

REPORT  
OF  
THE WORKING GROUP  
ON  
BALANCE OF PAYMENTS MANUAL  
FOR INDIA



September 2010  
RESERVE BANK OF INDIA  
MUMBAI



## Letter of Transmittal

September 30, 2010  
Ashwina 08, 1932

Dr. Subir Gokarn  
The Deputy Governor  
Reserve Bank of India  
Mumbai

Dear Dr. Gokarn,

We are glad to submit herewith the Report of the Working Group on Balance of Payments Manual for India. The Report contains two parts. Part I discusses various issues relating to India's Balance of Payments statistics and makes a number of suggestions to improve compilation, coverage and presentation of India's Balance of Payments consistent with international best practices. Part II presents the revised Balance of Payments Manual for India.

Yours sincerely,

(Deepak Mohanty)  
Chairman

(Anil Bisen)  
Member

(D. Sinha)  
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## Acknowledgements

The Balance of Payments Manual for India, a major part of the Report, has been compiled on the basis of the latest IMF's BoP Manual (BPM 6). The Manual for India, therefore, draws heavily from IMF's BPM6 particularly with respect to conceptual issues and framework of balance of payments accounting. The preparation of the new Manual for India has essentially been a collaborative effort of different Departments of Reserve Bank of India namely, Department of Economic and Policy Research (DEPR), Department of Statistics and Information Management (DSIM), and Foreign Exchange Department (FED). The Working Group places on record its appreciation of the contributions made by each of these Departments. The Group appreciates the suggestions and comments received from various Departments /Ministries of the Government of India as well as NASSCOM, which enriched the content of the Report and the Manual.

The Division of International Trade & Finance (DITF), DEPR has worked as the secretariat for the preparation of the Report and the Manual. Shri Rajan Goyal, Director, DITF and Member Secretary supervised the preparation of the Manual and the Report, under the guidance of Shri S.V.S. Dixit, Adviser. The preparation of the draft was undertaken by a team of officers comprising Shri Binod B. Bhoi and Shri Anand Prakash, Assistant Advisers as well as Shri Harendra Kumar Behera, Research Officer at the initial stage.

The Group had the benefit of comments offered by Dr. B.N. Ananthaswamy, Member of Faculty, RBSC Chennai on the initial draft of the Manual and editorial suggestions made by Smt. Gunjeet Kaur, Director, DEPR. Shri A. Karunakaran, Assistant Adviser, Shri Arvind Kumar Jha and Ms. Monika Kathuria, Research Officers, DEPR were also associated with the preparation of the Manual at various stages. The Group acknowledges the contribution made by these officers and expresses its thanks to all those who were directly or indirectly associated with this endeavour.

(Deepak Mohanty)  
Chairman

## List of Acronyms

ADB -	Asian Development Bank
ADRs -	American Depository Receipts
ADs -	Authorised Dealers
BAL -	Banking Assets & Liabilities
BoP -	Balance of Payments
BOPSY-	Balance of Payments Statistics Yearbook
BPM6 -	The sixth edition of the Balance of Payments and International Investment Position Manual
CAAA -	Controller of Aid Accounts and Audit
CAB -	Current Account Balance in the BoP
CIF -	Cost, Insurance and Freight
CPC -	Central Product Classification
CPs -	Commercial Papers
CS-DRMS -	Commonwealth Secretariat Debt Recording and Management System
DAD -	Deposit Accounts Department
DEA -	Department of Economic Affairs
DEIO -	Department of External Investment and Operations
DGCA -	Directorate General of Civil Aviation
DGCI&S -	Directorate General of Commercial Intelligence and Statistics
DSIM -	Department of Statistics and Information Management
DTRs -	Daily Trade Returns
EBOPS -	Extended Balance of Payments Services
ECBs -	External Commercial Borrowings
EDI -	Electronic Data Interchange
EDMU -	External Debt Management Unit
ESOPs -	Employee Stock Options
ETFs -	Exchange Traded Funds
FATS -	Foreign Affiliates Statistics
FCCBs -	Foreign Currency Convertible Bonds
FCEB -	Foreign Currency Exchangeable Bonds
FC-GPR -	Foreign Collaboration General Permission Route
FCNR(B) -	Foreign Currency Non-Resident Accounts (Bank)
FDI -	Foreign Direct Investment
FED -	Foreign Exchange Department
FEDAI -	Foreign Exchange Dealers Association of India
FEMA -	Foreign Exchange Management Act
FETERS -	Foreign Exchange Transactions - Electronic Reporting System
FISIM -	Financial Intermediation Services Indirectly Measured
FOB -	Free On Board
FRNs -	Floating Rate Notes
FTP -	Financial Transaction Plan
FTSI -	Foreign Trade Statistics of India
GDP -	Gross Domestic Product
GDRs -	Global Depository Receipts
GNDY -	Gross National Disposable Income
GNIE -	Government Not Included Elsewhere
IBRD -	International Bank for Reconstruction and Development
IDA -	International Development Association

IDBMS -	Integrated Database Management System
IFAD -	International Fund for Agricultural Development
IFC -	International Financial Corporation
IIP -	International Investment Position
IMF -	International Monetary Fund
IMTS -	International Merchandise Trade Statistics
IOC -	Indian Oil Corporation
IPO -	Initial Public Offerings
ITC -	International Trade Classification
ITC-HS -	International Trade Classification Harmonised System
ITES-BPO -	Information Technology Enabled Services - Business Process Outsourcing
JVs -	Joint Ventures
LRN -	Loan Registration Number
MoC -	Ministry of Commerce and Industry
MSFTI -	Monthly Statistics of Foreign Trade of India
MSITS -	United Nations' Manual on Statistics of International Trade in Services
NASSCOM -	National Association of Software and Services Companies
NPNNA -	Net Purchases of Non-Produced Non-Financial Assets
NRD-CSR -	Non-Resident Deposits–Comprehensive Single Returns
NR(E)RA -	Non-Resident (External) Rupee Accounts
NRO -	Non-Resident Ordinary Rupee Account
OECD -	Organisation of Economic Cooperation and Development
ORFS -	Online Returns Filing System
RPA -	Rupee Payment Area
RTP -	Reserve Tranche Position
SDRs -	Special Drawing Rights
SEZs -	Special Economic Zones
SME -	Small and Medium Enterprises
SNA -	System of National Accounts
SWIFT -	Society for Worldwide Interbank Financial Telecommunication
TMG -	Technical Monitoring Group on FDI Statistics 2003
TT -	Telegraphic Transfer
URS -	Unclassified Receipts Survey
WCO -	World Customs Organization
WOS -	Wholly Owned Subsidiaries



## Executive Summary

The Reserve Bank of India (RBI) has been compiling and publishing Balance of Payments (BoP) data for India since 1948. To put together the methodological changes as well as provide general information on concepts, main constituents and sources of data used, India's Balance of Payments Compilation Manual was brought out for the first time by the RBI in 1987 in line with the Fourth Edition of the Balance of Payments Manual of the IMF (BPM4, 1977). Since then, several developments have taken place both globally and domestically. Internationally, for example, the size of financial markets grew manifold witnessing innovations in the creation and packaging of financial instruments; and cross-border capital flows as well as the volume of international trade in services expanded exponentially. IMF came out with two editions of the BoP Manual, viz., the Fifth Edition of the Balance of Payments Manual (BPM5, 1993) and the Sixth Edition of the Balance of Payments Manual (BPM6, 2009), issuing guidelines to capture developments in cross-border transactions appropriately in the BoP statistics.

Domestically, during this period, the economy moved from a restricted regime of external payments to a more liberalised regime with a rise in the volumes of both trade and financial flows across the border. Moreover, the prominence of services in international trade as well as the flow of private transfers gained ground with the growing integration of the Indian economy with the rest of the world. Besides, there have been significant changes in the production processes, corporate structures, methods of financing and sourcing of funds. Against this backdrop, to bring out a comprehensive Balance of Payments Manual documenting current practices, procedures of compilation, presentation, coverage and sources of data for India's balance of payments and assess them in relation to international best practices, a Working Group was constituted, comprising members from the Government of India and concerned departments of the Reserve Bank.

With a view to improving the present compilation procedure as well as presentation of BoP statistics to conform to international best practices, the Group makes the following recommendations:

### ***Goods***

- Buying and selling of goods that do not cross national boundaries and do not undergo significant transformation have to be recorded as goods under “merchanted”.

- Repairs on goods, which have hitherto been recorded under goods, need to be included in services and renamed as “maintenance and repair services *n.i.e.*”
- A new purpose code for manufacturing services on physical inputs owned by others may be introduced to give separate treatment to "goods for processing".
- The data on imports should be presented on FOB basis. Necessary information may be gathered from the Daily Trade Returns (DTR) or through a survey.
- Re-exports may be presented as a supplementary item under exports and therefore, an additional code for re-export may be introduced at the custom's end.
- In view of the persistence of differences in the import figures between the RBI and the DGCI&S, the Group recommends that a reconciliation exercise, on a quarterly basis, between the RBI and the DGCI&S may be initiated.

### ***Services***

- Transportation services should be classified by route (sea, air and others) and by component (passenger, freight and others).
- International passenger survey, which was periodically conducted by the Ministry of Tourism in the past, should be revived. Moreover, it should be explored as to whether the immigration slips filled in by non-residents at the time of leaving the country could provide useful information.
- Regarding disaggregated information on health and education related services, new purpose codes should be introduced under FETERS and the Department of Commerce, Government of India should also follow up with the respective ministries to collect the relevant information.
- The Group recommends a complete switch over to banking channel data reported through FETERS to compile details on software services and use the industry sources (*i.e.*, NASSCOM data) for validation purposes only.
- New purpose codes be introduced to capture various services *viz.*, receipts for the cost of construction of projects executed by Indian companies abroad, pension and standardised guarantee services, “manufacturing services on physical inputs owned by others” and “maintenance and repair services *n.i.e.*” as well as “merchanting services”.
- To capture details on financial services related to derivatives in India's BoP, a separate Committee be set up.
- Invisibles article containing disaggregated information on services should be published on a quarterly basis and the possibility of releasing monthly aggregate data on trade in services should be explored.

### ***Income and Transfers***

- Income and transfers should be classified under the heads of primary income and secondary income.

- Disaggregated details on remittances made by those staying abroad for less than one year and those staying for more than a year, should be captured through the existing periodic survey on "Remittances from Overseas Indians" conducted by RBI.

### ***Capital Account***

- The Group recommends that the capital account in India's current standard presentation of BoP should be bifurcated and presented separately as "capital account" and "financial account". Accordingly, "capital transfers" and "non-produced and non-financial assets", are to be excluded from the current account of India's balance of payments, and include explicitly in the rechristened "capital account".
- An internal Group be set up to address the issue of definition and coverage of foreign direct investment.
- The acquisition of gold by the RBI, if any, from the residents including the Government, should henceforth be shown in the statement that reconciles flow (BoP) and stock (IIP).

### **Other Recommendations**

- A standing committee drawing officers from relevant departments of the RBI, Department of Commerce, DGCI&S, NASSCOM, Software Technology Parks of India (STPI) and other relevant ministries/departments, be constituted to look into various medium- and long-term issues relating to collection of data on trade in services and to examine data requirements for bilateral and multilateral trade negotiations (GATS). The Committee may also explore the possibility of capturing details of "Foreign Affiliates Statistics" (FATS) and Mode 3 transactions (commercial presence which represent domestic operations of foreign affiliates including the subsidiaries of subsidiaries).

### **Scheme of Implementation**

- The BoP data should be presented in the new format and the work to be initiated immediately to gather additional information as recommended in the Report.
- IMF expects its member countries to implement the BPM 6 standards by 2012. The Group is hopeful of meeting the expected time line.

### **BoP Manual**

Given the terms of reference for the Group and deliberations and recommendations of the Group, a detailed "Balance of Payments Manual for India" has been prepared. The Manual, besides discussing the conceptual and methodological issues pertaining to BoP, has made a detailed assessment of the current practices of compilation, data sources and presentation of BoP in India against the backdrop of the significant changes introduced by the IMF's latest Manual (BPM6).

**PART I: INDIA'S BALANCE OF PAYMENTS  
STATISTICS - ISSUES AND  
RECOMMENDATIONS**

## ***Introduction***

I.1 The Reserve Bank of India (RBI) has been compiling and publishing Balance of Payments (BoP) data for India since 1948. The articles on BoP published in the RBI Bulletin from time to time carried the methodological changes introduced over the years in the construction of India's balance of payments. However, a need was felt for bringing out a publication that would put together the methodological changes as well as provide general information on various aspects of BoP such as concepts, main constituents and sources of data used. Accordingly, India's Balance of Payments Compilation Manual was brought out for the first time by the RBI in 1987 in line with the Fourth Edition of the Balance of Payments Manual of the IMF (BPM4, 1977). The Manual provided a conceptual framework and procedures for compilation of India's balance of payments.

I.2 Since the publication of the First BoP Compilation Manual for India in 1987, several developments have taken place both globally and domestically. Internationally, for example, the size of financial markets grew multifold with innovations in the creation and packaging of financial services; this gave birth to a new breed of financial instruments and cross-border capital flows as well as the volume of international trade in services expanded exponentially. To keep in step with the developments in international transactions, the IMF came out with two editions of the BoP Manual, *viz.*, the Fifth Edition of the Balance of Payments Manual (BPM5, 1993) and the Sixth Edition of the Balance of Payments Manual (BPM6, 2009), issuing guidelines to capture the developments in cross border transactions appropriately in the BoP statistics. These Manuals, in essence, endeavoured to further improve the methodology of recording balance of payments transactions as well as to strengthen the theoretical foundations of balance of payments accounting and linkages of external transactions with other macroeconomic statistics. The Manuals also took into account multifaceted developments in globalisation, for example, the formation of currency unions, changes in cross-border production processes, evolving complex international company structures, shifts in the flow of remittances and changing dimensions of the mobility of international labour.

