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MUTUAL FUND

FPI Debt Flows – The Less Flashy Cousin, To the Rescue?

1. The whole world is fixated on foreign portfolio flows into equities, but **FPI debt inflows are not insignificant**. Since FY99, India has received \$154.4 Bn in FPI equity flows and \$95.5 Bn in FPI debt flows. Debt flows are 62% of cumulative equity flows and nearly 38% of combined equity plus debt FPI flows. This is not a footnote.
2. Since India entered global bond indices, the character of debt flows has changed. The Debt-FAR route, which allows FPIs fully open access to specified government securities, has become the dominant channel. **Since FY25, India has received around \$19.3 Bn of FPI debt inflows, of which \$11.8 Bn came through Debt-FAR**. In Mar-2025, the single biggest month for FPI debt flows, India received \$4.3 Bn, of which \$3.3 Bn came through FAR. **If the reported capital gains tax removal for FPIs in government securities goes through, FAR can become a quasi-open, tax-efficient window for global investors to buy Indian debt**. It can also help GOI in meeting its borrowing needs.
3. The largest debt inflow phase was the 2010-2015 cycle. The best rolling 5-year period was Mar-2010 to Feb-2015, when India received \$46.5 Bn in FPI debt flows with average 10-year G-Sec yields at 8.23%. The cleanest high-yield phase was May-2014 to Apr-2015, with \$29.4 Bn of inflows, 8.23% average 10-year yield, 5.62% inflation and 2.61% real yield. The data shows that FPIs like high nominal yields, but the cleanest signal appears when high nominal yields are accompanied by positive real yields. **Months where 10-year G-Sec yields were above 8% brought \$35.8 Bn of flows, but when real yields were above 2%, India received \$51.6 Bn of FPI debt inflows overall**. **Currently, real GSec yields are much higher than 2%.**

- 4. FPI debt flows can become an important stabilizer for the economy. They are volatile, but useful.** Since 2003, India has seen net \$95.3 Bn of net FPI debt flows. The recent Mar-2023 to Feb-2026 phase alone brought \$34.5 Bn at an average 10-year yield of 6.8% and real yield of 2.8%. **At a time when the capital account has been pressured by weak equity FPI flows and FDI outflows, debt flows can help bridge the current account deficit, reduce pressure on the rupee and give policymakers one more useful external-sector stabilizer. It may not always be about equity; the debt market can also attract flows which are somewhat more stable.**
- 5. FPI debt flows are not just yield tourism. FPIs prefer four things: positive real yield, stable or appreciating currency expectation, clean access and benign global risk appetite.** India currently offers strong real yields, and the rupee valuation comfort has improved with broad REER below 90. Access is the policy lever, and FAR already provides the base structure. **Removal of capital gains tax can improve it further.** It will provide better post tax returns to FPIs at a time when real yields are significantly higher than the past. Global risk appetite is not in India's control, but when it turns favourable, the flow response can be large, as seen in 2014-15, 2017 and the recent bond-index inclusion phase. Eventually India will continue to run a current account deficit and will need to attract foreign capital through equity based FDI. **This is an ancillary solution which can help in an adverse global environment, and probably better than trying to only fix the current account using import duty on precious metals.**

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