New from invisibles, our receipts from miscellaneous services

New forms of services, like consultancy, have gained in importance. However, all these are clubbed together under the category of “ miscellaneous”. For example, in 2001 -02, out of total receipts of Rs. 169, 841 crore from invisibles, our receipts from miscellaneous services were Rs. 69, 935 crore (or more than 41% of the total).

Regarding the portion of investment income in the category of invisibles, we should note that investment and loan flows (including the reverse flows generated by disinvestments and repayment of loans) they are included in the capital account. However, costs incurred in contracting and procuring these investment and loan flows, repatriated dividends and profits on such investments, and payment of interest on these loans are all included in the current account. The reasoning is that investment and loans flows represent movement of factors of production; as against this, dividends, profits and interest represent earnings of factors of production for the services rendered by them.

Remaining portions of “ invisibles” are self-explanatory. However, a word may be added about the transfer payments. These are unilateral or unrequited payments. Depending upon whether the donor or donee happens to be an official agency or a private entity, transfer payments are further classified as “ official” and “ private”. As in the case of balance of trade (BO T), in visible also need not balance in the accounting sense.

The balance (that is, the excess of payments received over payments made) on invisibles account can be positive (favourable) or negative (unfavourable).

3. Current Account: Addition of trade account and invisibles account yields the Current Account.

It covers a country's sale/purchase transactions in goods and services (including grants) with rest of the world. In an accounting sense, balance on current account can be " neutral" (or zero), a surplus (positive, or favourable), or a deficit (negative, or unfavourable). 4. Capital Account: The main characteristic of this account is that each capital inflow/outflow generates a reverse flow in course of time. Since grants, gifts and charities etc., do not generate reverse flows, they are recorded under " invisibles" of the current account.

Basically, capital account of a country records changes in the assets owned by its residents in foreign countries, and assets owned by foreigners in it, except changes in its official reserves and its net position with IMF. Within the category of " direct investment", transactions in " portfolio" investment represent sale/purchase transactions of existing equity capital. Portfolio investment is mainly undertaken by financial institutions (like mutual funds, pension funds and insurance companies) having funds to invest for varying periods of time. Their decisions are influenced by factors like expected returns and safety of invested funds. The portion of " banking" represents movement of funds on account of banking transactions, including transactions in foreign exchange.

Balance on Capital Account:

It is the excess of credit entries over debit entries in the capital account and is a measure of the net inflow of capital funds.

It is noteworthy that a surplus on capital account of a country may be due to an increase in its external indebtedness, a net sale of assets held abroad by its residents, a net purchase of assets by foreigners held within this country, and so on. 5. Errors and Omissions: This entry balances the sum of credits with the sum of debits in the capital account, and represents the net position of compensatory errors, omissions and inaccuracies. Its sign (- or +) is chosen to ensure an accounting balance between credit and debit entries.

6. Overall Balance: It is the algebraic sum of balance on current account and balance on capital account, and may be termed the overall balance of payments. In case of excess of total payments over total receipts, this overall balance has a negative sign and it is termed deficit, negative or unfavourable balance In contrast, the overall balance is termed surplus, positive or favourable if the total of receipts exceeds the total of payments.

In accounting sense, a surplus BOP only reveals an excess of payments received over payments made. Such an outcome may be due to one or more reasons like an additional inflow of loans, or of FDI or export earnings etc. Therefore, by itself, balance of payments surplus or deficit does not indicate: i. The gain or loss to the economy; or ii.

Its inherent strength or weakness. In a textbook type presentation, the transactions recorded in both current account and capital account are treated as “ autonomous” or induced by market incentives. Viewed this way, an OVERALL BOP surplus is the excess of autonomous credit entries over autonomous debit entries. 7. Monetary Movement:

Autonomous Transactions:

The portions of BOP account described above are collectively termed “ autonomous transactions” on the assumption that they are primarily taken (i) in response to economic incentives and (ii) without reference to their likely impact on BOP position.

Since the overall BOP position is determined by autonomous transactions they are said to be placed “ above the line”.

Accommodating Transactions:

In contrast, the transactions recorded in the portion of Monetary Movement are termed ‘ accommodating transactions’ on the assumption that they do not cause BOP surplus or deficit; they are the result of it. In case of a “ neutral” or “ balanced” BOP, Monetary Movement account will have only blank entries. Transactions entered in Monetary Movement account are not considered in estimating the Overall Balance of Payments and are, therefore, placed “ below the line”. Monetary Movement account is also known as “ Official Settlement Account” or “ Official Reserves Account”. The Monetary Movement account reveals the following: (i) If the overall BOP is positive, where have the excess receipts gone? (ii) If the overall BOP is negative, from where have the excess payments been made? The excess of receipts over payments (or of payments over receipts) give rise to the following two groups of transactions: (a) IMF Transactions: For financing a BOP deficit, a country may “ purchase” SDRs or take a foreign currency loan from the IMF to meet its payment obligations; and in the process it may sell its own currency or add to its other liabilities to the IMF. Similarly, in case of a BOP surplus, it may sell SDRs or other foreign currency to the IMF and " repurchase" its own currency or reduce its other obligations to IMF. The net amount of IMF Transactions equals (Purchases – Repurchases), with a negative sign indicating a reduction in indebtedness to the IMF, and vice versa.

In simple words, it means that the country has used a part of its surplus BOP for repaying a part of its debt to the IMF. (b) Increase (-)/decrease (+) in Reserves: This item represents a net change in the official foreign exchange reserves of the country. Foreign exchange reserves of a country increase if it has a BOP surplus, and they decrease when it has a BOP deficit. Note that since a surplus BOP has a positive sign, therefore, the net of monetary movement will be an equivalent amount with a negative sign.

And similarly, when BOP is a deficit and has a negative sign, the net of monetary movement will an equivalent amount with a positive sign. To repeat, the net amount of monetary movement is equivalent of the net amount of BOP, but with an opposite sign.