Int. Journal of Management and Development Studies 5(2): 26-32 (2016)
ISSN (Online): 2320-0685. ISSN (Print): 2321-1423
Impact Factor: 0.715

Recent Developments in India's Balance Of Payments: An Analysis

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Abstract: *This article seeks to analyse the recent developments in India's Balance of Payments as well as India's BoP position during the period from. 2008-09 to 2014-15. It also tries to explain the reasons behind such changes in India's BOP. During 2008-09 global financial crisis had put BoP again in stress and stood at US$ -20080 million of deficit, the CAD ratio to GDP was 2.3%. During 2011-12 current account of BOP has started to widen in dangerous level and reached to US $ 78155 million and ratio to the GDP was 4.2%. The India's merchandise trade was also increased, and its share to the GDP reached to 10.3%. Again during 2011-12 and 2012-13 India's BoP position was not favourable due to the dangerous level of increase in CAD and merchandise trade balance, during 2011-12 BoP stood at US $ 78155 million and ratio to the GDP was 4.2, in 2012-13 small surplus of US $ 3826 million was recorded in India's Balance of Payments position but merchandise trade deficit has raised to 10.7% to the GDP. In 2014-15 India's BOP position has been improved compared to the previous year.*

Keywords: India's Balance of Payments (BoP), Current Account Deficit, Capital Account Surplus, Merchandise Trade, and overall Balance of Payments.

Introduction

The position of the balance of payments shows the external strength of a country, it represents the volume of advancement in technological development and competitiveness in the world market and the status of BoP tries to explain the volume of goods and services of a country has been imported and exported along with the performance of borrowing or lending. In the context of Indian economy balance of payments (BoP) is one of the major economic problems faced by the Indian economy. Since independence it has been the chronic and periodic difficulty. At the time of independence India had a current account surplus from 1947 till 1956-57, by the end of the first plan, the Trade deficit was widened to US $ -279 million. From that time onwards, the trade deficit increased from 3.8% of the GDP at market prices to 4.5% of GDP (at Market Prices). This was the first ever BoP crisis India had faced, after independence, crisis of 1966, when India was at war with Pakistan in 1965. The idea of US as well as World Bank was to induce India to adopt a new agricultural policy and devalue the rupee. Thus, the Rupee was devalued by 36.5% in June 1966. The second Oil Shock of 1979 was more severe and the value of the imports of India became almost double between 1978-79 and 1981-82. From 1980 to 1983, there was global recession and India's exports suffered during this time. 1991 crisis was

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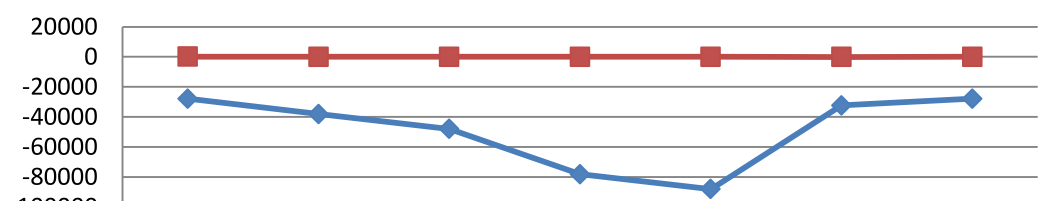
the reason for the worst payments crisis since 1947; it was the worst position of BoP in the history of India's economy. Things became worse by the Gulf war of 1990-91 which was accompanied by double digit inflation. India's credit rating got downgraded; the foreign currency assets had dipped below US$ 1.0 billion, covering barely two weeks of imports. With increasing recourse to the borrowings on commercial terms in the previous years, financing of CAD had also become more sensitive to creditors' confidence in the Indian economy. India had the only option left to fulfil its international commitments was to borrow against the security of India's Gold Reserves. The Indian government's immediate response for this Caretaker government was to secure an emergency loan of US$2.2 billion from the International Monetary Fund (IMF) by pledging 67 tons of India's gold reserves as collateral. 1991 crisis has brought tremendous reforms in economic policy. Hence economy was recovered from the crisis. After the crisis several measures were taken, rupee was once again devaluated, import tariffs were lowered and import restrictions were dismantled, Indian Economy was opened for foreign investments. In 2008 global financial crisis has put BoP again in stress and stood at US$ -20080 million of deficit, Capital Account surplus saw a decline by 92% and the Capital Account Deficit increased by 77% in that year, *the CAD ratio to GDP was 2.3%* of GDP. The current issue of the Balance of Payments of any developing countries including India has become a prominent issue in recent days to discuss across the global level. Hence this paper tries to analyse the recent developments in the India's balance of payments,

