Balance Of Payments Problems Of Developing Countries With Special Reference To India

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ABSTRACT

The main cause of disequilibrium in the balance of payment arises from imbalanceBetween exports and imports of goods and that is deficit or surplus in balance of trade. Balance of payment, genesis problems and solutions (BOP) is a record of all transactions, made between a particularcountry all other countries during a time period BOP compares the difference of the amount of exports and imports including all financial export and imports.

The balance of payment is broadly classified in to two that are can.

- *Current account,*
- *Capital account.*

The balance of payment positions of the country its economic health It records of different type of receipts, against exports of good and services. Imports of goods and services received along with capital transferred to non residents and non-foreigners

1. INTRODUCTION

The balance of payments, also known as balance of international payments and abbreviated BoP, of a country is the record of all economic transactions between the residents of the country and the rest of the world in a particular period (over a quarter of a year or more commonly over a year). These transactions are made by individuals, firms and government bodies. Thus the balance of payments includes all external visible and non-visible transactions of a country. It is an important issue to be studied, especially in international financial management field, for a few reasons.

- First, the balance of payments provides detailed information concerning the demand and supply of a country's currency.

For example:

If the United States imports more than it exports, then this means that the supply of dollars is likely to exceed the demand in the foreign exchanging market, ceteris paribus. One can thus infer that the U.S. dollar would be under pressure to depreciate against other currencies. On the other hand, if the United States exports more than it imports, then the dollar would be likely to appreciate

- Second, a country's balance-of-payment data may signal its potential as a business partner for the rest of the world. If a country is grappling with a major balance-of-payment difficulty, it may not be able to expand imports from the outside world. Instead, the country may be tempted to impose measures to restrict imports and discourage capital outflows in order to improve the balance-of-payment situation. On the other hand, a country experiencing a significant balance-of payment surplus would be more likely to expand imports, offering marketing opportunities for foreign enterprises, and less likely to impose foreign exchange restrictions.

- Third, balance-of-payments data can be used to evaluate the performance of the country in international economic competition. Suppose a country is experiencing trade deficits year after year. This trade data may then signal that the country's domestic industries lack international competitiveness. To interpret balance-of-payments data properly, it is necessary to understand how the balance of payments account is constructed. These transactions include payments for the country'sexports and imports of good s, services, financialcapital, and financial transfers. It is prepared in a single currency, typically the domestic currency for the country concerned. Sources of funds for a nation, such as exports or the receipts of loans and investments, are recorded as positive or surplus items. Uses of funds, such as for imports or to invest in foreign countries, are recorded as negative or deficit items.

2. COMPONENTS

The current account shows the net amount a country is earning if it is in surplus, or spending if it is in deficit. It is the sum of the balance of trade (net earnings on exports minus payments for imports), factor income (earnings on foreign investments minus payments made to foreign investors) and cash transfers. It is called the current account as it covers transactions in the "here and now" – those that don't give rise to future claims.

The capital account records the net change in ownership of foreign assets. It includes the reserve account (the foreign exchange market operations of a nation's central bank), along with loans and investments between the country and the rest of world (but not the future interest payments and dividends that the loans and investments yield; those are earnings and will be recorded in the current account). If a country purchases more foreign assets for cash than the assets it sells for cash to other countries, the capital account is said to be negative or in deficit.

The term "capital account" is also used in the narrower sense that excludes central bank foreign exchange market operations: Sometimes the reserve account is classified as "below the line" and so not reported as part of the capital account.

Expressed with the broader meaning for the capital account, the Bop identity states that any current account surplus will be balanced by a capital account deficit of equal size – or alternatively a current account deficit will be balanced by a corresponding capital account surplus:

CURRENT ACCOUNT + FINANCIAL ACCOUNT + CAPITAL ACCOUNT + BALANCING ITEMS = 0

The balancing item, which may be positive or negative, is simply an amount that accounts for any statistical errors and assures that the current and capital accounts sum to zero. By the principles of double entry accounting, an entry in the current account gives rise to an entry in the capital account, and in aggregate the two accounts automatically balance. A balance isn't always reflected in reported figures for the current and capital accounts, which might, for example, report a surplus for both accounts, but when this happens it always means something has been missed – most commonly, the operations of the country's central bank – and what has been missed is recorded in the statistical discrepancy term (the balancing item).

- The goods and services account (the overall trade balance)
- The primary income account (factor income such as from loans and investments)
- The secondary income account (transfer payments)

Balance of payments are also known as "balance of international trade"

3. BALANCE OF PAYMENTS PROBLEM IN INDIA

A default on payments, which would have a disastrous consequent for the Indian economy, had become for the first time in our history a serious possibility in June 1991. It was at this time that new Congress Government with Dr. Manmohan Singh as our Finance Minister took several short-term and long-term measures to overcome the balance of payments crisis.