I.3 Domestically, during this period, the economy has moved from a restricted regime of external payments, where many international transactions were regulated, to a more liberalised regime with a rise in the volumes of both trade and financial flows across the border. A discernible compositional shift has occurred over the years in India's BoP not only

in relation to magnitude but also in terms of destinations and sources of India's trade and financial flows. Furthermore, several new financial instruments have been introduced and have gained prominence in both domestic and international transactions. This has resulted in a greater integration of India's trade and financial market with the rest of the world.

I.4 The prominence of services in international trade as well as the flow of private transfers gained ground in the wake of the increasing globalisation of the Indian economy. Significant changes took place in production processes, company structures, methods of financing and sourcing of funds. These developments necessitated a review and revision of compilation methods as well as the coverage and presentation of BoP statistics.

I.5 Reflective of these developments, several changes and improvements in India's BoP compilation and presentation were gradually introduced since the publication of the first BoP Compilation Manual in 1987. For example, retained earnings were estimated and included in the preliminary balance of payments statistics from the beginning of the current decade. Similarly, as software exports gained importance, they have been shown as a separate item under service exports in the standard presentation of India's BoP since 2000-01. Data on suppliers' credit up to 180 days maturity have been estimated and incorporated in the capital account under short-term trade credits since the first quarter of 2004-05. These improvements in the coverage and compilation in balance of payments were discussed in the articles on India's balance of payments published in the RBI Bulletin from time to time. Nevertheless, there is no explicit and comprehensive record of these developments in one place.

I.6 At present, though the methodology, coverage and presentation of India's BoP statistics conform, by and large, to the IMF's BPM5 guidelines, there exist certain differences with respect to definitional issues and formats of presentation. For example, at present India's BoP statistics are presented under the "current account" and "capital account", whereas, as per the guidelines of the IMF, the "capital account" needs to be redefined as "Capital and Financial account" with a clear distinction between capital account transactions (covering only capital transfers and "non-produced and non-financial assets") and financial account transactions (covering transactions related to foreign investments, derivatives and other investments). The BPM6 has further suggested that not only "capital account" and "financial account" be presented separately but also that capital account transactions be recorded on a

gross basis, while financial account transactions (which also include reserve assets) be shown on a net basis.

I.7 At the same time, although significant disaggregation in services transactions has been introduced in line with BPM5 and the Extended Balance of Payments Statistics (EBOPS) as recommended by the IMF, there are still some gaps, especially regarding further disaggregation under certain heads of services such as travel and transportation. Furthermore, the latest manual (BPM6) has made a few additional recommendations in line with best international practices improving the coverage, classification and presentation of BoP statistics.

### ***The Working Group***

II.1 Against this backdrop, a need was felt to bring out a comprehensive Balance of Payments Manual documenting current practices, procedures of compilation, presentation, coverage and sources of data for India's balance of payments and assess them in relation to international best practices. Accordingly, a Working Group was constituted (Attachment I) drawing members from the Ministry of Finance, Government of India, Controller of Aid Accounts and Audit (CAA&A), Directorate General of Commercial Intelligence and Statistics (DGCI&S) and concerned Departments of the Reserve Bank, such as the Department of Economic and Policy Research (DEPR)<sup>1</sup>, Department of Statistics and Information Management (DSIM) and Foreign Exchange Department (FED), which are associated with the BoP statistics.

The Working Group consisted of the following members:

Shri Deepak Mohanty, Executive Director, RBI: Chairman  
Shri Anil Bisen, Adviser, Ministry of Finance, GOI: Member  
Dr. D. Sinha, Director General, DGCI&S: Member\*  
Smt. Dakshita Das, CAA&A, GOI: Member  
Shri Salim Gangadharan, CGM-in-Charge, FED, RBI: Member  
Shri S.V.S. Dixit, Adviser, DEPR, RBI: Member\*  
Shri A. P. Gaur, Adviser, DSIM, RBI: Member\*  
Shri Rajan Goyal, Director, DITF, DEPR, RBI: Member-Secretary\*

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<sup>1</sup> Earlier the Department was known as Department of Economic Analysis and Policy (DEAP).

\* Dr. D. Sinha, Director General, DGCI&S replaced Shri Nilachal Ray, Shri S.V.S. Dixit replaced Dr. R.K. Patnaik and Shri A.P. Gaur replaced Dr. Balwant Singh as members of the Working Group, while Shri Rajan Goyal replaced Dr. Rajiv Ranjan as the Member-Secretary of the Group.

The Division of International Trade and Finance (DITF), DEPR provided secretarial assistance to the Working Group.

## Terms of Reference

II.2 The Terms of Reference of the Committee are as under:

- (i) To review the existing methodology for compilation of Balance of Payments Statistics in India consistent with the guidelines contained in the latest IMF Balance of Payments Manual (BPM6).
- (ii) To prepare a Manual for compilation of the balance of payments statistics for India in line with international best practices.
- (iii) To examine the issue of divergence between the merchandise trade data on customs basis released by the Directorate General of Commercial Intelligence and Statistics (DGCI&S), Ministry of Commerce and Industry, and the banking channel data on payments basis released by the Reserve Bank of India, and suggest measures to reconcile the two.
- (iv) To explore the feasibility of capturing possible international transactions at a disaggregated level that may arise in future as a result of the ongoing liberalisation of financial markets and innovations in financial instruments.

II.3 The Group met twice to deliberate on the means to improve the coverage, classification and presentation of India's BoP data, as well as to guide the work relating to revision of the BoP Manual for India. Besides, an exclusive meeting was held to deliberate on the issues relating to trade in services, which was attended by, in addition to the members, two officials from the Ministry of Commerce, a representative each from the National Association of Software and Services Companies (NASSCOM) and the Ministry of Civil Aviation. The minutes of the meetings are set out in Attachment II.

## The Manual

II.4 Given the above terms of reference, the deliberations and recommendations of the Group are set out in Part I and a detailed "Balance of Payments Manual for India" has been presented in Part II. The Manual, besides discussing the conceptual and methodological issues pertaining to BoP, has made a detailed assessment of the current practices of



compilation, data sources and presentation of BoP in India against the backdrop of the significant changes introduced by the IMF's latest Manual (BPM6). The Manual also incorporates a revised format for standard presentation of BoP in India (Attachment III).

## ***Observations of the Group***

III.1 In light of the current practices of India's BoP compilation discussed in the revised Manual, and to align India's BoP statistics with international best practices, the Group has made several observations and series of specific recommendations which are set out below.

### **Current Account**

III.2 The current account of the BoP includes all the transactions (other than those in financial items) involving exchange of economic value which take place between resident and non-resident entities. The components of the current account also include offsetting entries to current economic values provided or acquired without a *quid pro quo*, e.g., private transfers. Therefore, current account transactions are broadly classified as goods, services, income, and current transfers.

### **Goods**

III.3 The IMF's latest BoP Manual (BPM6) has reclassified merchandise trade transactions into three categories, namely, general merchandise, net export of goods under merchanting and non-monetary gold. As a result, some parts of goods are now re-classified into services (such as goods for processing and repairs on goods) while some parts of services are shifted to goods (such as merchanting, by recording them as a separate item as “net exports of goods under merchanting”). However, India's standard BoP statistics at present only provide consolidated numbers on merchandise trade for both exports and imports without the above sub-heads.

III.4 For the purpose of compilation of BoP, exports are valued on the basis of 'free on board' (FOB), whereas imports are valued on a 'cost, insurance and freight' (CIF) basis. While customs data are the source for exports, the banking channel [Foreign Exchange Transactions Electronic Reporting System (FETERS) reporting] data are the basis for imports, as a few items of imports, such as some parts of defence equipment, do not pass through customs.

III.5 Although the exports data as reported by the customs forms the basis for BoP, they are adjusted to take into account valuation differences. The difference between BoP merchandise exports (the adjusted customs data) and the corresponding export receipts reported by the ADs through the banking channel is treated as “leads and lags in exports” and included in the capital account of BoP under the head “other capital”.

III.6 As regards imports, though they are recorded on the basis of the figures reported by ADs through the banking channel, the reconciliation of imports between the two sets of data sources (DGCI&S and the banking channel) are published along with the standard components of BoP for data validation and to improve the serviceability and usefulness of the data. As per international best practices, merchandise imports should also be presented on an FOB basis.

### *Services*

III.7 Traditionally, a distinction is made between goods and services in the current account of BoP to take into account the differences in the nature of their production and the manner in which they are traded. While in the case of goods, their production and trade are separate processes, the two are closely linked in the case of services. The production process of services itself involves a resident and non-resident with the simultaneous occurrence of production and trade.

III.8 The BPM5 (1993) had introduced considerable disaggregation in the classification of international services transactions. Subsequently, the United Nations’ Manual on Statistics of International Trade in Services (MSITS), 2002 suggested the compilation of an additional set of information compatible with BPM5, known as the Extended Balance of Payments Services (EBOPS) classification of transactions in order to facilitate the evaluation of market access opportunities and measure the extent of opening-up with respect to specific 'services' and 'markets'. EBOPS was recommended by the IMF and thus became an extension of BPM5.

III.9 Subsequently, the BPM6 has further strengthened the classification between goods and services by solely following the principle of change of ownership in the case of goods and time of 'providing' in case of services for recording the respective transactions.

Consequently, the BPM6 classified services under 12 heads as against 11 standard categories under BPM5.

III.10 In line with evolving international best practices, the coverage of services in India's BoP statistics has also been broadened over the years. The disaggregated data on services recommended by BPM5 along the lines of EBOPS have been disseminated in the article published annually in the RBI Bulletin titled "Invisibles in India's Balance of Payment: An Analysis of Trade in Services, Remittances and Income" which are also supplied to the IMF for the Balance of Payments Statistics Yearbook (BOPSY). Data on trade in services for India's BoP statistics are captured through purpose-wise reporting of transactions under FETERS.

III.11 Notwithstanding significant improvement in coverage over the years, the data on India's international trade in services do not fully comply with standard classification recommended under EBOPS. *First*, transportation services are classified by route (*i.e.*, sea, air and others); however, further disaggregation of these in terms of components such as passenger and freight are not available. *Second*, in the case of travel services, FETERS does not provide a detailed purpose-wise classification for the expenditure incurred by foreign travellers in India (travel credits), though detailed purpose-wise details are available on travel debits. As the travel receipts reported by FETERS are incomplete to some extent, they are estimated (only aggregate travel receipts) based on data on tourist arrivals obtained from the Ministry of Tourism, Government of India. Furthermore, the break-up of travel receipts into business and personal is not available. *Third*, the construction receipts (credit) are not adequately captured, as they do not include the cost of construction of projects executed by the Indian companies abroad. *Fourth*, pension services are not covered separately at present in India's BoP. Also financial services do not cover risk assumption services like hedging and other financial derivatives. *Fifth*, under personal, cultural and recreational services, disaggregated data especially on health and education are not available. Sixth, at present no information is available on the two new categories of services, *viz.*, "Manufacturing services on physical inputs owned by others" and "Maintenance and repair services n.i.e".

III.12 Apart from these, "other business services" in India's BoP are not grouped under the recommended heads, namely, "Research and development services", "Professional and management consultancy services", and "Technical, trade-related and other business

services”. Besides, merchanting services are not included under goods as recommended by the BPM6. Similarly, as per the current practice of BoP compilation and presentation in India, “telecommunications, computer and information services” are not presented as a single category as suggested by BPM6. Moreover, “communication services” in India's BoP also include “postal and courier services” which should be included under “transportation services” as per BPM6.

III.13 With regard to compilation of “computer services”, two different data sources are used; NASSCOM for receipts and FETERS for payments.

III.14 While merchandise trade data are available on a monthly basis, similar statistics on trade in services are not available with the same frequency.

### *Income and Transfers*

III.15 While the “goods and services account” shows transactions in items that are outcomes of production activities, the income account shows income receivables and payables in return for providing temporary use of factors of production (*i.e.*, primary income such as investment income and compensation of employees) and redistribution of income through current transfers (*i.e.*, secondary income, such as personal transfers and current external assistance). The BPM6 has thus introduced two accounts, namely, “primary income account” and “secondary income account”.

### *Primary Income*

III.16 The BPM6 has distinguished the following types of primary income: (1) compensation of employees, (2) dividends, (3) reinvested earnings, (4) interest, (5) investment income attributable to policyholders in insurance, standardised guarantees, and pension funds, (6) rent, and (7) taxes and subsidies on products and production. In India, transactions relating to income are in the form of interest, dividend, profit and others for servicing of capital transactions.

## **Secondary Income**

III.17 The secondary income account in BPM6 shows current transfers between residents and non-residents. Current transfers are classified according to the sector of the compiling economy into two main categories: general government (*e.g.*, current international co-operation between different governments, payments of current taxes on income and wealth, social contributions and benefits, *etc.*) and other sectors which include personal transfers (*e.g.*, workers' remittances) and other current transfers (current taxes on income and wealth, benefits payable under social security schemes, non-life insurance premium and claims, *etc.*).

III.18 In India's BoP, at present, transfers (private and official) represent one-sided transactions, *i.e.*, transactions that do not have any *quid pro quo*, such as grants, gifts, and migrants' transfers by way of remittances for family maintenance, repatriation of savings and transfer of financial and real resources linked to change in the resident status of migrants. Thus, for the purpose of BoP compilation, private transfers include (i) remittances for family maintenance, (ii) local withdrawals from Non-Resident Rupee Account [NR(E)RA], (iii) gold and silver brought through passenger baggage, and (iv) personal gifts/ donations to charitable/religious institutions. Official transfer receipts include grants, donations and other assistance received by the government from bilateral and multilateral institutions. Currently, private transfers do not appear to distinguish between remittances made by those staying abroad for less than a year and those staying for more than one year.

## **Capital Account and Financial Account**

III.19 As per international best practices, the capital account covers all transactions between residents and non-residents that involve receipt or payment of capital transfers and acquisition or disposal of non-produced non-financial assets. The financial account covers all transactions associated with changes of ownership in the foreign financial assets and liabilities of an economy. Some of the major components of financial accounts include direct investment, portfolio investment, financial derivatives (other than reserves) and employee stock options, other investment, reserve assets, equity and investment fund shares, debt instruments and other financial assets and liabilities. All changes that do not reflect transactions, such as valuation, reclassification and other adjustments, are excluded from the capital and financial accounts.