Recent Trends in Current Account

The Current Account of a country consists of all transactions relating to trade in goods and services and unilateral (or unrequited) transfers. Services transactions include cost of travel and transportation, insurance, income and payments of foreign investments, etc. Transfer payments related to gifts, foreign aid, pensions, private, remittance, charitable donations, etc. received from foreign individuals and governments to foreigners.

Chart I. Trends in Current Account Defict in (US $ Million)



	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15
Current Account	-27914	-38181	-48053	-78155	-88163	-32397	-27937
CAGR	77.37	36.78	25.86	62.64	12.81	-63.25	-13.77

Source: *Computed from the Data given in Handbook of Statistics on Indian Economy, 2014-15, RBI.*

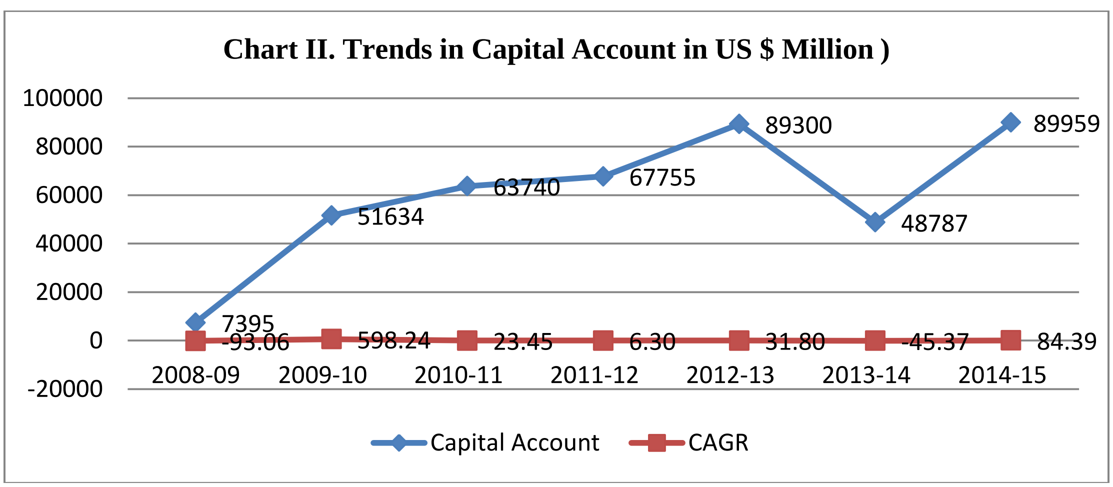
Chart I. reveals that the Current Account of BoP has recorded many fluctuations in recent years, during 2008-09 the current account of BoP was US$ -27914 million, in 2009-10 again India's current account decreased to US$ 38181 million, with the 25.86 % of annual negative growth rate. In 2010-11 again India's CAD continued to decrease and stood to US$ -48053 million. During 2011-12 current account of BoP started to widen in dangerous level and reached to US$ 78155 million and ratio to the GDP was -4.2%, the main factor for such an amount of deficit is increased to US$ 56501.7 million with the 38.97 % of annual negative growth rate which had the share in import bill of 17.7%, and on other hand rising dependence on oil imports and rising demand for petroleum products which raised the import bill by 30% in this year. During 2012-13 Current Account Deficit was staggering at US$ 88163 million which was increased by 12.81%. This is due to the slightly increase in import bill by 0.5%, lower than 30% increase in 2011-12. There was drop in the value of imports of gold and precious stones. On the other hands the export had declined by 1.03%. CAD ratio to the GDP was very high at -4.8 %.

