SJIF Impact Factor (2021): 7.689 |Journal DOI: 10.36713/epra0212 ISSN: 2277–3142
International Journal of Indian Economic Light (JIEL) - Peer-Reviewed Journal
Volume: 10 | Issue: 3 |November 2022

FOREIGN TRADE AND BALANCE OF PAYMENT POSITION OF INDIA

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ABSTRACT

This paper studies the foreign trade and Balance of Payment of India. Balance of payment is an essential measures of the sound the healthy economic conditions of a country. It can be studied with the help of foreign trade. Foreign trade is a trade of economic transactions between two individual countries or more groups of countries during any given period of time. The position of balance of payment of India can be studied under the major components of current account, capital account and official reserve account. This paper attempts the study of the current position of balance of payment of India and also analysis the causes of disequilibrium (deficit) in balance of payment.

KEY WORDS: ***Balance of payment, current account, capital account and factors affecting the deficit balance of payment.***

INTRODUCTION ABOUT THE TOPIC

"Balance of payment is the difference between the visible and invisible goods and services of export and import of a country during a specified period of time". In other words, balance of payment is a statement of a systematic record of all economic transactions between one country and the rest of the world during a year. It shows what is sent to foreign countries by domestic country and what is received from foreign countries. This statement includes all the transactions made by individuals, corporates and the government and helps in monitoring the flow of funds to develop the economy. It means that balance of payment shows the international economic position of India in making decisions of monetary and fiscal policies, foreign trade, foreign exchange and international payments to the government authorities.

REVIEW OF LITERATURE

According to The International Monetary Fund, "Balance of payments is a statistical statement that subsequently summarizes, for a specific time period, the economic transactions of an economy with the rest of the world". In the words of C B Kindle Berger, "The balance of payments of a country is a systematic record of all economic transactions between the residents of the reporting and the residents of the foreign countries during a given period of time".

"Balance of payment is a record of a country's international transactions with the rest of the world". Given by Organization for Economic Co-operation and Development.

OBJECTIVE OF THE STUDY

- To know about the balance of payment position of India.
- To understand the importance of foreign trade and international economic transactions.
- To understand the concept of current account and capital account surpluses and deficits.
- To know about the causes of disequilibrium or deficit balance of payment.
- To understand how balance of payment determines the India's growth and structural changes.

RESEARCH METHODOLOGY

The study is based on the Secondary data. The data was obtained through Journals, reports, publication of professional and research organizations.

Components of Balance of Payment

There are three major components of the balance of payment.

1) Current account
2) Capital account
3) Official reserve account

1) **Current account: - Current** account balance of payments deals with export and imports of goods and services and transfer payments. It consists of three groups.
   a) **Trade account**: - Trade account includes transaction related to export and imports of commodities which is tangible in nature.
   b) **Invisible account: -** This account includes transaction related to export and imports of invisible services like, banking, transportation, shipping, insurance, tourism, software services etc.
   c) **Transfer payments account**: - Transfer payments are unilateral payment made to and received from foreign countries, certain payments are financial aid, grants, remittance of funds, subsidies etc.

   Current account is calculated by adding the balance of merchandise trade, the balance of trade in services, net investment income and unilateral transfers.

Therefore,

Current account = Trade balance+ net Services + net investment income + net transfer

2) **Capital account: -** Capital account deals with payment of debt and claims. It Includes capital transaction such as investment, borrowing and lending of loans, repayment of loans and sale and purchase of assets on both credit and debit side. There are three types of capital account,
   a. **Investment: -** The investment account includes direct investment, such as foreign direct investment, equity capital earning and other deposits of capital flow. And it also includes Portfolio Investment such as foreign institutional investment and offshore funds etc.
   b. **External borrowing: -** In capital account external borrowing like external commercial borrowing and short term debt and loans are included in this account.
   c. **External assistance: -** External assistance likes government aid, intern-government, multilateral and bilateral loans are included in this account.