III.20 According to BPM6, transactions in financial accounts should be recorded on a net basis (in contrast, the current and capital accounts are recorded on a gross basis). Net recording in the financial account means aggregation, whereby all debit entries of a particular variety of asset or liability are netted against all credit entries in the same asset or liability type. However, changes in financial assets should not be netted against changes in liabilities, with the possible exception of financial derivatives.

III.21 India's standard BoP presentation has only a capital account which is the equivalent of the financial account of the IMF's standard presentation. On the other hand, the capital account of IMF's standard presentation, which includes only capital transfers, is subsumed in the current account under 'transfers' in India's BoP presentation.

III.22 As per current practice, the basic structure of the capital account of India's Balance of Payments (*i.e.*, equivalent to the IMF's financial account) consists of assets and liabilities covering direct investment, portfolio investment, loans, banking capital, NRI deposits, short-term credits and other capital. The data on capital account are compiled on the basis of various returns filed by the entities engaged in capital account transactions mostly through ADs (in a few cases, directly) to the Reserve Bank as and when the transaction takes place.

III.23 The IMF Manual (BPM6) recommends adherence to the 10 per cent threshold limit in equity stake for defining Foreign Direct Investment (FDI). The present definition being used to classify FDI in India is at variance with this definition (to the extent that the threshold limit of 10 per cent is not strictly adhered to).

### **Foreign Exchange Reserves**

III.24 Reserve assets constitute an important component of financial account in the balance of payments statistics and are an essential element in the analysis of the economy's external position. Reserve assets are defined as those external assets that are readily available to and controlled by monetary authorities for meeting balance of payments financing needs, for intervention in exchange markets to affect the exchange rate of the currency, and for other related purposes. Reserve assets comprise monetary gold, SDR holdings, reserve position in

the IMF, foreign exchange assets (currency, deposits, securities, financial derivatives) and other claims (loans and other financial instruments).

III.25 In India, foreign exchange reserves are defined as external assets which are readily available to and controlled by the Reserve Bank for meeting balance of payments financing needs, for intervention in exchange markets to contain the volatility of exchange rate of the Rupee, and for other related purposes. Accordingly, at present, reserves include foreign currency assets of the RBI, gold, SDRs and the Reserve Tranche Position in the IMF, which conforms to international best practices as suggested in the IMF Manual. Movement in reserves is recorded in the balance of payments statistics after excluding changes on account of valuation. Valuation changes arise because foreign currency assets are expressed in US dollar terms and they include the effect of appreciation/depreciation of other major currencies (such as the Euro, Sterling, Yen, *etc.*) held in reserves *vis-à-vis* the US dollar.

III.26 The BPM6 has suggested that gold transactions only with non-resident entities should be captured under the BoP (no transactions should be recorded under BoP if the counterparty is a resident).

### ***Specific Recommendations***

IV.1 In light of the above, the Group makes the following recommendations to improve the present compilation procedure as well as presentation of BoP statistics to conform to international best practices:

#### ***Goods***

*First*, buying and selling of goods that do not cross national boundaries and undergo significant transformation have to be recorded as goods under merchanting. Therefore, the Group recommends that henceforth merchanting transactions be included in merchandise trade in India's BoP. The FETERS purpose code may be suitably revised to capture such transactions. **(Action: DSIM, RBI)**

*Second*, repairs on goods, which have hitherto been recorded under goods, need to be included in services and renamed “maintenance and repair services *n.i.e.*”. As India’s BoP, at

present, does not cover this item, the Group suggests that a new purpose code be introduced under FETERS on both the receipt and payment sides and reclassified as services in the presentation of the BoP. **(Action: DSIM, RBI)**

*Third*, at present, India's merchandise trade data do not give separate treatment to goods for processing. Therefore, it is recommended that a new purpose code for manufacturing services on physical inputs owned by others may be introduced under FETERS and included as a new category of services. **(Action: DSIM, RBI)**

*Fourth*, to present data on imports on an FOB basis (instead of the present practice of reporting imports on a CIF basis), freight and insurance on imports should be segregated. Accordingly, the Group recommends that DGCI&S should estimate freight and insurance by collecting the necessary information either from the Daily Trade Returns (DTR) or through survey on a regular basis. **[Action: DGCI&S, DEPR (RBI)]**

*Fifth*, in order to present the information on re-exports as a supplementary item under exports, the Group recommends that an additional code for re-export may be introduced at the custom's end. The DGCI&S should pursue the issue with the customs authorities. **[Action: DGCI&S, DEPR (RBI)]**

*Sixth*, in view of the persistence of differences in the import figures between the RBI and the DGCI&S, the Group recommends that a reconciliation exercise, on a quarterly basis, between the RBI and the DGCI&S may be initiated. **[Action: DGCI&S, DEPR, (RBI)]**

## **Services**

*First*, transportation services should be classified by route (sea, air and others) and by component (passenger, freight and others). Two separate purpose codes each for passengers and freight under FETERS for all the routes, viz., sea, air and others should be introduced. **(Action: DSIM, RBI)**

*Second*, the Group recommends that the present practice of using estimates for travel receipts should be strengthened further through periodic surveys. Accordingly, the international passenger survey that provides information on the expenditure pattern of foreign tourists in



India, which was periodically conducted by the Ministry of Tourism in the past, should be revived. Moreover, the immigration slips filled in by non-residents at the time of leaving the country could provide useful information. The Department of Commerce, Government of India should coordinate with the Bureau of Immigration and Ministry of Tourism to explore the possibilities as noted in the last meeting held on “Trade in Services” (Minutes enclosed at Attachment II). **(Action: Department of Commerce, GOI)**

*Third*, regarding disaggregated information on health and education related services, new purpose codes should be introduced under FETERS. Recognising the limitations under FETERS, it is recommended that the Department of Commerce, Government of India should follow up with the respective ministries to collect the relevant information.

**[Action: DSIM, (RBI) and Department of Commerce, GOI]**

*Fourth*, the Group recommends a complete switch over to banking channel data reported through FETERS to compile details on software services and use the industry sources (*i.e.*, NASSCOM data) for validation purposes only. **[Action: DSIM (RBI) and DEPR, (RBI)]**

*Fifth*, the Group recommends the introduction of a new purpose code under FETERS to capture receipts for the cost of construction of projects executed by Indian companies abroad.

**(Action: DSIM, RBI)**

*Sixth*, the Group recommends that separate purpose codes for pension and standardised guarantee services should be introduced under FETERS. **(Action: DSIM, RBI)**

*Seventh*, to capture details on financial services related to derivatives in India's BoP, the Group recommends that a separate Committee be set up. **(Action: DEPR, RBI)**

*Eighth*, the Group recommends that “business services” be segregated into the standard categories recommended under BPM6. Moreover, the Group recommends appropriate revision in the FETERS purpose code for merchanting services and its inclusion within the goods account as “net exports under merchanting”. **(Action: DSIM, RBI)**

*Ninth*, the Group recommends that two new purpose codes on both receipts and payment sides should be introduced under FETERS to obtain information on “Manufacturing services on physical inputs owned by others” and “Maintenance and repair services n.i.e”.

**(Action: DSIM, RBI)**

*Tenth*, at present, disaggregated information on services as per EBOPS are published annually in the Invisibles article. The Group recommends that it should be published on a quarterly basis.

**(Action: DEPR, RBI)**

*Eleventh*, the Group recommends that the possibility of releasing monthly aggregate data on trade in services should be explored.

**(Action: DSIM, DEPR, RBI)**

### ***Income and Transfers***

*First*, keeping in view best international practices, the Group recommends that income and transfers should be appropriately classified under the heads of primary income (covering investment income and compensation of employees) and secondary income (which deals with redistribution of income through current transfers, such as personal transfers and current external assistance).

**(Action: DEPR, RBI)**

*Second*, in order to capture disaggregated details on remittances made by those staying abroad for less than one year and those staying for more than a year, it is recommended that such information be collected through the existing periodic survey on "Remittances from Overseas Indians".

**(Action: DEPR, RBI)**

### ***Capital Account***

*First*, the Group recommends that the capital account in India's current standard presentation of BoP should be bifurcated and presented separately as "capital account" and "financial account".

**(Action: DEPR, RBI)**

*Second*, the Group recommends identifying and excluding "capital transfers" and "non-produced and non-financial assets", as defined in the Manual, from the current account of India's balance of payments, and including them explicitly in the rechristened "capital account".

**(Action: DEPR, RBI)**

*Third*, regarding the definition of FDI, the Group recommends that an internal Group be set up that draws members from DEPR, FED and DSIM to address the issue of definition and coverage of foreign direct investment.

**(Action: DEPR, RBI)**

*Fourth*, the acquisition (monetisation) of gold from residents (including the government) by the RBI, if any, need not be shown henceforth in the BoP. Instead, these transactions may be shown in the statement that reconciles flow (BoP) and stock (IIP). **(Action: DEPR, RBI)**

### ***Other Recommendations***

V.1 A Standing Committee drawing officers from relevant departments of the RBI, Department of Commerce, DGCI&S, NASSCOM, Software Technology Parks of India (STPI) and other relevant ministries/departments, may be constituted to look into various medium- and long-term issues relating to collection of data on trade in services and to examine data requirements for bilateral and multilateral trade negotiations (GATS). The Committee may explore the possibility of capturing details of “Foreign Affiliates Statistics” (FATS) and Mode 3 transactions (commercial presence which represent domestic operations of foreign affiliates including the subsidiaries of subsidiaries). **(Action: DEPR, RBI)**

### ***Scheme of Implementation***

VI.1 The IMF has just released the latest version of the BoP Manual (BPM6) and the accompanying compilation Guide is expected shortly. The IMF expects its member countries to implement the BPM6 standards by 2012. Against this background, it is recommended that the hand-posts for implementation of the recommendations contained in this Report should be as follows:

First, the revised format should be adopted as recommended in the Report by recasting the available information in the new format to begin with.

Second, to capture the additional information as recommended in the Report, the work relating to the revision of the code box (FETERS) should be taken up with immediate effect by the internal Group comprising officers of DEPR, DSIM and FED. It is recognised in this context that the preparation of a new code box, modification of the software package and training of the Authorised Dealers would take a relatively long time if past experience is any indication. Nevertheless, the Group is hopeful that the time-line prescribed by the IMF for adopting BPM6 standards would be met.

**Part II: BALANCE OF PAYMENTS  
MANUAL FOR INDIA**

September 2010

**RESERVE BANK OF INDIA**

**MUMBAI**

## Chapter I: Concepts and Definitions<sup>2</sup>

1.1. The sixth edition of the *Balance of Payments and International Investment Position Manual* (BPM6) of the International Monetary Fund (IMF) defines the Balance of Payments (BoP) as a statistical statement that summarises economic transactions between residents and non-residents during a specific time period. The BoP, thus, includes all transactions showing: (a) transactions in goods, services and income between an economy and the rest of the world, (b) changes of ownership and other changes in that economy's monetary gold, special drawing rights (SDRs), and financial claims on and liabilities to the rest of the world, and (c) unrequited transfers. These transactions are categorised into (i) the "current account" including "goods and services", the "primary income", and the "secondary income", (ii) the "capital account", and (iii) the "financial account".

### **Concept of Residence**

1.2. The concept of "residence" is central to BoP compilation as it is a statistical statement showing all economic transactions between residents of one economy and those of the rest of the world (non-residents). In compiling BoP, it is, therefore, necessary to determine the economic entities which are residents of an economy and those which are non-residents. For this purpose, the IMF Manual has prescribed certain criteria. Besides, some conventions have also evolved over the years.

1.3. In BoP, the concept of residence is not based on nationality or legal status, but is based on the transactor's centre of economic interest. Therefore, it is necessary to recognise the economic territory of a country as the relevant geographical area to which the concept of residence is applied. The concept of economic territory is defined as the area under the effective economic control of a single government and, therefore, has both the dimensions of legal jurisdiction as well as physical location, which decides the association of entities with a particular economic territory.

1.4. According to the BPM6, "an institutional unit is resident in an economic territory when there exists, within the economic territory, some location, dwelling, place of production, or other premises on which or from which the unit engages and intends to

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\* This section comprises for the most part extracts from BPM5 and BPM6 published by the IMF.

continue engaging, either indefinitely or over a finite but long period of time, in economic activities and transactions on a significant scale”. Actual or intended location for one year or more is used as an operational criterion for the purpose of determining residence. Based on the above definition, each institutional unit is a resident of one and only one economic territory determined by its centre of predominant economic interest.

## Households

1.5. The residence of an individual is determined by that of the household of which he is a part and not by the place of his work. His status of residence continues till he acquires a centre of predominant economic interest abroad. Normally, the predominant economic interest and, therefore, the status of residence is said to have been acquired by staying or intending to do so for one year or more in a territory. Students going abroad for full-time study (even for more than one year) and patients going abroad for medical treatment even for a longer time generally continue to be the residents of their home country. Similarly, crew of ships and aircrafts, oil rigs, space stations, or other similar equipment that operate outside a territory or across several territories are treated as residents in their home base territory. National diplomats, peacekeeping and military personnel, and other civil servants employed abroad in government enclaves, as well as members of their households are considered to be residents of the economic territory of the employing government. Similarly, the staff of international organisations are residents of their home country and not of the economy in which they physically reside. Locally recruited staff of foreign embassies, consulates, military bases, *etc.* are, however, treated as residents of the compiling economy. In the case of border workers, seasonal workers, and other short-term workers, the residence of the persons concerned is based on the “principal dwelling” rather than the territory of employment.

## Enterprises

1.6. In contrast to individuals and households, where there is the possibility of inclusion in two or more economies when they change their residence, enterprises are almost always connected to a single economy. As a general principle, an enterprise is resident in an economic territory where the enterprise is engaged in a significant amount of production of goods and/or services. An enterprise is defined as an “institutional unit” engaged in

production, which may be a corporation or quasi-corporation, a non-profit institution, or an unincorporated enterprise (part of the household sector).