During the 2013-14 India's Current Account Deficit was slightly narrowed compared to the previous year which was decreased to US$ 323997 million with the -63.25% of negative growth rate. This improvement is due to the decline in import value by 7.17%, declined in edible oil by 16.86% declined in gold import to US$ 53819 million (2012-13) to US $ 28892.4 million (2013-14) by 46.32% and on the other hand in this year import and exports were declined by 7.17% and 3.92% respectively.

In 2014-15 Current Account Deficit was narrowed sharply to US $ 279337 million, lesser than 13.77 from last year and placed at 1.3% of GDP significantly lower than the earlier years. The main factors are, fall in international crude oil price translated in to a sizable saving on account of petroleum oil lubricants (POL), increasing in invisible net,

Capital Account

The capital account of a country consists of its transactions in financial assets in the form of short-term and long-term lending and borrowings, and private and official investments. In other words, the capital account shows international flow of loans and investments, and represents changes in the country's foreign assets and liabilities. Long-term capital transactions related to international capital movements with maturity of one year or more include direct investments like building of foreign plant, portfolio investment like the purchase of foreign bonds and stocks, and international loans. A capital account deficit shows that more money is flowing out of the economy along with increase in its ownership of foreign assets and vice-versa in case of surplus.



Source: *Computed from the Data given in Handbook of Statistics on Indian Economy, 2014-15, RBI.*

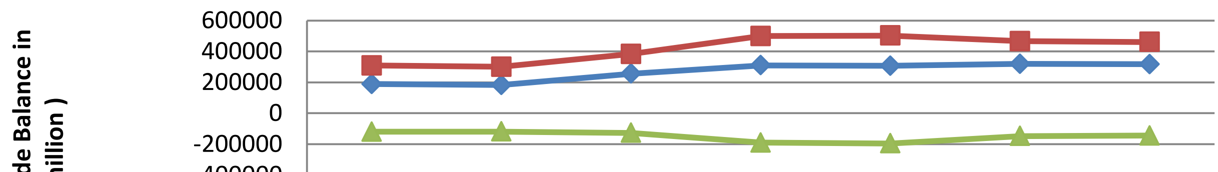
Chart II Reveals the trends of Current Account of BOP. The capital account on the other hand has almost recorded surplus since liberalization, here we can note surplus in Capital Account in all years. In the year 2007-08 the capital account surplus stood high at US$ 106585 million due to the increase in the foreign investment by almost 108%. Lehman crisis worsened the Balance of Payments position in 2008. Even though the currency depreciated by 5.5%, the capital account surplus lowered at US$ 7395 million.

In 2009-10 598.24% of growth was recorded in capital account and stood at US$ 51634 million; foreign investment had increased by 134 %. The NRI inflow was US$ 2924 million. During 2010-11 external assistance have increased with more than 52 % and stood at US$ 4967 million, and commercial borrowings have increased by more than 360 % in this year and stood at US$ 11832 million. During 2011-12 inflow of NRI deposits have increased drastically with more than 268%. It stood at US$ 11918 million, whereas in the previous year NRI inflow was US$ 3238 million. The foreign investments however have declined by 16.8%, but the hike in the inflow of NRI deposits accentuated for the increase in the Capital Account surplus. Further in the year 2012-13, the Capital Account Surplus increased significantly by 40.81% compared to the last year (2011-12). During 2013-14 capital account surplus has declined by 45% and stood to US$ 48787 million. Foreign investments have declined by 34.59%, and commercial borrowings also declined by 6%, NRI inflows were increased by 24.53%, further in 2014-15 capital account surplus again increased to US$ 8959 million appreciated by 84%, foreign investment has increased by 178%, external assistance 57% but the NRI inflows have declined by 63 % compared to the last year.

