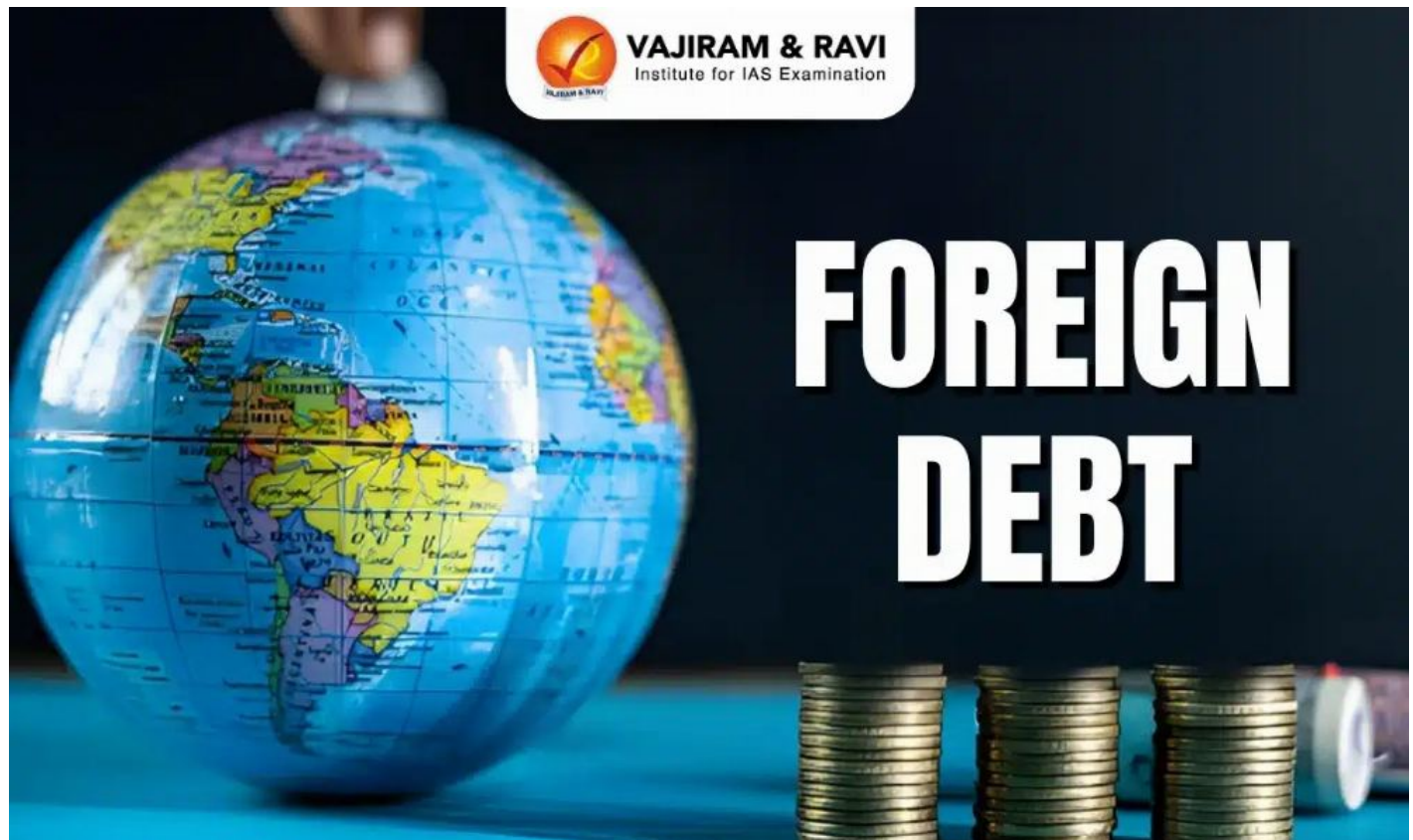


Foreign Debt Inflows Fall Short Despite Easier FAR Norms

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Foreign Debt Latest News

Foreign debt inflows into India have remained below expectations in 2025 despite relaxed norms under the Fully Accessible Route (FAR) and inclusion of Indian bonds in global indices.

Background

- India's efforts to attract more foreign debt investments under the **Fully Accessible Route (FAR)** have yielded modest results in 2025, despite expectations of record inflows following policy liberalisation and global index inclusion.
- Data from the **National Securities Depository Ltd (NSDL)** shows that **foreign portfolio investor (FPI) inflows into Indian debt** have amounted to just **Rs. 69,073 crore (\$7.8 billion)** so far this year, far short of the anticipated **\$20-25 billion** expected through FAR alone.