3) **Official reserve account: -** The official reserve account or official settlement account is, in fact, a part of the capital account. This account measures the change in nations' liquidity and non-liquid liabilities to foreign official holders and the change in a nation's official reserve assets during the year. The official reserve account includes its gold stock, foreign currencies, special drawing rights and net position the IMF. It shows the transactions in a country's net official reserve assets.

Errors and Omission: - It is difficult to record all international transaction accurately. Thus we third element of balance of payment called Errors and Omission which is balancing item so that total credits and debits of the three accounts must equal in accordance with the principles of double entry book-keeping so that the balance of payments of a country always balances in the accounting sense.

Is Balance of payment always in equilibrium?

Balance of payment always balance means that the sum of the net credit and debit balance of current account, capital account and official settlements account must equal to zero.

It can be written as,

$\mathbf{BOP = R_f - P_f}$

BOP = Balance of Payment

R_f = Receipts from foreign country

P_f = Payment to foreign country

When BOP = $R_f - P_f = 0$ is called as **balanced balance of payment**, it implies that when Receipts from foreign country is equal to Payment made to foreign country. It means when visible and invisible goods and services

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of export are equal to import of a country during a year. Which are advantages to maintain each country in their developing path?

When BOP = $R_f - P_f > 0$ is called as **surplus balance of payment**, it implies that when Receipts from foreign country is exceeds Payment made to foreign country. It means when visible and invisible goods and services of export are greater than the import of a country during a year. Which is favorable to the developed and developing country?

When BOP = $R_f - P_f < 0$ is called as **deficit balance of payment**, it implies that when Receipts from foreign country is less than the Payment made to foreign country. It means when visible and invisible goods and services of export are lesser than the import of a country during a year. Which is unfavorable to the developed and developing country. The deficit balance of payment leads to disequilibrium; sometime it leads depression situation of the country.

The Balance of Payment Position of India

Let us analyze the Current account, Capital account and Official Reserve accounts surpluses and deficits balance of payment position of India with the help of following table.

- **Developments in India's Balance of Payments during the Fourth Quarter (January-March) of 2021-22**

Table 1: Major Items of India's Balance of Payments

(US$ Billion)

	January-March 2022 P			January-March 2021			2021-22 P			2020-21		
	Credit	**Debit**	**Net**	**Credit**	**Debit**	**Net**	**Credit**	**Debit**	**Net**	**Credit**	**Debit**	**Net**
A. Current Account	218.8	232.2	-13.4	173.4	181.5	-8.1	798.7	837.4	-38.7	603.5	579.5	24.0
1. Goods	118.0	172.5	-54.5	91.3	133.0	-41.7	429.2	618.6	-189.5	296.3	398.5	-102.2
Of which:												
POL	21.3	49.3	-28.0	8.2	28.7	-20.5	67.5	161.8	-94.3	25.8	82.7	-56.9
2. Services	69.9	41.6	28.3	56.0	32.5	23.5	254.5	147.0	107.5	206.1	117.5	88.6
3. Primary Income	7.2	15.6	-8.4	5.2	13.9	-8.7	25.8	63.0	-37.3	20.8	56.8	-36.0
4. Secondary Income	23.7	2.6	21.2	20.9	2.1	18.9	89.3	8.8	80.5	80.3	6.8	73.6
B. Capital Account and Financial Account	182.1	167.8	14.3	162.7	153.8	8.8	777.4	739.2	38.2	599.0	622.7	-23.7
Of which:												
Change in Reserves [Increase (-)/Decrease (+)]	16.0	0.0	16.0	0.0	3.4	-3.4	16.0	63.5	-47.5	0.0	87.3	-87.3
C. Errors & Omissions (-) (A+B)		0.9	-0.9		0.7	-0.7	0.5		0.5		0.3	-0.3
P: Preliminary.												
Note: Total of sub-components may not tally with aggregate due to rounding off.												