Balance of Trade

Balance of Trade is simply the difference between the value of exports and value of imports. Thus, the Balance of Trade denotes the differences of imports and exports of a merchandise of a country during the course of year. It indicates the value of exports and imports of the country in question. If the value of its exports over a period exceeds its value of imports, it is called favourable balance of trade and, conversely, if the value of total imports exceeds the total value of exports over a period, it is unfavourable balance of trade. The favorable balance of trade indicates good economic condition of the country.

Chart III. Trends of India's Trade Balance in (US $ Million)



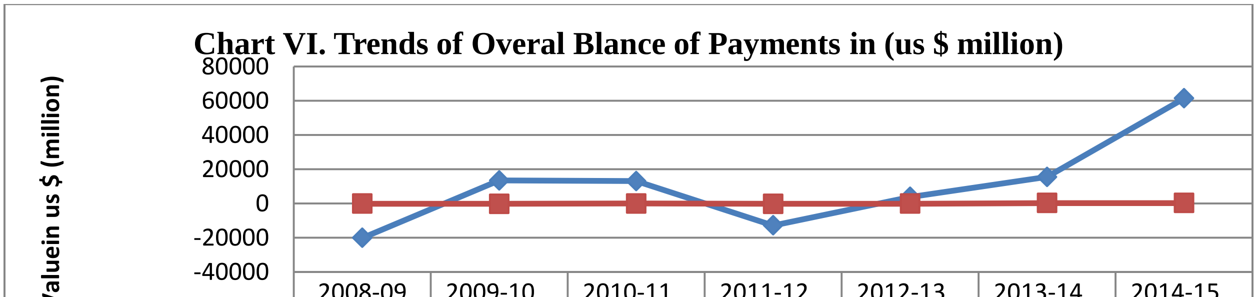
	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15
Merchandise Export	189001	182441	256159	309774	306581	318607	316741
Merchaise Imports	308521	300645	383481	499533	502237	466216	460920
Trade Balance	-119521	-118204	-127322	-189759	-195656	-147609	-144179

Source: *Computed from the Data given in Handbook of Statistics on Indian Economy, 2014-15, RBI.*

Chart III reveals the trends of India’s trade balance, the figures regarding the merchandise exports and imports over the years. As above chart shows, the merchandise exports have been increased in a very slow growth rate and on the other hand, merchandise imports have been increased more than the merchandise exports. For the favourable trade balance of a country, exports should be greater than imports. But in the case of Indian economy, most of the times it is unfavourable which is not a good sign for the growth of economy. During 2008-09 India’s trade balance stood at US$ -119521 million which was more than 30% of the previous year. In this year India’s foreign trade performance was not satisfactory, imports were surged by 19 % over the previous year and on the other hand exports were increased by 13%, it is mainly because of the hike in fertilisers and gold import by 152% and 23.93% respectively and on the other hand petroleum products’ import also raised by 17.61%. Meanwhile the total exports were also raised by 13.74% which is less than the imports. Gems and jewellery export was raised by 42.06%, on other hand agriculture and allied products and, handicraft product exports have been declined by 4.86% and 40.77% respectively. In 2009-10 India’s trade balance slightly declined by -1.1% over previous year. Due to the decline in the fertiliser and petroleum product imports, import value slightly decreased. During 2010-11 Merchandise export was increased by 40% and on the other hand merchandise imports have been increased by 27.55% over the previous year, and trade balance stood at US$ -127322 million with the 7.7% change over the previous year, and trade balance ratio to the GDP was -7.5%. During 2011-12, India’s estimated trade balance stood at US$ -189759 million which was increased by 49% over the previous year, this hike was due to the increase in merchandise imports which was raised by more than 30% over the previous year. In that fertilizer import was increased by 61.98%, edible oil by 47%, petroleum product import by 46.24%, gold import by 38.97%. On the other hand exports were also increased but it was less than the increased imports i.e. 20%; and ratio to the GDP was at -10.5 %. In 2012-13 again Indian balance of trade continued decrease and estimated at US$ 195656 million and ratio to the GDP was -10.7%. During that year India’s export performance was not satisfactory, engineering goods, gems and jewellery, manufacture goods, were declined by 3.62%, 3.20 %, 1.33 % respectively hence total exports were declined by 1.03 %. In 2013-14 trade balance recorded improvement over the last year and estimated at -147609 which was less than 2.32 % over the previous year. Imports have declined by 7.17% which was a positive sign to the foreign trade. Fertilizer import declined by 21.64%, gold by 4.75%. On the other hand exports have increased by 3.92% over the previous year. In 2014-15 also India’s trade balance narrowed and merchandise exports declined by -0.59% and merchandise imports declined by -1.14%. As a result of this, India’s trade balance narrowed by 2.32% and stood at US$ -144179 million. Ratio to the GDP was -7.0%.