1.7. Corporations and non-profit institutions are normally expected to have a centre of economic interest in the economy in which they are legally constituted and registered. Corporations may be resident in economies which are different from those to which their shareholders belong. Similarly, subsidiaries may be resident in economies which are different from that where their parent corporations are located. When a corporation or an unincorporated enterprise maintains a branch, office or production site in another territory in order to engage in a significant amount of production over a long period of time (usually one year or more) but without creating a corporation for the purpose, the branch, office or site is considered to be a quasi-corporation (that is, a separate institutional unit) resident in the territory in which it is located.

1.8. In the case of an enterprise using its location as a base to deliver services to other locations, the residence of the enterprise is determined from its place of operations, rather than the point of delivery or location of mobile equipment, unless the activities at the point of delivery are sufficiently large to relate to a branch. This mode is used for transport (like operation of ships) and delivery of some services like on-site repairs, short-term construction, and other business services. For entities, such as special purpose entities, irrespective of the location, the residence is determined by their place of incorporation.

1.9. When a non-resident has ownership of land and buildings, and natural resources other than land, the assets are deemed to be owned by a notional resident institutional unit in the economy of location, even if he does not engage in other economic activities or transactions in the economy. All buildings, land and other natural resources are, therefore, owned by residents.

### ***Nature of Transactions***

1.10. Transactions affecting international flows can be recorded in the “BoP” accounts, while changes in external financial assets and liabilities are recorded in the account of International Investment Position (IIP). A transaction is an interaction between two persons (residing in different economies) or institutional units (located in different economies) that

occurs by mutual agreement or through the operation of the law and involves an exchange of value or a transfer. In BoP parlance, there is a subtle difference between “exchange” and “transfer”. An “exchange” involves providing something having economic value (for example, goods, services, income, or a financial asset) in return for a corresponding item of economic value, while “transfers” do not require such corresponding return of an item of economic value. In other words, an “exchange” is called a transaction involving “something for something in return” or a transaction with a *quid pro quo*, whereas a “transfer” is called a transaction involving “something for nothing in return” or a transaction without a *quid pro quo*. Taxes, debt forgiveness, grants and personal transfers are examples of transfers.

1.11. Transactions recorded in the BoP are economic interactions between a resident and a non-resident. Owing to the nature of international accounts, intra-unit transactions are not recorded. The flows between the branch and its parent enterprise are shown as interactions between institutional units, since a branch is recognised as a separate institutional unit (a quasi-corporation). Similarly, when a notional enterprise (a quasi-corporation) is created for holding land and associated buildings by non-resident owners, the flows between the non-resident owners and the notional enterprise are considered interactions between institutional units and are, therefore, captured in the BoP. Any transactions between two resident institutional units in external assets are treated as domestic transactions and are not recorded in the BoP. Similarly, when financial instruments issued by residents are exchanged between non-residents, no transactions, other things being the same, are recorded in the BoP as there is no change in overall external liabilities.

1.12. Some transactions are governed by mutual agreements involving three parties. For example, guarantees involve the guarantor, the debtor, and the creditor. Transactions occurring between any two parties (for example, between the guarantor and debtor, or between the guarantor and creditor, or between the debtor and creditor) should always be identified. For one-off guarantees, the activation of the guarantee gives rise to transactions and/or other flows between each of the three pairs of the three parties. For each pair of parties, transactions in the international accounts are recorded if one party is a resident and the other party is a non-resident.

1.13. Service activities may consist of one unit (an agent) arranging for a transaction to be carried out between two other units in return for a fee from one or both parties to the



transaction. In such a case, the transaction is recorded exclusively in the accounts of the two parties engaging in the transaction and not in the accounts of the agent facilitating the transaction.

## ***Accounting System***

### **Double-entry book-keeping**

1.14. The basic principle involved in compilation of the BoP is the use of the internationally accepted convention of double-entry recording system. The accounting system followed for recording international transactions is guided by three broad book-keeping principles: (i) vertical double-entry book-keeping, also simply known as double-entry book-keeping involving corresponding entries (credit/debit); (ii) horizontal double-entry book-keeping ensuring the consistency of recording for each transaction category by counterparties; and (iii) quadruple-entry book-keeping involving the simultaneous application of both vertical and horizontal book-keeping, which is the accounting system underlying the recording of transactions in the national and international accounts.

1.15. An economy's international accounts are required to be compiled on a vertical double-entry book-keeping basis from the perspective of the residents of that economy. In principle, each transaction in the BoP is recorded as consisting of two opposite entries with equal values: one with a credit entry (signifying inflow) and the other with a debit entry (signifying outflow). The accounting characteristics of transactions recorded in the BoP are as follows:

- i. Credit (CR.): exports of goods and services, income receivable, unrequited transfer receipts, reduction in foreign assets, or increase in foreign liabilities.
- ii. Debit (DR.): imports of goods and services, income payable, unrequited transfer payments, increase in foreign assets, or reduction in foreign liabilities.

1.16. Illustratively, under assets — real or financial — a positive figure (credit) represents a decrease in assets, and a negative figure (debit) reflects an increase in assets. In contrast, under liabilities, a positive figure (credit) shows an increase in liabilities, and a negative figure (debit) shows a decrease in liabilities. Similarly, in the case of services, a credit entry

is recorded when the services are provided to non-residents and a debit entry reflects receiving services by residents from non-residents.

1.17. In the case of transfers (which are unilateral in nature), no good, service, or financial asset is received in return from the counterpart. Nevertheless, the recording of a transfer gives rise to two entries for each party to the transaction. Unilateral transfers are shown as credits or debits, as the case may be, against the head “transfers”, with a contra entry either under merchandise or financial assets/liabilities or reserves. For example, transfers received in kind (*e.g.*, gold) are recorded as a credit entry under transfers and the offsetting entry will be a debit entry in imports. Similarly, transfers received in ‘cash’ are shown as “credit” against transfers under the current account, and the consequent increase in foreign currency holdings is shown as “debit” under the foreign exchange assets of the banking system.

1.18. Under the system of vertical double-entry book-keeping, the total of all credit entries and that of all debit entries become equal, which ensures consistency of accounts for a single unit. More specifically, as each transaction involves two mutually offsetting entries, the difference between the sum of credit entries and the sum of debit entries is conceptually zero in the BoP statistics. Thus, in principle, the BoP accounts as a whole are in balance. In practice, however, the accounts frequently do not balance. For example, the data for BoP are often drawn independently from different sources; as a result, there may be a summary net credit or net debit (*i.e.*, net errors and omissions in the accounts). Net errors and omissions are derived by subtracting the sum of “net balance in the current account” together with “net balance in the capital account” from “net borrowing/lending in the financial account” (which includes reserve assets). Errors and omissions with a negative sign indicate either understatement of payments or overstatement of receipts or both. Conversely, positive errors and omissions connote either understatement of receipts or overstatement of payments or both.

### **Basis of Recording**

1.19. In deriving BoP aggregates, the current and capital account transactions are recorded on a gross basis (*i.e.*, showing full values) as credit and debit entries. In general, gross transactions recorded in the current account often indicate the relative importance of particular item within an economy. Recording the transactions on a gross basis also helps in measuring their global share. On the other hand, the components of the financial account are

recorded on a net basis (*i.e.*, as net changes, which are increases less reductions in the same type of transactions) separately for each category/instrument of assets and liabilities on the same side of the balance sheet, partly because gross data for transactions often are not available. Therefore, a positive change indicates a decrease in assets or an increase in liabilities (credit entry) and a negative change indicates an increase in assets or a decrease in liabilities (debit entry).

## Valuation

1.20. The BPM6 strengthens the basic principles followed by BPM5 in establishing a clear linkage between flows (transactions) and the stock of external financial assets and liabilities, by making a clear distinction between transactions and other changes in the accounts arising out of valuation and other adjustments. For this purpose, a uniform system of valuation of transactions in real resources and financial assets and liabilities and the stocks of assets and liabilities, becomes necessary. Therefore, it is suggested that market prices be used as the basis for valuation of both flows and stocks for compiling BoP and the International Investment Position (IIP) to ensure consistency. This would also ensure international comparability. Apart from linking flows and stocks, the role of valuation is important from the perspective of ensuring internal consistency under the double-entry recording system of BoP. Unless debit and credit entries for various transactions are valued at the same market price, the sum of all debit and credit entries in the BoP statement will not be equal and, therefore, will result in errors and omissions. Uniform valuation has to be followed, particularly because the credit and debit aspects are often derived independently from separate sources. Second, in the absence of a uniform valuation system, different items within the BoP cannot be compared with each other.

1.21. In addition, BoP statements of different countries will not be comparable, unless the two partner countries adopt uniform valuation principles for recording entries in their respective BoP statistics. Ideally, the price at which the transaction is put through should be considered for valuation. For BoP purposes, the BPM6 defines market prices for transactions as “the amounts of money that willing buyers pay to acquire something from willing sellers; when the exchanges are made between independent parties and on the basis of commercial considerations only”. Thus, a market price refers only to the price for one specific transaction. A market price defined in this way is to be clearly distinguished from a price

quoted in the market, a world market price, a going price, a fair market price, or any price that is intended to express the generality of prices for a class of supposedly identical exchanges rather than a price actually applying to a specific exchange.

1.22. In the case of merchandise trade, market price is the price payable by the buyer after taking into account any rebates, refunds, adjustments, *etc.* from the seller. Imports and exports of general merchandise are recorded at free on board (FOB) values, which take into account any export taxes payable or any tax rebates receivable. However, transactions in financial assets and liabilities should be recorded exclusive of any commissions, fees, and taxes whether charged explicitly, included in the purchaser's price, or deducted from the seller's proceeds, and such charges should be shown separately under the appropriate categories. This is because both debtors and creditors should record the same amount for the transaction in the same financial instrument.

1.23. In recording certain transactions, the conditions needed to establish a market price as defined in the IMF Manual may not be present, such as barter transactions, provision of goods and services without a charge, and goods under financial lease. In such cases, the BPM6 recommends that valuation based on market-price-equivalents be worked out as these provide an approximation for market prices. Therefore, market prices of the same or similar items, when such prices are quoted in the market, will provide a good proxy. In some other cases, actual exchange values may not represent market prices, such as transactions involving transfer pricing between affiliated enterprises, manipulative agreement with third parties and certain non-commercial transactions, including concessional interest. In the case of affiliated enterprises, the exchange of goods does not occur between independent parties (for example, specialised components that are usable only when incorporated in a finished product) and, therefore, prices may be under- or over-invoiced, necessitating adjustments to arrive at the market equivalent price (with corresponding adjustments shown in the counterpart accounts). Similarly, the exchange of services, such as management services and technical know-how, may have no near equivalents in the types of transactions in services that usually take place between independent parties. Thus, for valuing transactions between affiliated parties, one may have no choice other than to accept valuations based on explicit costs incurred in production or any other values assigned by the enterprise.

1.24. Another dimension to the valuation issue is that the values of real resources and financial items are constantly subject to changes because (i) of alteration in terms of the currency in which the price is quoted, and/or (ii) the exchange rate for the currency in which the price is expressed may change in relation to the unit of account that is being used. In principle, amounts denominated in foreign currencies are to be converted into domestic currency at market rates of exchange prevailing at the time of the transaction. In principle, the actual exchange rates applied for the currency conversion under a particular transaction should be used for the purposes of BoP. However, at times it is not feasible to use the transaction rates. Therefore, average rates for the shortest period are recommended, though daily average exchange rates provide a good approximation. In this context, it may be noted that valuation changes arising due to changes in exchange rates are not included in the BoP, which is a 'flow' concept, but are included in the IIP which represents stock position.

### Timing

1.25. Generally, there are four broad principles to determine the time of recording transactions, namely: the accrual basis, the due-for-payment basis, the commitment basis, and the cash basis. Since BoP is compiled on an accrual basis, the accrual accounting principle governs the time of recording for all transactions. Under accrual accounting, flows are recorded at the time when economic value is created, transformed, exchanged, transferred, or extinguished. Accordingly, a change of economic ownership is recorded when ownership changes, and services are recorded when they are provided. The change of economic ownership is central in determining the time of recording for transactions in goods, non-produced non-financial assets, and financial assets on an accrual basis. When a change in economic ownership is not obvious, the change is considered to have occurred at (or is proxied by) the time when the parties to the transaction record it in their books or accounts. When services are provided within a discrete period (*e.g.*, transport or hotel services), there is no problem in determining the timing of recording. However, when services are provided on a continuous basis over a period of time (*e.g.*, construction services, operating-leasing and insurance services), there may be advance payments or settlements at later dates (freight, insurance, port services, *etc.*). In such cases, the provision of services should be recorded on an accrual basis in each accounting period, *i.e.*, they should be recorded as they are rendered and not when payments are made.

1.26. Distributive transactions (compensation of employees, social contributions, and interest and dividend payments) are recorded at the moment when the related claims arise, *i.e.*, when the amounts payable accrue. For grants and other voluntary transfers, the time of recording is determined by the time at which there is a change in the economic ownership of the resources that corresponds to such transfers.

1.27. While the concept of change in economic ownership is generally the basis for time of recording the transactions in financial assets/liabilities, there are certain financial claims/liabilities (*e.g.*, trade credit) which result from non-financial transactions. In such cases, the financial claim is deemed to arise (*i.e.*, the time of recording) at the time when the corresponding non-financial transaction occurs.

### **Timing Adjustments**

1.28. Timing adjustments may be necessary particularly in the case of merchandise trade as the latter may not always reflect changes in economic ownership due to a time lag in the physical movement of goods. Sometimes, the practices followed in customs statistics also may lead to distortions requiring timing adjustments. When the process of importing or exporting involves a lengthy voyage, a change in the economic ownership of goods can vary widely from the time when the goods are recorded in trade statistics. In such cases timing adjustments should, in principle, be applied to correct the trade statistics.

1.29. In brief, the timing of certain transactions in goods, services, and income may not coincide with the corresponding payments for settling the transactions due to differences in procedure followed for recording the same (cash and/or accrual basis). Therefore, alternative information should be used routinely to verify and/or adjust selected transaction categories. Therefore, compilers using an exchange record system should check each large settlement transaction. Similarly, data on interest payments obtained from either the payment records or debt service schedule may not be appropriate for accrual accounting. In such cases, other possibilities for deriving interest accruals may be explored, such as using the information contained in the loan agreements.