Apart from undertaking various measures of domestic liberalization, he took several for-reaching measures relating to balance of payments problem. Rupee was devalued in July 1991 and later in two years' time; foreign exchange rate of rupee was made market-determined and also convertible into foreign currencies.

Anti-export basis in our economic strategy was removed and accordingly tariffs on imports were reduced, so as to promote competition. In this way costly import-substitution strategy of industrialization was abandoned. These measures bore fruits and India was successful in solving the balance of payments problem. Our exports started growing at a relatively rapid rate than before. Capital flows and remittances by NRIs increased manifold. Of course for a short time, we got special assistance from IMF and World Bank to fulfill our obligations regarding balance of payments.

4. FACTORS AFFECTING BALANCE OF PAYMENTS

- Current account
- A country's current account balance can signification affects its economy therefore it is important to identify the factors the influence it. The most important factors are:
- Inflation
- The country's inflation rate increase relatives that countries with witch it trade. It is current account would be expected to decrease due to highest price at home consumers and corporations with in the countries will most likely purchase more goods. While country's exports to the others countries will decline.
- National income
- If a country's national income rises by a higher percentage than those of other countries its current account is expected to decrease other thing being equal it increased demand for foreign goods.

The Bop has to balance overall, surpluses or deficits on its individual elements can lead to imbalances between countries. In general there is concern over deficits in the current account. Countries with deficits in their current accounts will build up increasing debt or see increased foreign ownership of their assets. The types of deficits that typically raise concern are

- A visible trade deficit where a nation is importing more physical goods than it exports (even if this is balanced by the other components of the current account.)
- An overall current accountdeficit.
- A basic deficit which is the current account plus foreign direct investment (but excluding other elements of the capital account like short terms loans and the reserve account.)

The Washington Consensus period saw a swing of opinion towards the view that there is no need to worry about imbalances. Opinion swung back in the opposite direction in the wake of financial crisis *of* 2007–2009. Mainstream opinion expressed by the leading financial press and economists, international bodies like the IMF – as well as leaders of surplus and deficit countries – has returned to the view that large current account imbalances do matter. Some economists do, however, remain relatively unconcerned about imbalances and there have been assertions, such as by Michael P. Dooley, David Folkerts-Landau and Peter Garber, that nations need to avoid temptation to switch to protectionism as a means to correct imbalances.

Current account surpluses are facing current account deficits of other countries, the indebtedness of which towards abroad therefore increases. According to Balances Mechanics byWolfgangStützel this is described as surplus of expenses over the revenues. Increasing imbalances in foreign trade are critically discussed as a possible cause of the financial crisis since 2007. Many Keynesian economists consider the existing differences between the current accounts in the euro zone to be the root cause of the Euro crisis, for instance HeinerFlassbeck, Paul Krugman or Joseph Stieglitz.

Problems of India's in BOP - 1949-50 to 1999-2000

The disequilibrium in India's BOP has been accounted to both internal as well as external factors. The requirement for development of such a big nation with a large population is one of the main factors resulting in recurring BOP problem. The BOP is always under some pressure and had large deficits due to high level of imports of food grains and capital goods, the profound external borrowings, their payment and poor exports.

After independence, the primary challenge in front of the country was to attain economic growth with social justice. India’s aim after accomplishing independence was to achieve economic self-reliance. For this the country had to strike both the internal as well as the external resources. Not only our technology but our food availability was also on the backward stage. Hefty amounts of food grains had to be imported to supply the demand of such a large population.

5. Balance of Trade and Balance of Payments

Balance of trade and balance of payments are two related terms but they should be carefully distinguished from each other because they do not have exactly the same meaning. Balance of trade refers to the difference in value of imports and exports of goods only, i.e., visible items only. Movement of goods between countries is known as visible trade because the movement is open and can be verified by the customs officials.

During a given period of time, the exports and imports of goods or merchandise may be exactly equal, in which case, the balance of payments of trade is said to be balanced. But this is not necessary, for those who export and import are not necessarily the same persons. If the value of exports exceeds the value of imports, the country is said to experience an export surplus or a favorable balance of trade. If the value of its imports exceeds the value of its exports, the country is said to have-a deficit or an adverse balance of trade.

The terms “favorable” and “unfavorable” are derived from the mercantilist writers of the 18th century. In those days, settlements of the foreign transactions were made in gold. If India had exported Rs. 100 crores worth of goods but had imported Rs.80 crore worth of goods, India would receive Rs. 20 crores worth of gold from the foreign countries. As gold was regarded as wealth and as the receipts of gold made a country wealthy, the mercantilist writers regarded exports surplus as being favorable to the country.