About the Fully Accessible Route (FAR)

- The **Fully Accessible Route** is a policy framework introduced by the **Reserve Bank of India (RBI)** and **SEBI** to liberalise foreign investment in Indian government securities (G-secs).
- Under FAR, **foreign portfolio investors and other eligible non-resident investors** can **freely invest** in specified G-secs **without any investment caps**, repatriation limits, or sectoral restrictions.
- The FAR mechanism aims to:
 - Deepen the **Indian debt market**,
 - Enhance the inclusion of Indian bonds in **global indices**, and
 - Attract **long-term, stable foreign capital** into government securities.
- Indian G-secs under FAR are considered particularly attractive due to **competitive yields, policy stability**, and **full repatriation rights**, features designed to align India's bond market with global best practices.

Expectations and Reality: A Missed Opportunity

- When **JP Morgan** announced the inclusion of Indian Government Bonds (IGBs) in its **Emerging Markets Bond Index**, analysts projected inflows of around **\$20-25 billion** over a ten-month period till March 2025.
- However, cumulative inflows from 2024-2025 have reached only **\$10.7 billion**, less than half of projections.
- **Investment Distribution (2025 so far):**
 - **FAR Category:** Rs. 66,528 crore (\$7.5 billion)
 - **Debt-General Category:** Rs. 12,083 crore (\$1.3 billion)
 - **Debt-VRR (Voluntary Retention Route):** Outflow of Rs. 9,538 crore
- This represents a significant reversal from 2024, when **Rs. 1.52 lakh crore (\$17.3 billion)** flowed into Indian debt, led largely by general category investments.

Cautious Policy Moves by the Government and RBI

- In August 2024, following India's bond index inclusion, the government and RBI made a strategic move by **excluding long-term government bonds (14-year and 30-year maturities)** from the FAR.
- The decision was driven by concerns that **unrestricted inflows could destabilise domestic markets**, increase yield volatility, and amplify risks if global investors engaged in short-term arbitrage.
- While the policy ensured macroeconomic prudence, it simultaneously **limited the pool of eligible securities**, curbing potential inflows.

Global and Domestic Factors Behind Slower Inflows

- Several **macroeconomic and geopolitical factors** have influenced investor behaviour in 2025.
- **Global Uncertainty and Interest Rate Volatility:**
 - Unpredictable rate movements by the **U.S. Federal Reserve**, coupled with persistent **geopolitical tensions** and inflation concerns, have made global investors cautious.
- **Shift in FPI Strategy:**
 - FPIs have **withdrawn Rs. 1.39 lakh crore from Indian equities** this year, reflecting a preference for short-term tactical moves rather than broad-based exposure.

- **Selective Debt Investments:**

- While Indian G-secs offer steady returns, global investors are adopting a “**barbell strategy**”, balancing between low-risk sovereign debt and high-yield emerging market opportunities.

- **Currency Concerns:**

- Fluctuations in the **rupee-dollar exchange rate** and rising **U.S. Treasury yields** have affected the relative attractiveness of Indian bonds.

The Domestic Context: India's Macro Strengths

- Despite subdued inflows, India remains a **bright spot among emerging markets**, thanks to:
 - **Stable inflation** near RBI's target of 4-5%,
 - **Resilient GDP growth** projected at 7% in FY26, and
 - **Strong domestic consumption trends**, evident in record festive season sales.
- These fundamentals continue to **anchor investor confidence**, making Indian debt a long-term opportunity even amid global headwinds.
- Analysts note that as **valuation differentials narrow** between India and other markets, FPIs may re-enter Indian bonds more aggressively, especially if the **U.S. rate cycle peaks** by early 2026.

Importance of Debt Market

- The Indian government's inclusion in **JP Morgan's global bond index** is a historic milestone, symbolising India's integration with global capital markets. A robust inflow into government securities would:
 - **Reduce borrowing costs** for the government,
 - Deepen the **sovereign yield curve**,
 - Improve liquidity in the bond market, and
 - Support the **Rupee's external stability**.
- However, sustained inflows depend on **policy predictability**, **macro stability**, and **continued reform momentum** in India's financial markets.

Future Outlook

- While 2025's inflows have been below target, analysts remain optimistic about the medium-term outlook. Factors that could boost inflows include:
 - **Completion of index inclusion cycles** by global rating agencies like FTSE and Bloomberg,
 - **The potential India-U.S. trade deal** is improving market sentiment, and
 - **Gradual easing of global monetary policy**.
- However, risks remain. A resurgence in global inflation or an unexpected rate hike by the **Federal Reserve** could once again limit the flow of funds into Indian bonds.

Source: **IE**

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