## ***Applicability of IMF Guidelines***

1.30. The IMF's Balance of Payments Manual provides guidance to its member countries on the compilation of BoP and IIP and also serves as an international standard for the conceptual framework for compiling statistics relating to external transactions. The IMF's Balance of Payments Compilation Guide, which is brought out along with the Manual, provides detailed information on standard concepts, definitions, coverage, classifications and conventions followed in the construction of BoP and IIP statistics to enhance international comparability of data. However, the Manual suggests that the principles and practices of BoP construction at the country level should be based on country-specific circumstances keeping in view the practical and legal constraints for data collection. The Manual provides a general framework that is applicable for all countries ranging from small open economies and least developed economies to the more advanced and complex economies. Therefore, it is recognised that not all items are relevant in all cases.

1.31. It is for the national compilers to apply international guidelines in a way appropriate to their specific circumstances. Factors to be taken into account when determining the items to be collected and the techniques employed include the relative importance of disparate types of economic activities, the diversity of institutions, range of instruments available in financial markets and whether or not exchange controls exist. In addition, data collection for some items of BoP may not be practical if the item is too small and the cost of collecting such data is relatively high. Similarly, some countries may be interested in identifying certain other items of economic transaction outside the general framework of BoP as recommended by the IMF, which are of interest to their policymakers and analysts.

## Chapter II: External Accounts, SNA and their Linkages

2.1. The previous chapter dealt with the concepts, definitions and conventions associated with BoP accounts. It has, *inter alia*, covered concepts of residence, the nature of transactions, double-entry book-keeping, valuation and time of recording. This chapter discusses the triangular inter-relationship between BoP, IIP and the System of National Accounts (SNA). The concepts and coverage of BoP as well as the international investment position are discussed in relation to those under SNA, on the one hand, and the links between different components of external transactions and various segments of the SNA are traced on the other. This chapter also discusses the evolution of international best practices in constructing BoP, as embodied in the various editions of the IMF's Balance of Payments manuals, which have facilitated a systematic integration and proper synchronisation of external accounts with SNA.

2.2. The international accounts for an economy summarise the economic relationships between residents and non-residents. They comprise:

- (i) The IIP, which presents at a point in time (stock) the value of (i) the financial assets of residents which are, in effect, claims on non-residents, (ii) the monetary gold (gold bullion held as reserve assets), and (iii) the liabilities of residents to non-residents reflecting essentially the claims held by non-residents on residents. The difference between the assets and liabilities represents the net position in the IIP, which could either be a net claim on or a net liability to the rest of the world.
- (ii) The BoP which is a summary statement presenting economic transactions between residents and non-residents (flows) during a specific time period; and
- (iii) Other changes in financial assets and liabilities, which sets out other flows, such as valuation changes and acquisition of monetary gold from residents. This statement reconciles the BoP and IIP for a specific period by showing changes due to economic events other than transactions between residents and non-residents.



2.3. While the IIP reflects the stock position of international assets and liabilities of a country at the end of a period, the BoP shows the flows of goods, services, remittances and movement of capital during the reference period. Although, in principle, the sum of “flows” (BoP) over a period should add up to the stock (IIP) at the end of the period, there remain, in practice, some differences between the two mainly arising out of disparate valuation methods and the use of different exchange rates. While stocks (IIP) are valued at end-period exchange rates, flows (BoP) are recorded on the basis of transaction rates or rates which are closer to transaction rates.

### ***International Investment Position***

2.4. The IIP is a subset of the national balance sheet. Apart from the IIP, the national balance sheet incorporates the stock of both non-financial as well as financial assets and liabilities between residents (domestic assets and liabilities). While the simple IIP statement sets out the stock of assets and liabilities of a country at a point in time, the integrated IIP statement has an opening value (as at the beginning of the period) and a closing value (as at the end of the period). Further, the opening and closing values of the IIP are reconciled through the financial account (flows arising from transactions) of the BoP and the “other changes in financial assets and liabilities account” (other volume changes and revaluation). Therefore, the values in the IIP at end-period are essentially made up of transactions and other flows recorded till date.

2.5. The IIP, financial account under BoP, and other changes in assets and liabilities account are constructed on the basis of functional classification, which combine the financial instruments and types of flows. The functional categories are direct investment, portfolio investment, financial derivatives and employee stock options (other than reserves), other investment, and reserve assets. The SNA does not have such categories; rather it records financial account activity by type of instrument only.

### ***Balance of Payments***

2.6. The BoP is a statistical statement that comprises transactions between residents and non-residents during a period. It consists of the goods and services account, the primary income account, the secondary income account, the capital account, and the financial

account. The different accounts within the BoP are distinguished according to the nature of the economic values provided and received, under the double-entry system of accounting in the BoP.

### **Current Account**

2.7. The current account includes flows of goods, services, primary income, and secondary income between residents and non-residents and thus constitutes an important segment of BoP. While the “goods and services account” generally forms a major part of the current account, the primary income account reflects amounts payable and receivable in return for providing temporary use of labour, financial resources, or non-produced non-financial assets (natural resources). The secondary income account shows redistribution of income between resident and non-residents, *i.e.*, when resources for current purposes are provided without economic value being exchanged in return (transfers). The net effect of all the transactions under the above accounts is known as the “current account balance”. In other words, the current account balance shows the difference between the sum of exports of goods and services as well as income receivable, on the one hand, and the sum of imports and income payable on the other. From a macroeconomic perspective, the value of the current account balance reflects the inflow/outflow of foreign resources bridging the savings-investment gap.

### **Capital Account**

2.8. The capital account comprises credit and debit transactions under non-produced non-financial assets and capital transfers between residents and non-residents. Thus, acquisitions and disposals of non-produced non-financial assets, such as land sold to embassies and sales of leases and licences, as well as transfers which are capital in nature, are recorded under this account.

### **Financial Account**

2.9. The financial account reflects net acquisition and disposal of financial assets and liabilities during a period. The transactions under financial account appear both in the BoP and in the integrated IIP statement owing to their effect on the stock of assets and liabilities. The sum total of net transactions under the current and capital account represents net lending (surplus) or net borrowing (deficit) by the economy from the rest of the world, which is

reflected in the financial account as net outflow or inflow of capital. Thus, the financial account shows how the net lending to or borrowing from the rest of the world has occurred. Conversely, it shows how the current account surplus is used or the current account deficit is financed. The financial account together with the “other changes account” explains the change in the IIP between the beginning and end-periods.

2.10. In contrast to the current and capital accounts which show transactions in gross terms, the financial account is recommended to show transactions on a net basis, separately for financial assets as well as liabilities (*i.e.*, net transactions in financial assets show acquisition of assets less disposal of assets and not assets net of liabilities). Incidentally, the transactions relating to merchanting and re-exports under the current account are also recorded on a net basis.

2.11. The capital account and financial account from the BoP statistics, together with “other changes in financial assets and liabilities account”, constitute the accumulation accounts which show acquisition and disposal of assets and liabilities, their financing, and other changes. While the current account is concerned with transactions relating to the current period that affect the current income and pool of goods and services available during the period, the accumulation account deals with the provision and financing of assets and liabilities having implications for future cash flows. The financial account shows the acquisition of financial assets and incurrence of liabilities during the period on a net basis. In contrast, the “other changes in assets and liabilities account” comprises those flows that are not covered under BoP transactions. Thus, the “other changes in financial assets and liabilities account” presents changes in revaluation due to exchange rate changes and changes in the volume of reserve assets arising out of acquisition of monetary gold from residents, which do not figure in the BoP.

### **Net Errors and Omissions**

2.12. While BoP accounts are, in principle, balanced, imbalances may occur in practice on account of imperfect compilation procedures and different data sources. This imbalance, a usual feature of BoP statistics, is termed “net errors and omissions” and is identified explicitly in the BoP statement. Net errors and omissions in simple terms are derived residually as the difference between total of receipts and payments (both current and capital

together with the financial account). Therefore, a positive value of net errors and omissions indicates any or all of the following:

- (i) the credit transactions (current or capital or both) are understated;
- (ii) the debit transactions (current or capital or both) are overstated;
- (iii) the net increase in assets in the financial account is overstated;
- (iv) the net increase in liabilities in the financial account is understated.

In the case of a negative value of net errors and omissions, the opposites of the above would hold.

2.13. The size and trends of net errors and omissions provide useful insights into the accuracy of data sources in terms of coverage and reporting, as well as accounting methods. The number of errors and omissions should not be too large, as this raises questions about the quality and reliability of BoP data. Furthermore, BoP statistics with a high number of errors and omissions may fail to serve as useful input to policy making, since it implies that the values of certain transactions are not appropriately captured and, therefore, they are not representative. A higher order of errors and omissions are also said to be the consequence of flight of capital as they arise essentially due to mis-invoicing of trade transactions. Although there is no rule of thumb for the magnitude of errors and omissions, errors and omissions to the extent of 4 per cent of total trade transactions is considered normal as per the convention (BPM4). However, subsequent editions of IMF's BoP Manuals (BPM5 and BPM6) are silent on such conventions.

### ***Linkages between BoP and IIP***

2.14. Some of the important linkages between these two sets of accounts are:

- i. The end of period values that appear in the IIP are the summation of the values at the beginning of the period in IIP and net transactions put through in assets and liabilities during the period (BoP) together with, *inter alia*, the changes arising out of valuation.
- ii. The balance on the sum of the current and capital accounts is equal to the balance on the financial account with the opposite sign (including errors and omissions). This

balance is called net lending / net borrowing to the rest of the world and influences the IIP.

- iii. Financial assets and liabilities generally give rise to investment income, which should broadly correspond to net interest receipt/payment under BoP. The rate of return could be derived as the ratio of income to the corresponding stock of assets. This may be inclusive of holding gains or losses.

### ***System of National Accounts (SNA)***

2.15. Conceptually, BoP transactions and the corresponding data in the IIP are closely linked to the system of national accounts that provides a broader framework for collection and presentation of the economic statistics of the economy. The SNA is the international standard framework for the accounting of national income, which encompasses transactions, other flows, stocks, and other changes affecting the level of assets and liabilities from one accounting period to another. The SNA covers the transactions between “residents and residents” as well as those between “residents and non-residents”. As such, BoP statistics and IIP data feed into national accounts.

2.16. The SNA is a closed system as both ends of every transaction are recorded. *i.e.*, each transaction is shown as a use for one part of the system and as a resource for another part. Stocks of assets affected by transactions, valuation and other volume changes (such as uncompensated seizures or destruction of assets) are recorded as at the beginning and end of the appropriate periods.

2.17. Under the SNA, economic entities, *viz.*, transactors and holders of stocks are the residents of a particular economy. Uses or resources for non-resident entities are captured through the section known as the “rest of the world account”. The segment for resident entities or sectors consists of accounts for production, income generation, primary and secondary distribution of income, redistribution of income, consumption, and accumulation. Since the system is closed, the rest of the world account is constructed from the perspective of the non-resident (rest of the world) rather than that of the resident (compiling economy). Consequently, entries in the BoP and the IIP are reversed in the presentation of rest of the world accounts in the SNA.

## ***Harmonisation between the SNA and External Accounts***

2.18. The IMF's latest manual (BPM6) is in agreement with the SNA (2008). As the BoP and the IIP are integral parts of the SNA, there is virtually complete concordance—between the Manual and the SNA—on issues such as the defining resident units (producers or consumers), valuation of transactions, the stock of external assets and liabilities, time of recording transactions and stocks, conversion procedures, coverage of international transactions in goods, services, income, capital transfers, and foreign financial assets and liabilities.

2.19. The SNA and the Manual identify resident producers and consumers in no different way. Both employ the concepts of economic territory and the centre of economic interest to identify resident units. In the Manual and the SNA, market price is the primary concept for valuation of “transaction accounts” and “balance sheet accounts”. BoP and national accounts are prepared, in principle, on an accrual basis. The two systems employ essentially identical applications of the accrual basis in specific categories of transactions. Both systems employ consistent procedures for converting transactions denominated in a variety of currencies or units of account into the unit of account (usually the domestic currency) adopted for compiling the BoP statement or the national accounts. There is also consistency between the two systems on conversion procedures used in constructing balance sheet accounts.

2.20. The SNA uses an accounting system which is similar to that of BoP. However, the entries for both parties to a transaction (such as a resident and a non-resident) are included in the SNA, rather than just one party (the resident) as in the BoP. As a result, each transaction gives rise to four entries in the SNA, that is, two entries for each party. Credits in the BoP are called “resources” in the SNA, while debits are called “uses”.

2.21. The SNA and BPM6, in general, follow the same classification system and coverage. The terminologies of major aggregates are fully harmonised between them. However, two systems vary in terms of presentation in that the international accounts use functional categories as the primary level of classification for investment income, the financial account, and the IIP, while the SNA uses instruments and sectors. Apart from functional categories, the details of “instrument and institutional sectors” in the international accounts allow the

data to be converted to or compared with the SNA. Furthermore, there exist differences in classification or level of details between the rest of the world accounts (SNA) and international accounts (BoP). These satisfy varying analytical requirements and the necessity of using, in the SNA, a uniform classification scheme for all sectors of the economy. Because of the use of consistent terminology, the links can be established between the components of international accounts and the corresponding items under SNA.

### ***Treatment of Transactions under Various Accounts***

2.22. The “rest of the world accounts” in the SNA and international accounts (BoP) employ the same terminology, except for some minor differences. The SNA coverage of exports and imports of both goods and services is consistent with BoP coverage of the corresponding items. In BoP statistics, exports and imports of services are further disaggregated to meet the data requirements, particularly for negotiations in international trade in services within the framework of international agreements. The major elements of the capital account of the external accumulation accounts in SNA correspond to the capital account of the BoP. The balancing item of net lending/net borrowing in SNA is, in fact, obtained from the BoP.

2.23. The coverage of the SNA with regard to the financial account is similar to that of the financial account in the BoP, though they may vary in the level of detail. Similarly, the coverage under the external assets and liabilities account of the SNA is identical with that of the IIP. However, in the SNA, financial assets are mainly classified by type of instrument. In the BoP, financial items are classified largely by functional category—direct investment, portfolio investment, financial derivatives (other than reserves), employee stock options, other investment, and reserve assets. In addition to the categories identifying the types of financial instruments, the BoP contains sector-wise break-up (central bank, other deposit-taking corporations, general government, other financial corporations, and other sectors) to provide links with other parts of economic and financial statistics, such as money and banking, government finance, international banking, and external debt.