On the other hand, if India had exported Rs. 100 crores worth of goods, but imported Rs. 150 crores worth of goods, it had to pay Rs. 50 crores in gold to the foreigners. India would be losing gold and would be poorer to that extent. Therefore, an import surplus was regarded by the mercantilist writers as adverse balance. But in these days, the international transactions are not settled in terms of gold. Even then, the terms “favorable” and “unfavorable” balance of trades has continued to be used till today.

6. BALANCE OF TRADE IN INDIA

The trade deficit in India widened 25.9% year to & 13 billion in November of 2016. Exports went up 23% to 20% billion and import increased 5.9% to 6.8 billion. Considering April to nor exports were up 0.1% while imports declined 8.4%, narrowing the trade deficit to 6.6% billion.

Calendar	Gmt	Reference	Actual	Previous	Consensus	Forecast
2016-10-14	2:50	Sep	$-8.34B	$ 7.7 B	$-8.34 B	$-6.5 B
2016-11-15	12:50	Oct	$.16B	$-8.34 B		$-B
2017-1-16	12:30	Dec	$13B	$10.16B	$10.16B	
2017-2-15	12:30	Jan		$13 B		
2017-3-15	12:30	Feb				$-8-7B

India trade	Last	previous	Highest	Lowest	Unit
Balance of trade	13008.90	10610	258	20210.90	USD million
Exports	20009.58	23512.00	30514.00	59.01	USD million
Imports	33018.50	33678.50	45281.90	117.40	USD million
Current account	-3400.00	300.00	7360.90	-31857.20	USD million
Current account to GDP	-1.25	-1.31	2.28	-4.82	%
External debt	48400.00	479658.00	480578.78	96392.00	USD million
Terms	57.9	60.2	100.	57.9	Index

of trade	0	0	00	0	points
Capital flows	-17.51	155.56	766.96	-271.46	USD
Foreign direct investment	4612.00	9686.59	5670.00	-60.00	USD
Remittances	75000.00	61500.00	12293.40	5999.10	USD
Tourist arrivals	9942.81	557.56	91300.00	129289.00	USD
Gold reserve	557.77	749.00	557.77	357.75	Tonnes
Crude oil production	736.00	7.75	813.00	526.00	BBL/D/1K
Terrorism index	7.48	53.00	8.09	7.22	BBL/D/1K

7. Determinants of Balance of Payments

- National income at home and abroad,
- Exchange rate of national currency,
- The domestic prices of goods and factors,
- International oil and commodity prices and
- Demand for and supply of foreign currency.

At the back of these variables lie the supply factors, production function, the state of technology, tastes, distribution of income, economic conditions, the state of expectations, etc. If there is a change in any of these variables and there are no appropriate changes in other variables, disequilibrium in balance of payments will occur.

The main cause of disequilibrium in the balance of payments arises from imbalance between exports and imports of goods and services, that is, deficit or surplus in balance of trade. When for one reason or another value of exports of goods and services of a country are smaller than the value of its imports the disequilibrium in balance of payments is likely to occur.

The value of exports may be small due to the lack of exportable surplus which in turn results from the low production of goods to be exported or the exports may be small because of the high cost and prices of exportable goods and severe competition in the world markets.

The important causes of lower exports are inflation or rising prices in the country or over-valued exchange rate. When there is higher rate inflation in a country resulting in higher prices of exportable goods, its exports are discouraged and imports encouraged. If it is not matched by other items in the balance of payments, disequilibrium will occur.

8. DEVELOPMENTS IN INDIA'S BALANCE OF PAYMENTS 2015-2016

- Key feathers of India's bop in Q3 of 2015-2016 India's current account deficit (CAD) at US & 7 lower than US & 7.7 billion (1.5% of GDP of GDP in the preceding quarter.
- The contraction in CAD was primarily on account of a lower trade US & 34.0 billion then the Q3 of last year US $ 37.4 billion in the preceding quarter.

9. CONCLUSION

The balance of payments crisis of 1991 led the policy makers to review the trade strategy and as a result 'outward – oriented strategy' was adopted. The government undertook several

reforms in the – fiscal, financial, industrial and trade sectors. Some of the major achievements of trade sector reforms are:

- Increase in trade openness,
- Satisfactory export performance,
- Maintaining a reasonable level of current account deficit,
- Increase in non – debt creating capital flows like foreign investment,
- Control of inflation,
- Satisfactory industrial and overall Real GDP growth.

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