

Balance of Payment

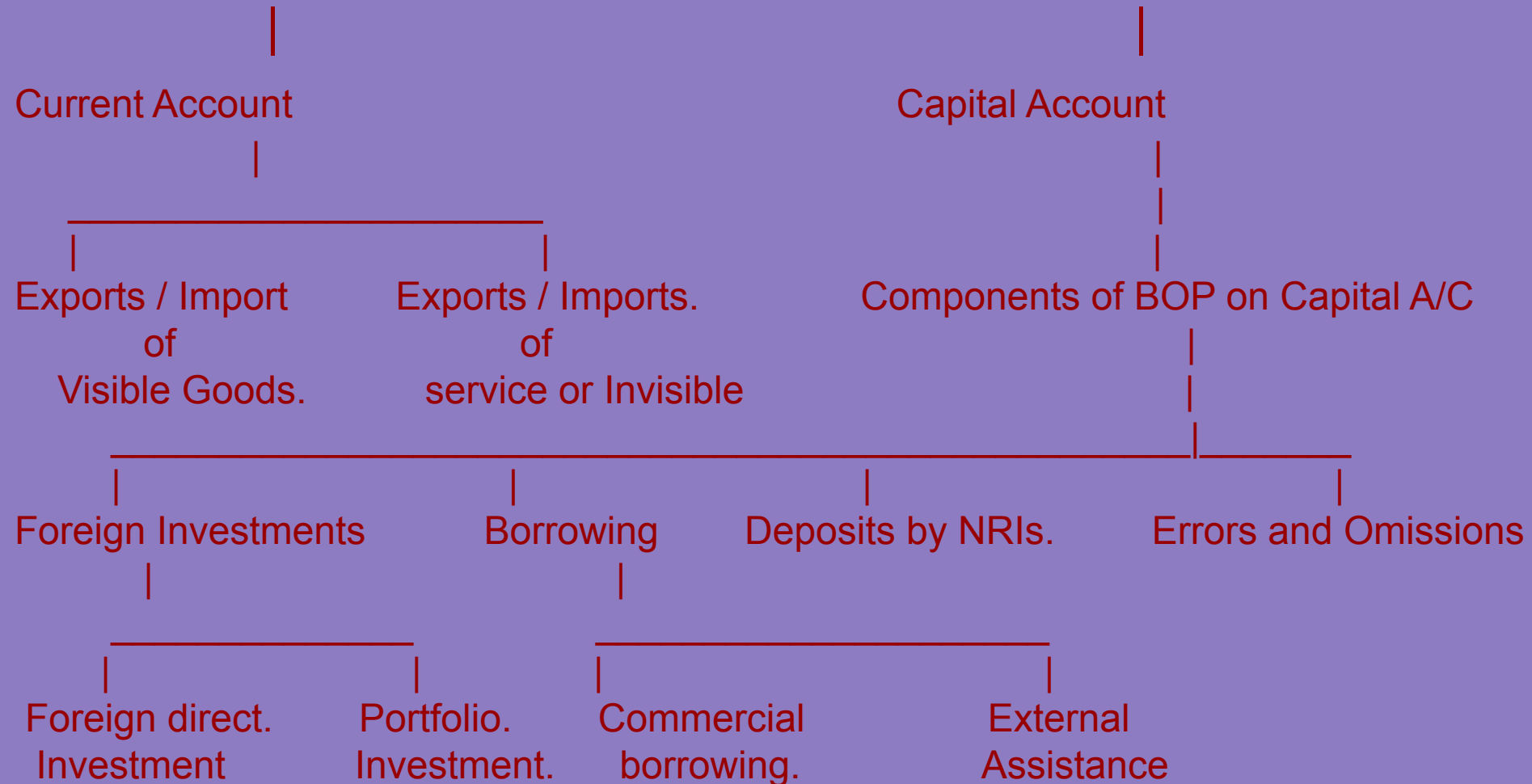
BOP is the systematic record of all economic transaction between the residents of the reporting country and residents of foreign countries during a given period of time. Thus, it is a systematic record of all economic transaction between one country on the one hand and the rest of world on the other, in a given period of time. BOT includes trade of service, invisible, unilateral transfer, capital transactions, payments for service & gold shipment etc.