Source: -RBI Publication

This above table clearly explains that, the current year balance of payment position of Fourth Quarter (January-March) of 2021-22

1. There is current account deficit decreased to US$ 13.4 billion in Q4:2021 – 2022 from US$ 22.2 billion in Q3:2021-22. This is mainly on account of moderation in trade deficit and lower net outgo of primary income.
2. The current account balance recorded a deficit of 1.2 per cent of GDP in 2021-22 as against a surplus of 0.9 per cent in 2020-21 as the trade deficit widened to US$ 189.5 billion from US$ 102.2 billion a year ago.
3. Net services receipts increased, both sequentially and on a year on year basis, on the back of a rise in net earnings from computer and business services.
4. Private transfer receipts mainly representing remittances by Indians employed overseas, increased to US$23.7 billion, up by 13.4 % from their level previous year.
5. In the financial account, net foreign direct investment (FDI) at US$ 13.8 billion was higher than US$ 2.7 billion in Q4:2020-21 and net portfolio investment recorded an outflow of US$15.2 billion because of the equity market.
6. External commercial borrowings to India were lower at US$ 3.3 billion in Q4:2021-22. but there was a drawdown of US$ 16.0 billion in the foreign exchange reserves as against an accretion of US$ 3.4 billion in Q4:2020-21

Factor affecting the deficit (disequilibrium) of balance of payment: -

A disequilibrium in the Balance of payment of a country may be either a deficit or a surplus. Surplus is favorable to country; deficit is unfavorable or it will increase the adverse effect on the growing economy like India. There are so many causes of deficit balance of payment, they are discussed below;

1. **Temporary factors:** - Temporary factors are one of the reasons for the deficit balance of payment. These are the short term causes like random variations in trade, seasonal fluctuations, the weather and heavy rainfall on agricultural sector reduces the production activity therefore import excess than the export causes the deficit balance of payment.
2. **Changes in Exchange rate: -** If foreign exchange rate changes due to overvaluation or undervaluation of foreign currency lead to disequilibrium in balance of payment. Sometimes market forces of exchange rate misguide the economic activity which reduces the export of a domestic country
3. **Cyclical fluctuations: -**The cyclical fluctuations like recession and depression in domestic as well as other countries also leads deficit in balance of payment.
4. **Changes in taste and preference and fashion trends: -** When the people of domestic country start adopting foreign country goods it leads excess of import than the export. this is also reason for the deficit balance of payment of a country.
5. **Price effect: -** The inflation or deflation is another cause of deficit balance of payment. If there is inflation in the country increase the price of export, as a result export falls; domestic product demand reduces in foreign market. It leads to decrease in export and increase in import.
6. **Increase in national income: -** If national income of a country increases, it will lead to increase in standard of living and increases the import of foreign goods and services. Therefore, increase in national income indirectly causes the disequilibrium in balance of payment.
7. **Political conditions: -** The Political conditions of the country also plays very important role in determining the export and import of international trade. Ineffective political actions lead to deficit in balance of payment.
8. **Trade barriers**: - The trade barriers like tariffs and quotas will restrict the international transactions of goods and services; this is also one of the causes of deficit in balance of payment.
9. **International Competition**: - There is availability of higher standard of goods at lower prices in international market. It causes deficit in balance of payment and also increases the unhealthy international competition.
10. **Stage of economic development:** - When the country is in developing stage, the country is in need of raw materials, technical knowledge, modern equipment, machinery and other services which promote the development of the country. So the stage of economic development also one of the factors affecting the deficit balances of payment.

CONCLUSION

This paper completely explains the concepts of balance of payment position of India. India is one of the developing economies, where the country needs to concentrate on its growth in international trade. The international trade provides the wide range of opportunities to the India to export its primary goods to other country. But due to scarcity of resources India has to depend on the other country for importing of goods and services. India is the member of various international organizations and also has different agreement on import and export of international trade. The balance of payment explains the complete economic transactions of international trade with the help of current account, capital account and official settlement account.

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