Overall Balance of Payments

Since from the Independence of the country has faced series of crises such as rupee devaluation (1966), first (1973) and second (1980) oil shocks and, external payment crisis of 1991. The figures regarding the overall balance of India’s balance of payments over the years are presented in the chart.



	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15
overal BOP	-20080	13441	13050	-12831	3826	15508	61406
CAGR	-121.8	-166.9	-2.9	-198.3	-129.8	305.3	296.0

Source: *Computed from the Data given in Handbook of Statistics on Indian Economy, 2014-15, RBI.*

Above chart no VI describes overall balance of India's balance of payments. India's balance of payments was adversely affected by Lehman crisis of 2008. The Capital Account surplus saw a decline by 92% and the Capital Account Deficit increased by 77% and stood at $ -20080 million in that year. The years 2009-10 and 2010-11 have witnessed surplus in overall balance and stood at US$ 13441 million and US$ 13050 million respectively. Capital account was increase by 558% in 2009-10 and 28% in 2010-11. In 2010-11 exports have been increased by 40% of annual growth in this year, further in 2011-12 India's Balance of Payments position had deficit of US$ 12831 million, raising in petroleum products which raised the import bill by 30% in this year. Further 2012-13 recorded small surplus of US $ 3826 million in the India's balance of payments position. In 2013-14 India's balance of payments position has improved to US$ 51108 million, in this same year CAD has been widened and on the other hand capital account witnessed surplus of US$ 89300 million because of the increase of 40.81% in capital account. Further in the 2014-15 India's balance of payments position has improved and stood to US$ 61406 million, CAD has been narrowed by -13.77% and stood to US$ -27937 million, and on the other hand capital account also witnessed surplus of US$ 89959 million with 84.39% of CARG growth rate; exports are declined by 0.58% whereas imports are also declined by 1.13%; hence India's Trade balance declined to US$ -144179 million by 3.2%, share of overall BOP to GDP was 3.0% which is more than that of the previous year(0.8%).

Concluding Remarks

The New economic Policy aim was to evolve a long term solution to promote price stability to bring about equilibrium in Balance of Payments. But India witnessed quite unfavourable Balance of Payments during its entry into the liberalized trade regime (See Mathew 2013). Since liberalization, the current account is facing deficit more often. On one hand Capital account of the BoP in recorded in surpluses but in same time on other hand current account of the BoP has mounting to the dangerous level. In recent years it has reached to the historical height, during 2011-12 and 2012-13 years ratio to the GDP was 4.2% and 4.8 % respectively. Government has taken many measures in order to control the CAD deficit. Imports tariffs are being imposed for restricting imports, but still India is not able to decrease its import bill considerably. In 2014-15 deficit of trade balance and CAD has improved, over the earlier years, trade balance and CAD of a balance of payments narrowed substantial compare to the 2011-12 and 2012-13 years. But Current Account of the BoP is not favourable to the economy.

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