Balance of payment is a an annual statement of account of monetary transaction of a country vis-a-vis the rest of world. These monetary transaction can be identified as:-

- 1 .Transaction in goods, know as visible trade. It involves ijnflow and outflow of goods among nations;. **Transactions -- GOODS -- SERVICES -- CAPITAL**
- 2 .Transaction in service, also known as invisible items. It involves inflow and outflow of service among nations; and
- 3 . Transaction in capital, like loans, deposits, investments,etc. It involves inflow and outflow of capital among nations.

All these transactions must be either settled in the home currency of the exporting country or in some generally accepted currency like US dollar (USD)

Structure of Balance of Payment



Components of Balance of Payment

Current Account:- The current account records all transactions related to import and export of goods and services and unilateral transfers during a given period of time. The main compartment of this account are:-

1 Export and import of goods -(visible items) -The balance of export and import of goods is called the balance of visible trade. Payment for import of good is written on the negative side and receipt from export is shown on positive side.

2 Export and Import of Services (Invisible Trade) -The balance of exports and imports of services is called the balance invisible trade. Example Shipping, Banking ,Insurance etc. Payments for these services are written on the negative side and receipt on positive side

3 Unilateral Transfer To And Fro Abroad - Unilateral transfers is received which residents of a country make without getting anything in returns. eg. Gifts, Donation Personal remittance etc.

4 Income Receipts And Payment To And Fro Abroad - It includes income in the form of interest,rent and profits.

The net balance of visible trade, invisible trade and of unilateral transfers is the balance on current account . Current Account shows the net income.

There may be following three possibilities in relation to the current account balance:-

1. Current account balance may be in surplus (CAS): if total value of exports of goods and services is greater than the total value of imports of goods and services ($V_x > V_m$)

$$CAS = V_x - V_m \text{ (positive)}$$

2. Current account balance may be in deficit (CAD): If total value of exports of goods and services is less than the total value of imports of goods and services ($V_x < V_m$)

$$CAD = V_x - V_m \text{ (Negative)}$$

3. Current account it may be in balance (CAB): If total value of exports of goods and services is equal to the total value of imports of goods and services. ($V_x = V_m$)

$$CAB = V_x - V_m = 0$$

Capital Account:- It records are international transactions that involve a resident of the domestic country changing his assets or liability with a foreign resident . It is concerned with financial transfers ,So it does not have direct effect on income, output and employment of the country.

Various forms of capital account transactions:-

1 Private Transactions:- There are transactions that affect the liabilities and assets of individuals.

2 Official Transactions:- Transactions affecting assets & liabilities by the government and it's agencies.

3 Portfolio Investment(FII):- It is the acquisition of an asset that does not give the purchase control over the asset.

4 Direct Investment (FDI):- It is the act of purchasing an asset and at the same time acquiring control on it.

5 Banking Inflow:- Inflow of hot money seeking the highest rate of return as NRI deposit.

OFFICIAL RESERVE TRANSACTION :- It includes change in countries gold reserves, foreign exchange reserves ,foreign securities and SDRs with IMF.

The net value of the balance of direct & portfolio investment is called the balance on capital account.

Disequilibrium in BOP

Equilibrium----- Receipts. = Expenditures

$$\begin{array}{ccc} & | & | \\ & \text{F.E.} & = & \text{F.E.} \end{array}$$

So net BOP is zero

Disequilibrium.	Deficit.	$R <$	Payment
	Surplus	$R >$	Payment

Causes of Disequilibrium:-

1. Economic factors.

- Huge development. expenditure(India).
- Business Cycle
- High rate of inflation.
- Development of. import substitutes
 - Change on the Cost of structure and training factory technology etc.

2. Political factors.

- political instability. F.E.
- population Politics

3. Social factors

- Change in tastes & Preference
- Cross- borders western dress (USA)