2.24. The explicit link between BoP items and the items under the national accounts is set out in Table II.1.

**Table II.1: Linkage between Balance of Payments and National Accounts**

<b>National Accounts</b>		<b>Balance of Payments</b>	
<i>Goods and services</i>		<i>Current account</i>	
<b>Gross domestic product (GDP)</b>	<b>1700</b>		
= Government final consumption expenditure (G)	400		
+ Non-government final consumption expenditure (C)	800		
+ Gross capital formation (I)	400	Goods and services	
+ Exports of goods and services (X)	500	Credit (export)	500
- Imports of goods and services (M)	400	Debit (import)	- 400
		<b>Total</b>	<b>100</b>
<i>Current and capital accounts</i>			
<b>GDP</b>	<b>1700</b>	+ Income	
+ Net income from abroad	50	Credit	100
		Debit	-50
		<b>Total</b>	<b>50</b>
+ Net current transfers from abroad	150	+ Current transfers	
		Credit	300
= <b>Gross National Income</b>	<b>1900</b>	Debit	-150
- Final Private consumption expend	1200	<b>Total</b>	<b>150</b>
= <b>Gross Savings</b>	<b>700</b>	= Balance on current account (CAB)	300
+ Net capital transfers received from Abroad	5	<i>Capital account</i>	
		Credit	5
- Net acquisition of non-produced, non-financial assets	-15	Debit	-15
		<b>Total</b>	<b>-10</b>
- Gross capital formation	400	<i>Financial account</i>	
= <b>Net lending (+)/Net borrowing(-)</b>	<b>290</b>	Assets	400
<i>Financial account</i>		Liabilities	110
Net acquisition of financial assets less net incurrence of liabilities	290	<b>Total</b>	<b>290</b>

The linkage between key aggregates of accounts of the total economy and BoP flows can also, by the use of symbols, be summarised algebraically within a savings/investment framework.

- C = private consumption expenditure
- G = government consumption expenditure
- I = gross domestic investment
- S = gross domestic saving
- X = exports of goods and services
- M = imports of goods and services
- NY = net income from abroad



GDP = gross domestic product  
 GNDY = gross national disposable income  
 CAB = current account balance in the BoP  
 NCT = net current transfers  
 NKT = net capital transfers  
 NPNNA = net purchases of non-produced, non-financial assets  
 NFI = net foreign investment or net lending/net borrowing *vis-à-vis* the rest of the world

BoP flows are italicised in the following equations.

$GDP = C + G + I + X - M$  (where  $X - M$  = balance on goods and services in the BoP)

$CAB = X - M + NY + NCT$

$GNDY = C + G + I + CAB$

$GNDY - C - G = S$

$S = I + CAB$

$S - I = CAB$  (*current account balance is the gap between saving and investment*)

$S - I + NKT - NPNNA = CAB + NKT - NPNNA = NFI$

( $NKT - NPNNA$  = balance on the capital account of the BoP)

2.25. In the Indian context, with reference to the BoP and IIP, the BoP compilation is generally in accordance with international best practices. However it does not have separate financial account, which is instead subsumed in the capital account. The IIP, too, is compiled along the lines of international best practices. There is a broad correspondence between the BoP and IIP numbers.

### ***Progress in Strengthening the Linkages***

2.26. The IMF's fifth edition of the BoP Manual (BPM5) published in 1993 introduced a variety of changes and improvements in the coverage, compilation and presentation of the BoP. Important among them was the expansion of the conceptual framework to encompass BoP flows (transactions) and stocks of external financial assets and liabilities (IIP). A clear distinction was made between (i) transactions and (ii) other changes in the accounts—valuation, reclassification, and other adjustments. Additionally, linkage of the IIP and BoP accounts to the rest of the world account in the SNA was strengthened and harmonised to the maximum possible extent. Cases in point are identical treatments in the two systems of residence, valuation, timing, and reinvested earnings on direct investment. Also, to strengthen the harmonisation with the SNA, a distinction between current and capital transfers was introduced in the Manual. “Capital account” was re-designated as the “capital and financial account” in BPM5.

2.27. There were also changes in the treatments of international services, income, and certain financial transactions. First, a clear distinction was made in the current account between international transactions in services and transactions in income. Earlier, labour and non-financial property income were grouped together with “services other than shipment, travel, and transportation”, while investment income was covered separately. In the BPM5, the two main components of income flows between residents and non-residents, *viz.*, compensation of employees and investment income were separately identified, strengthening the harmonisation with the SNA. Second, services transactions were broken down further to reflect their growing prominence in international transactions and their importance in international trade negotiations on the one hand, and to provide links between separate statistical systems on the other. Third, the coverage of financial flows and stocks was significantly expanded and restructured in view of the emergence of financial innovations.

2.28. The sixth edition of the Manual (BPM6) carried forward the efforts to improve the coverage, compilation and presentation of BoP by addressing many important developments that have occurred in the world economy since the release of the fifth edition in 1993. The BPM6 built further on the growing interest in examining vulnerabilities, using balance sheet data and extensive elaboration of balance sheet components. The Manual also took into account developments in globalisation, for example, the formation of currency unions, change in cross-border production processes, evolving complex international company structures, shifts in the flow of remittances and the changing dimensions of mobility of international labour.

2.29. The Manual tried to elaborate on the economic significance of new innovations in the financial markets, such as financial derivatives, securitisation of loans, and the business of Special Purpose Vehicles. In other words, the three major factors that necessitated the revision of the Manual were globalisation (for understanding the importance of the globalised nature of production processes and the need for new institutional arrangements to deal with special purposes entities and complex, multi-economy corporate structures); increasing elaboration of balance sheet issues (for proper understanding of international economic developments, particularly vulnerability and sustainability), and financial innovations (necessitating differential treatment of new and complex financial products such as derivatives and securitised instruments). In order to address these developments and

strengthen the inter-linkages, the BPM6 introduced some significant changes in its guidelines for BoP compilation as compared with the BPM5. The most important changes include:

- i. Goods for processing are now classified as services, while merchanting is included under merchandise trade.
- ii. Financial Intermediation Services Indirectly Measured (FISIM) is now identified separately. Similarly, spreads on the purchase and sale of securities and the compilation of insurance and pension services are now captured under a distinct category.
- iii. Elaboration of direct investment while making it consistent with the OECD Benchmark Definition of Foreign Direct Investment (FDI). Notably, the recasting of the definition of FDI in terms of control and influence, bringing into focus chains of investment and fellow enterprises, and the presentation of FDI on a gross asset/ liability basis.
- iv. The inclusion of SDRs as reserve-related liabilities in BoP as well as IIP statistics as against its earlier omission. In other words, they were only part of assets and not liabilities.
- v. The scope of personal transfers is widened to include all current transfers in cash or in kind made or received by resident households to or from non-resident households independent of the source of income of the sender and the relationship between the households.
- vi. BPM6 focused on balance sheets and balance sheet vulnerabilities by strengthening the linkages between flows (BoP) and stock (IIP) by streamlining the account of “other changes in the assets and liabilities”.
- vii. BPM6 re-grouped “income” and “transfers” (BPM5) into “primary income” and “secondary income” in order to strike concordance with the SNA.

## Chapter III: Merchandise Trade

3.1. The current account of the BoP includes all transactions (other than those in financial items) involving economic values which take place between resident and non-resident entities. The items covered under the current account also include offsetting entries on account of current economic values provided or acquired without a *quid pro quo*, e.g., private transfers. Accordingly, current account transactions are broadly classified into goods, services, income, and current transfers. While the goods and services account reflects transactions in items that are outcomes of production activities, the income account shows income receivables and payables in return for providing temporary use of factors of production (*i.e.*, primary income, such as investment income and compensation of employees) as well as redistribution of income through current transfers (*i.e.*, secondary income such as personal transfers and current external assistance). This chapter deals with the merchandise trade (goods) account in terms of its coverage, valuation and sources of data as well as the compilation procedures followed in the Indian context.

### ***International Best Practices***

#### *Coverage*

3.2. Goods, a component of the current account, generally covers all movable goods that residents export to, or import from, *non-residents*, which involve changes in ownership (actual or imputed). As per the IMF's latest BoP manual (BPM6), the goods account comprises (a) general merchandise, (b) goods under merchanting and (c) non-monetary gold.

### **General Merchandise**

3.3. According to BPM6, general merchandise covers goods “whose economic ownership is changed between a resident and a non-resident and that are not included in the following specific categories: goods under merchanting, non-monetary gold, and parts of travel, construction, and government goods and services *n.i.e.*”

3.4. In addition to export and import of commodities, the items included in general merchandise on the basis of change of ownership of goods are as under:

- i. Goods acquired by travellers for re-sale abroad (also called shuttle trade), and goods for own use or those acquired by travellers in excess of customs thresholds which are included in customs statistics.
- ii. Goods acquired abroad (*i.e.*, purchases of materials) and sold abroad (*i.e.*, finished goods) by the resident units in the compiling economy without passing them through its territory. Processing should have brought about significant transformation in the state of the goods and if not so, they have to be included under merchanting.
- iii. Goods such as fuels (bunkering), provisions, stores, ballast, dunnage, *etc.*, procured by non-resident transport operators in ports from residents are considered as exports of general merchandise. Similarly, goods procured by resident transport operators from non-resident providers in foreign ports are considered as imports. Ports for this purpose are defined broadly to include sea and ocean terminals, airports and inland waterways. In addition, the procurement of goods from residents by non-resident road and rail transport operators are included under merchandise exports.
- iv. Non-customised packaged software (systems and applications) and video and audio recordings on physical media, such as disks and other devices, with a licence for perpetual use are considered as general merchandise. These products are recorded at their full transaction value (and not at the value of the empty disks or other storage devices). Software provided in this form is included in goods, while other software (customised) is included under services.
- v. The amount spent for import or export of electricity, gas and water are part of goods. However, charges involved for the transmission, transport, or distribution of these products are included in services under transport and other business services.
- vi. Goods sent abroad on consignment or for storage, repair, exhibition, processing, *etc.* which do not involve a change of ownership are not recorded as merchandise at the time they are sent abroad. However, if they are later sold to a resident of an economy different from that of the owner, they should be recorded in general merchandise.
- vii. Banknotes and coins not in current circulation and un-issued securities are to be valued as commodities rather than at their face value and included as general merchandise.
- viii. Goods supplied or acquired by carriers in a different territory than the residence of the operator.

- ix. Goods acquired by a lessee under a financial lease (where the lessee is the owner, while the lessor has only the legal title and not the economic ownership). In contrast, goods under operating leases do not change ownership to the lessee when delivered, and thus form part of services rather than general merchandise.
- x. Goods without involving associated payments, such as those financed by grants or loans are treated as merchandise trade.
- xi. Other items to be included are goods lost or destroyed after an importer acquires ownership but before crossing the frontier, illegal goods, smuggled goods, gifts, parcel post, live stock, humanitarian aid in the form of goods, *etc.*

Similarly, goods not covered under merchandise are:

- i. Goods that do not involve change of ownership or have no economic value; and goods entering the territory under transit trade;
- ii. Goods consigned to embassies, military bases, *etc.* from their home authorities;
- iii. Personal property that accompanies people changing residence;
- iv. Goods for assembly, packing, labelling, or processing by an entity that does not own the goods concerned (which is included as manufacturing services on physical inputs owned by others);
- v. Goods acquired by a lessor (who has legal titles but no economic ownership) under a financial lease;
- vi. Goods with no positive value (*viz.*, dangerous items) for disposal or storage, returned goods or sample products which are not for sale. In the case of returned goods, revised entries should be made to exports and imports against what was initially recorded; and
- vii. Goods exported or imported temporarily without involving any change of ownership (*e.g.*, goods for repair as part of an operating lease or for storage, and animals or artefacts for participation in exhibitions or competitions).

3.5. The exclusion of some items of export and import from general merchandise is recommended because they are included elsewhere; these are:

- i. Goods acquired or sold by residents without entering the economic territory; they are shown separately as goods under merchanting, an arrangement that is generally used for wholesale and retail trade.

- ii. Non-monetary gold, either as bullion or in any other form, is shown separately within the goods account;
- iii. Goods that are included in travel such as those acquired by persons while on study or medical care outside their territory of residence;
- iv. Goods acquired locally for construction undertaken by non-resident enterprises at the location of the work (which are included under construction services);
- v. Customised devices, such as disks with stored computer software or data (which are included under computer services);
- vi. Products such as packaged software (systems and applications), video and audio recordings, *etc.* that are delivered on disks, magnetic media, or storage devices, but with a fixed period licence to use (as there is no change of ownership, they are included under computer or audiovisual services). Licence to reproduce and/or distribute audio and video, are included as charges for the use of intellectual property n.i.e.;
- vii. Customised blueprints and non-bulk newspapers and periodicals sent as part of direct subscriptions (which are included in information services). Such products, if exported or imported in bulk, are included in general merchandise.

### **Re-Exports/Re-Imports**

3.6. Re-exports are exports of those goods which were imported earlier with the intention of exporting at a later date, without making substantial change in the state of the goods. In cases where the state of the imported goods is substantially transformed, they should be recorded as domestically produced exports rather than re-exports (*e.g.*, goods assembled or processed or goods that have become rags, wastes, scraps, antiques, *etc.*). For goods to be recorded as re-exports, a resident must acquire the goods and then re-sell them, with the goods passing through the territory. Goods that do not pass through the territory of the owner are recorded as goods under merchanting. Goods in transit are neither recorded under imports nor re-exports. Apart from some value addition, the price of the re-exported goods may also be different from their price at the time of original import due to various factors, such as transportation cost, dealers' margins and holding gains/losses.

3.7. Re-imports are domestic goods imported in the same form as previously exported, without the goods undergoing substantial transformation while they were outside the

territory. Wherever possible and where they are significant, re-exports and re-imports should be shown separately as supplementary items.

