in equities in many emerging markets as these economies are leading the economic recovery and will remain major destinations for equity investment. The following table reveals that net foreign investment in emerging market economies during the first half of 2010 is uneven. While Japan, India, Indonesia and Philippines have witnessed a YoY spurt in investments in 2010 (till August 11), the inflows are lower in countries like Brazil and South Africa.

Net Foreign Investment in Equities	2010 (till Aug 11) (in \$m)	2009 Aggregate (in \$m)
Japan	21,665	17,078
South Africa	2,508	8,979
Brazil	867	10,028
Taiwan	2,645	13,720
Korea	7,357	24,827
India	11,363	17,626
Thailand	-208	1,141
Indonesia	1,373	1,385
Philippines	437	132

Source: Bloomberg, JP Morgan, EPFR Global Data

India and FII Inflows

The FII outlook for India remains positive in the second half of the year, with another \$5-7 billion expected to flow into Indian equities, according to recent Merrill Lynch Global Wealth Management estimates. During January-June 2010, FIIs invested \$6.88 billion in equities and \$6.08 billion in debt. Data sourced from SEBI shows that the number of registered FIIs stood at 1,713 and number of registered sub-accounts rose to 5,426 as of June 30, 2010. There has been a steady increase in FII cumulative net investment but the incremental yearly growth has been uneven. FIIs share in the market capitalization is roughly 14 percent and portfolio investments brought in by FIIs have been the most dynamic source of capital to India.

FII Shareholding Pattern as on March 31, 2010

Segments	No of shares %	Market capitalization %
I Promoter Group	54.46	56.35
II Public Shareholding	36.92	29.98
III FII	8.62	13.67
Total	100	100

FIIs have shown a marked preference for investment in the financial sector, followed by materials and energy segments. The following table shows the portfolio trends of FIIs in the last two quarters.

FII portfolio sector trend

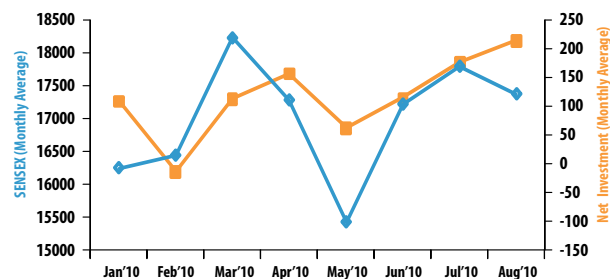
Sector	Portfolio share		
	Dec '09	Mar '10	June '10
Cons. Disc.	7.63%	5.44%	5.73%
Cons. Stap.	11.05%	10.71%	11.91%
Energy	11.55%	11.27%	11.80%
Financials	24.40%	24.90%	24.78%
Health Care	3.62%	3.58%	3.69%
Industrials	8.32%	10.26%	10.57%
IT	5.74%	5.55%	5.44%
Materials	15.26%	16.64%	14.09%
Telecom	3.54%	3.22%	3.03%
Utilities	8.90%	8.44%	8.94%

Source: RCML Research, CMIE

FII Inflows and Sensex

It may be observed that FII inflows impact Sensex volatility to some extent, though Sensex volatility is a function of many variables.

SENSEX vs. FII Net Investment



The overall performance of both emerging market equities and bonds is also attracting the attention of institutional investors. Capital flows are important to meet the investment needs of emerging market economies. Problems arise when the inflows are largely in excess of the economy's absorptive capacity and also when they are highly speculative in nature.

Contributed by M Ravindran

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Exchange Square, 1st Floor, Suren Road,
Chakala, Andheri (East), Mumbai - 400093, India.
Tel: +91 22 6731 8888 • Fax: +91 22 6726 9541
Email: marketsinmotion@ftkmc.com • Website: www.ftkmc.com

Register Now
For details, contact:
Mr Afzal Saboovala
+91 99302 67954
afzal.saboovala@ftkmc.com

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