### Goods under Merchanting

3.8. Merchanting is defined by the BPM6 “as the purchase of goods by a resident (of the compiling economy) from a non-resident combined with the subsequent resale of the same goods to another non-resident without the goods being present in the compiling economy”. In fact, there are two important features of merchanting, *viz.*, the goods acquired should not enter the territory of the compiling economy and the state of the goods should not undergo any transformation. Merchanting arrangements are generally used for wholesaling and retailing; they are also used in commodity dealing and in handling global manufacturing processes. When these *activities* are carried out under an arrangement where the goods are present in the economy of the owner, they are recorded as general merchandise rather than as merchanting. In cases where the goods do not pass through the territory of the owner but there are changes in the physical form of the goods, because they are processed in another economy, such transactions are recorded under general merchandise (the processing fee is recorded under manufacturing services).

3.9. "Merchanting" appears only as exports in the accounts of the merchant's economy (acquisitions are shown as *negative* exports, while the sale is shown as positive exports) and reported as “net exports of goods under merchanting”; the counterpart exporting and importing economies record sales to merchants as export and purchases from merchants as import under general merchandise. When a merchant resells goods to a resident of his own economy, the purchase of goods is shown as import under general merchandise; the subsequent re-sale to a resident of another economy, irrespective of whether or not the goods enter his economy, is recorded as export under general merchandise in the merchant's economy. Merchanting entries are recorded on a gross basis at the time of change in economic ownership of goods and are valued on the basis of transaction prices as agreed upon by the parties and not on FOB basis.



## Non-monetary Gold

3.10. Non-monetary gold covers all gold other than monetary gold. Monetary gold is the gold (which includes gold bullion and unallocated gold accounts with non-residents that give title to claim the delivery of gold) owned by monetary authorities and held as a reserve asset. Non-monetary gold can be in the form of bullion, gold powder and gold in other unwrought or semi-manufactured forms. Jewellery, watches *etc.* that contain gold are to be included under general merchandise and not under non-monetary gold. The demand for non-monetary gold arises either as a store of value or for other uses in manufacturing jewellery or dental work.

3.11. Sales and purchases of non-monetary gold that are not shipped should be valued at transaction prices (not on FOB basis), inclusive of dealer's margins or commissions not billed separately. Allocated gold accounts are treated as being arrangements for the storage of gold bullion (and not as deposits) and ownership of the gold continues to be with the entity placing it for safe custody. Therefore, putting gold into or withdrawing gold from the allocated account is not recorded as transactions. On the contrary, unallocated gold accounts are claims against the account provider (rather than against gold as in the case of allocated accounts), who, in turn, holds title to the gold. Thus, these accounts are treated as financial assets (and included under monetary gold or deposits, depending on the holder). When both parties to a gold transaction are either monetary authorities (that hold the gold as reserve assets) or international financial organisations, the sale of gold is recorded as monetary gold in the financial account; otherwise, gold sales are recorded under non-monetary gold. Following the principle of change in ownership, gold sales and purchases should be recorded even when there is no physical movement (*i.e.*, held at specialised bullion storage centres).

## Time of Recording

3.12. Ideally, the recording of transactions relating to general merchandise should coincide with the time of change of ownership. However, international trade statistics do not adopt this concept and, for the most part, it is impractical to adjust the timing of transactions in goods to the time of ownership change. In practice, the timing of the change of ownership is usually approximated with the time when customs records the transactions. Thus, in the case of goods, ownership is said to change when the parties to the transaction enter the goods as a

real asset in their books and make a corresponding adjustment in their financial assets and liabilities.

3.13. With respect to goods on consignment, as per international best practice, goods intended for sale, storage, auction, *etc.*, should not be included in the international accounts until their ownership changes, in order to avoid a source of discrepancy between the flow of goods and the corresponding changes in the financial assets and liabilities.

## Valuation

3.14. The BPM6 suggests that the principle for valuation of general merchandise should be the market value of the goods at the customs frontier of the economy from which the goods are first exported and imported, *i.e.*, the market value of goods free on board (FOB) for both exports and imports. The International Merchandise Trade Statistics (IMTS), however, uses FOB-type valuation for exports and CIF-type (cost, insurance and freight type) valuation for imports. Therefore, to convert imports from CIF to FOB basis for the purpose of international accounts, the value of freight and insurance premia incurred from the frontier of the exporting country to the border of the importing country has to be deducted. The relationship between FOB and CIF prices depends on various factors, such as type of goods, weight, scale (bulk or not), modes of transport and the distance travelled.

## ***Indian Practice: Merchandise Trade***

### Data Sources

3.15. There are two sources of data for merchandise trade in India — customs data reported by the Directorate General of Commercial Intelligence and Statistics (DGCI&S) and banking channel data reported by Authorised Dealers in foreign exchange (ADs) to the Reserve Bank of India through the Foreign Exchange Transactions Electronic Reporting System (FETERS). For the compilation of BoP in India, the exports valued at the customs which is on “free on board” (FOB) basis and imports valued on the basis of “cost, insurance and freight” (CIF) reported through the banking channel are used. While the banking channel data provide full coverage of payments, the customs data provide valuable information related to commodity-wise and source-wise imports for policy formulations. However, given the importance of the

two data sources, the discrepancies in the merchandise imports reported by the DGCI&S and the RBI are published along with the standard components of BoP as part of the reconciliation exercise to improve the usefulness of the data. These aspects are discussed below in detail under the compilation procedures.

## **Directorate General of Commercial Intelligence and Statistics**

### Coverage and Valuation

3.16. The Indian Customs Act, 1962 (Section 14) lays down the basis for valuation of goods imported into and exported from the country. Sub-section (1) of Section 14 (as amended) states that when customs duty is chargeable on any commodity by reference to its value, the value of such goods shall be deemed to be the price at which such or like goods are ordinarily sold, or offered for sale, for delivery at the time and place of importation or exportation, as the case may be, in the course of international trade, where the seller and the buyer have no interest in the business of each other and the price is the sole consideration for the sale or offer for sale. As far as export of goods is concerned, the provisions of Sub-section (1) of Section 14 provide a complete code of valuation by itself. On the other hand, for imported goods, as per Sub-section (1A) of Section 14, the value is required to be determined in accordance with rules made in this regard. Accordingly, the Customs Valuation (Determination of Price of Imported Goods) Rules, 1988 have been framed and notified.

3.17. According to the Customs Valuation Rules, 1988, the customs value should normally be the “transaction value”, *i.e.*, the price actually paid or payable and subject to (a) compliance with the valuation conditions, and (b) the customs authorities being satisfied with the genuineness and accuracy of the declared value. The price actually paid or payable is the total payment made or to be made by the buyer to the seller. It includes all payments made as a condition of sale of the imported goods by the buyer to the seller or by the buyer to a third party to satisfy an obligation of the seller. However, in certain cases, the transaction value may not be acceptable to the authorities and valuation as provided in Rule 4(2) and Rule 10A is worked out.

3.18. Exports of goods are valued on FOB basis at the customs frontier where the price includes the value of the goods, the value of outside packaging (other than international

containers used for containerised cargo) and related distributive services used domestically, up to and including loading the goods onto the carrier at the customs frontier.

### Currency Conversion

3.19. The values of exports and imports of goods denominated in foreign currencies are converted into Indian rupees at market exchange rates by using representative mid-points of the buy and sell FEDAI indicative average rates of the respective month.

### Reporting of Data

3.20. DGCI&S is the official organisation for compilation and dissemination of India's trade statistics based on the returns received from the customs authorities. In the customs returns, the exports statistics are expressed based on the declarations made by individual exporters in shipping bills which are subsequently checked and cleared by Customs/SEZ authorities, while the import statistics are indicated on the basis of declarations made by importers in the Bills of Entry that are subsequently checked and cleared by the customs authorities. Based on such declaration forms filed by exporters and importers, the customs authorities, in turn, prepare the Daily Trade Returns (DTRs) from their records and send them to DGCI&S for processing and presentation of statistics on foreign trade.

3.21. The trade returns, which are received by DGCI&S from customs authorities, are in electronic form [(on-line processing system of Electronic Data Interchange (EDI), e-mail, CD) or manuscript form (typed/ handwritten) through postal mails. In terms of total number of transaction records, about 85 per cent of exports and 94 per cent of imports were received through EDI mode during 2009-10. In terms of value of trade, 58 per cent of exports and 66 per cent of imports were received through this mode. The remaining data were received through non-EDI/manual mode directly from the customs formations.

3.22. The non-EDI returns (e-mail and CD) accounted for 8 per cent and 4 per cent of transactions in 2009-10, and in terms of value these were about 30 per cent and 12 per cent of exports and imports, respectively. Manual DTR accounted for 7 per cent and 2 per cent of transactions, while in value terms these formed 12 per cent and 22 per cent of exports and imports, respectively. There was an increase in the share of non-EDI data compared to the

previous years. This was mainly due to the inclusion of SEZ data (which furnish DTRs by e-mail/CD). At present there are 213 active ports (including airports, seaports, land customs stations, foreign post offices, Export Processing Zones, etc.) which are reporting trade data. Of these 42 have been transmitting data through the EDI online mode, 46 through the non-EDI electronic mode and 125 send data on manual mode.

3.23. Since 1987, the DGCI&S has adopted the Indian Trade Classification (ITC) system of goods for merchandise trade (ITC-HS), which conforms to the international classification system called “Harmonised Commodity Description and Coding System” evolved by the World Customs Organization (WCO). Being a signatory to the WCO, India has adapted to ongoing changes in the international trade data classification. For instance, India adopted the 8-digit classification code with effect from February 1, 2003. Subsequent to changes in the trade data classification by the WCO in January 2007, DGCI&S adopted the latest 6-digit classification of the WCO, with a further 8-digit classification to suit Indian requirements in accordance with changing trends in the production and consumption of commodities. As per the new 6-digit international classification, DGCI&S releases the trade data regularly in its publication titled *Foreign Trade Statistics of India*, effective April 2008.

3.24. According to the DGCI&S, the statistics on merchandise exports and imports cover all trade carried by different modes of transport such as recognised sea ports, airports, land customs stations of India and inland container depots. From the year 2008-09, the data also cover merchandise exports and imports through the Special Economic Zones (SEZs). Apart from the expanded coverage of modes of transport, the merchandise trade data also cover (i) transactions in silver (other than current coins) and in notes and coins not yet in circulation or withdrawn from circulation, and (ii) indirect transit trade. However, it excludes direct transit trade, transshipment trade, passenger baggage, ship’s stores, defence goods and transactions in treasure, *i.e.*, current coins and notes, diplomatic goods, and “prohibited substances” under the Atomic Energy Act, 1962. In other words, it excludes cross-border movements that (i) do not (usually) involve change of ownership, such as direct transit trade, transshipment trade and animals for racing and breeding, and (ii) those which qualify for classification elsewhere in the BoP, such as currency.

3.25. To meet users’ needs, the trade data, comprising time-series and cross-section data on merchandise exports and imports in both value and volume terms, are provided by the

DGCI&S under different categories such as commodity, country and port as well as on an aggregate basis. The aggregate data are provided both on a monthly and cumulative basis. Provisional data on India’s total exports and imports on a monthly and cumulative basis are released by the Ministry of Commerce and Industry (MoC), Government of India through its Press Release. These data are released on the first or second working day of every month, with a lag of one month. Shortly after the Press Release, these data on total exports and imports are also released every month by the DGCI&S through a Press Note<sup>3</sup>.

3.26. In the next stage, the trade data classified by principal commodities and countries on a monthly and cumulative basis are released by the DGCI&S in the form of a publication titled “Foreign Trade Statistics of India (FTSI): Principal Commodities and Countries”, commonly known as “Brochure”, with a time lag of around 2 to 3 months, which may contain revisions in the trade data. Subsequently, the detailed commodity/country-wise data as per the International Trade Classification (Harmonised System) [ITC-HS)] codes at the 8-digit level is released by the DGCI&S on a monthly and cumulative basis through the publication known as the “Monthly Statistics of Foreign Trade of India (MSFTI)”, with a lag of about 4 to 5 months, which generally carries further revisions of trade data (Table III.1). All these releases also normally contain revised data pertaining to the corresponding period of the previous year.

**Table III.1: Calendar for Release of Trade Data**

Serial No.	Name of Publication	Periodicity	Time Lag *	Data Released By
1	Press Release	Monthly	1 month	MoC
2	Press Note	Monthly	Shortly after Press Release	DGCI&S
3	FTSI	Monthly	3 months	DGCI&S
4	MSFTI	Monthly	6 months	DGCI&S

\*Approximate indicative time lag from the period to which data pertains. Actual lag may vary marginally.

3.27. Further, the DTRs for a particular month received from the Customs after the release of MSFTI of that month are termed as ‘late receipt data’, which are added to the database. While releasing the MSFTI for the following month, data in respect of all the previous months of that financial year are also revised incorporating the late receipt data into the respective months. DGCI&S follows this dynamic revision policy with effect from April, 2009. This way if the monthly figures are added up from April to any particular month, the

<sup>3</sup> Generally, the Press Release and Press Note present the same data set.

same will tally with the cumulative figure for that month. In other words, DGCI&S revises the monthly MSFTI figures with the release of MSFTI for all the months following that month till the finalisation of data for that financial year. DGCI&S also follows this dynamic data revision policy for its other publication namely FTSI -‘Principal Commodities and Countries’.

3.28. The revisions take place at the stage of Press Note, FTSI and MSFTI till data for the month of March is finalised and released. As the two data sets are getting continuously updated/revised every month and data for a particular month is released at different points of time, the provisional data of Principal Commodities and the 8-digit ITC (HS) commodity level data may not always tally until the two data sets are frozen at the end of the financial year. The data for April-March after it is frozen at 8-digit ITC (HS) commodity level will be termed as the final figures for the year and corresponding monthly figures will be the final figures for the respective months.

3.29. Revisions in the trade data take place mainly on account of a considerable time lag involved in the receipt of non-EDI data — both electronic and manual— with the time lag running into several months. Some ports that handle bulk cargo, such as gems and jewellery, crude oil and petroleum products, are not covered under EDI. Since the shares of these commodities are significant in imports and exports, the scale of revisions is also, at times, very large. Moreover, in the absence of complete data from all the custom ports, the DGCI&S employs an estimation procedure (both trend- and model-based) for non-receipt/delayed receipt of data, which at times generates a significant downward bias.

3.30. In order to reduce the gap between the provisional and final figures, several efforts have been undertaken by the DGCI&S to improve the method of collection of non-EDI and manual data with minimum errors as well as time lag, and expand the coverage to additional ports and SEZs, as mentioned earlier. It may be noted that the data capture stage was switched over to “Let Export Order” (*i.e.*, clearance by customs authorities after physical verification of the export contents and after satisfying that goods are not prohibited for export and that export duty, if applicable, is paid) in the year 2003-04 from “Export General Manifest” (*i.e.*, a declaration filled in by the person in-charge of the vessel or craft or by his agent before departing Indian territory) to reduce the time lag in reporting.

## **Banking Channel: RBI-FETERS**

3.31. As opposed to customs data provided by the DGCI&S, which are recorded only on clearance of goods at customs, banking channel data (RBI-FETERS) on merchandise trade are captured at different points — on the day of payments in the case of imports on cash basis, on the date of release of loan to the supplier in the case of imports financed by credits/loans, and on the date of imports reported by the company in the case of goods imported through equity participations. As regards exports, they are recorded when documents are submitted by the exporters to the ADs for collection or when export receipts are realised. Once the exporters submit the documents to ADs for collection /negotiation /discount /purchase of the export bill, those transactions are reported in the ENC file of FETERS. The data captured in this file are based on the negotiation date and not on the shipment date. Moreover, all individual transactions pertaining to export, non-export, import, non-import, intermediary export and intermediary import are reported in the BoP file, as discussed in detail in the next chapter. Realised transactions related to exports are reported exclusively in the Sch. 3 to Sch. 6 file of FETERS which are used for monitoring purposes by the Foreign Exchange Department of the RBI.

## **Compilation and Presentation of Merchandise Trade in BoP**

### ***Compilation***

3.32. In India, for compilation of BoP, export data are gathered through both customs and banking channels. Export data on customs basis (*i.e.*, on FOB basis) are used for the purpose of BoP compilation; however, they are adjusted for the valuation difference. The differences in valuation arise as the exchange rate used by the customs and the RBI are different. Exports data at the customs are valued at foreign currency rates prevailing at the beginning of each month while, in principle, for BoP purposes the valuations should be made using the exchange rate applicable for each transaction or by a rate which is close to the transaction rate. As exchange rate movements vary from day to day, week to week and period to period, there can be no accurate predetermined percentage adjustment to account for the valuation difference. Nonetheless, a standard percentage rate (based on the Reserve Bank's survey for estimating differences between the data reported by DGCI&S and the data captured in the original currency at the customs end) has been used to adjust the customs export data.



3.33. The other source of export data is the banking channel, which is based on reports submitted by Authorised Dealers (ADs) on relevant foreign exchange transactions put through during the reporting period (FETERS). Although the data on exports recorded in the BoP are based on those reported by DGCI&S, the exports statistics reported in FETERS are used to estimate “freight & insurance” and “leads and lags” in exports, which are recorded under the “services account” and the “financial account”, respectively. From FETERS exports data, the portion on freight and insurance is extracted with the help of the results of a survey (survey of customs returns). Similarly, software exports reported under export receipts in FETERS are also taken out to arrive at merchandise exports. The difference between the merchandise exports so derived from FETERS and those recorded in the BoP based on customs data is called “leads and lags in exports” and included in the capital account under the head “other capital”. The “lead and lag” occurs essentially because of the timing of recording of exports. The differences in timing of recording arises as customs data are reported when shipments take place, while banking channel data are reported when receipts are realised.

3.34. As regards imports, the banking channel data, based on reports submitted by ADs, are used to compile India’s BoP. As import data reported by the ADs are based on payments mode, they do not include “non-AD” imports, *i.e.*, not paid for through ADs. The “non-AD” imports, which are included in the aggregate imports, cover grant components of aid (reported by the Government of India), gold and silver imported by returning travellers and migrants (extracted from customs data), imports paid from accounts held abroad (reported by Indian corporates accessing external commercial borrowings) and suppliers’/ buyers’ credits considered on a net basis. Therefore, these items are added to imports reported under FETERS to arrive at total imports on BoP basis. As in the case of exports, the advance payments under imports, *i.e.*, leads and lags in imports, which are reported by ADs in FETERS are included in the capital account under the head “other capital”. The DGCI&S import data are, however, used for the purpose of cross-checking and monitoring.

### **Presentation**

3.35. Table III.2 provides the comparative position of India’s presentation of merchandise trade data under BoP *vis-à-vis* that suggested by the IMF Manual.

**Table III.2: India's status vis-à-vis BPM5 and BPM 6 (Goods)**

<b>BPM5</b>	<b>BPM6</b>	<b>India's Position</b>
<b>Goods (1 to 5)</b>	<b>Goods (a+b+c)</b>	<b>Goods</b>
1. General merchandise	(a) General Merchandise Of which: Re-exports#	Only general merchandise
2. Goods for processing	No (included in services as manufacturing services on physical inputs owned by others)	Not separately shown
3. Repairs on goods	No (included in services as maintenance & repairs services)	Not separately shown
4. Goods procured in ports by carriers	Yes (included under general merchandise)	Not separately shown
##	(b) Net exports of goods under merchanting#	Merchanting is part of business services
5. Non-monetary gold	(c) Non-monetary gold	Not separately shown

#: Recorded on net basis as credits in BPM6.

##: Merchanting was part of other business services in BPM5.

3.36. As for the coverage, to comply with international best practices in the presentation of merchandise trade data as per BPM6, the re-classification requires the following:

- i. Goods for processing not to be recorded as goods (the processing component to be included in services and renamed “manufacturing services on physical inputs owned by others”).
- ii. Repairs on goods not to be recorded as goods (which are to be included in services and renamed “maintenance and repair services *n.i.e.*”).
- iii. Goods procured in ports by carriers need to be reviewed and reclassified as goods under general merchandise.
- iv. Goods subject to merchanting will have to be recorded under merchandise exports (in BPM5, merchanting was recorded as a service).

3.37. Thus, to comply with the standard presentation of merchandise trade data as suggested in BPM 6, the methodology to be followed in India's BoP should be as follows:

**Table: III.3: Methodology for Compiling Merchandise Trade**

<b>Items</b>	<b>Description</b>
A. Goods (A.1+A.2+A.3)	Recorded trade (Customs and FETERS.)
	Adjustment for valuation
A.1. General Merchandise	A — (A.2+A.3)
Of which: <i>Re-exports</i>	Recorded under Customs
A.2. Net Merchanting	Captured through FETERS
A.3. Non-monetary gold	Captured through Customs

3.38. The merchandise trade data received from DGCI&S need to be segregated into (i) general merchandise (with *re-exports* as a supplementary item), (ii) net exports of goods under merchanting and (iii) non-monetary gold. Towards this end, non-monetary gold needs to be taken out from total imports and shown separately. Merchanting transactions, *i.e.*, the buying and selling of goods that do not cross national boundaries are to be recorded in the BoP as a goods component and valued as profits or losses on sales of goods. The profit should be recorded with a positive sign, while the loss should be recorded with a negative sign on the credit side of the goods account. It is difficult to capture the transactions on a gross basis as the net gains/losses are known only to the merchants and not to the importer. Therefore, the transactions can be captured through FETERS when the merchant receives the profits or makes payments for losses. Accordingly, the present purpose code for merchanting under FETERS needs to be redefined appropriately to capture net merchanting and the same needs to be adjusted for in the DGCI&S total exports. To show re-exports as an “*of which*” item under general merchandise, an additional code for re-export will have to be introduced at the custom's end and reported by the DGCI&S in their merchandise trade data. Moreover, to comply fully with international best practices on presentation of merchandise trade data, there is a need to move away from the present practice of reporting imports on a CIF basis to an FOB basis.

### ***Reconciliation between Banking Channel and DGCI&S Data on Merchandise Trade***

3.39. The divergence in the merchandise trade data, particularly imports, compiled by the Reserve Bank of India using the banking channel data reported by the Authorised Dealers (ADs) and the Directorate General of Commercial Intelligence and Statistics (DGCI&S),

Ministry of Commerce and Industry using customs data has been a subject of serious concern since the 1980s. In order to reconcile the two sources of data, a number of Committees/Groups were set up to examine the relevant issues, which have made various recommendations.

3.40. The main reasons for divergence as identified by the various Groups were the exclusion of some items of merchandise trade by DGCI&S and the probable inclusion of non-merchandise trade items by the RBI. First, while RBI data are based on payments made for imports, customs data are generally recorded on the basis of movements of goods across the customs frontier. Second, the difference in timing of recording of goods arises since imports are recorded only on clearance of goods at customs. Thus, the customs data excludes cross-border movements that do not (usually) involve change of ownership, such as direct transit trade, transshipment trade covering imported goods transported under bond for re-shipment from one vessel to another, animals for racing and breeding, and defence goods/fissionable material. As per international best practices, merchandise imports in the BoP should record all goods that change ownership from non-residents to residents in the reporting period. Besides, the scope, definition and methods of data differ considerably between the two agencies, as discussed earlier. As such, given the leads and lags in reporting, the two sets of data may not match. However, the gap usually reduces with the provisional customs data getting revised subsequently with greater coverage as well as realisation of imports through customs for which payments had already been made and as such covered under banking channel data. Therefore, the better comparison is between revised customs data and BoP.

3.41. Apart from these methodological issues, historically, there have been several other causative factors behind the divergence, such as: (i) non-inclusion of defence imports in the DGCI&S data; (ii) non-capture of data relating to purchase of goods and services in order to operationalise oil fields or acreages acquired abroad particularly by oil companies in DGCI&S data; and (iii) non-coverage of acquisition of aircrafts on lease or hire purchase basis, and ships or vessels acquired by shipping companies abroad but remaining on foreign runs for a considerable length of time that are often not reported in the DGCI&S data. It may be noted that DGCI&S is now partially covering some of these data through special arrangements with the Directorate General of Civil Aviation (DGCA) and Directorate General of Shipping.

3.42. Notwithstanding the implementation of some of the recommendations of various Groups over time, the divergence is still high on various occasions. The key recommendations of some Groups and the progress in their implementations are set out in Table III.4. For instance, the difference between the RBI and customs data for imports during April-December 2008 amounted to US\$ 14.4 billion, which came down subsequently to US\$ 6.8 billion for the full year 2008-09 (April-March) and further to US\$ 4.0 billion (partially revised) after the revision of customs data due to late receipts of data from several ports and from Special Economic Zones (SEZs). As per the preliminary data released by the RBI for 2009-10, BoP imports captured through the banking channel were higher by about US\$ 12.6 billion over the DGCI&S imports data. This underscores the need for a fresh examination of the issue of divergence between the two sources of data. Reconciliation is, thus, necessary to aid data validation and improve the serviceability of the data.

**Table III.4: Status of Implementation of Key Recommendations on Reconciliation of Merchandise Trade Data**

Group	Key Recommendations	Progress in Implementation
<p>High Level Committee on Balance of Payments:1993 (Chairman: Dr. C. Rangarajan, Government of India)</p>	<p>(i) Where imports do not pass through customs declaration, concerned agencies may be requested to report in a consolidated form the value of imports on a routine basis for purposes of incorporation into the customs data; and (ii) Information system may be established through the Ministry of Shipping and Ministry of Petroleum to obtain information on payments made but not reflected in customs data.</p>	<p>(i) Not fully implemented  (ii) Not fully implemented</p>
<p>Technical Group on reconciling Balance of Payments and DGCI&amp;S data on Merchandise Trade: 1995 (Chairman: Shri O.P. Sodhani; Reserve Bank of India)</p>	<p>(i) To establish commonality between the data recording systems with the long-run objective of ensuring online information transfer between the concerned organisations. (ii) DGCI&amp;S should make necessary arrangements to record imports not passing through customs or exempted from customs declaration. (iii) DGCI&amp;S should send a monthly report on the import of gold and silver brought in as baggage by returning Indians. (iv) The Ministry of Finance should make necessary arrangements for regular reporting of defence imports data to the RBI. (v) Use of common exchange rates.</p>	<p>(i) Commonality is not fully established. (ii) Partially implemented (iii) Implemented (iv) Partially implemented (v) Implemented</p>
<p>Study Group on Merchandise Trade Data: 2001 (Convenor: Shri M.R. Nair, Reserve Bank of India)</p>	<p>(i) Reiterated the need to establish connectivity among Customs, RBI and DGCI&amp;S, adoption of DTRs as a common evidence of actual shipment of goods; and inclusion of imports of defence goods in merchandise trade data of DGCI&amp;S. (ii) Need for DGCI&amp;S to improve the coverage of data in consultation with Customs for various omitted items of data as also those from minor ports. (iii) Need to carry out suitable modifications in the software package used by AD branches (FETERS package) to include IE code and BIN as given by customs as separate entries.</p>	<p>(i) Partially implemented in the case of connectivity and DTRs while DGCI&amp;S yet to include defence data in their imports. (ii) Partial reporting from minor ports with a time lag. (iii) Implemented</p>

<p>Sub-Group on Reconciliation of the Merchandise Trade Data: 2007 (Chairman: Shri Ashok Jha, Government of India)</p>	<p>(i) A reconciliation statement to be prepared annually by the Department of Economic Affairs explaining and qualifying the major reasons for divergence.</p> <p>(ii) As regards defence imports, the information may not be included in DGCI&amp;S data. A parallel reporting system may be adopted and the consolidated position to be shown in the reconciliation statement.</p> <p>(iii) Apart from getting a statement on defence imports from the Ministry of Defence, the Customs authorities may give summary value recorded under defence imports (Embarkation Commandant) to DEA and RBI on a monthly basis.</p> <p>(iv) DGCI&amp;S has to adopt the customs DTR data for imports of petroleum products and crude petroleum. This data has to be compared with oil import data of MoP&amp;NG and, in case of large divergence, it is required to reconcile through a system of detailed consultation on a record-by-record basis by MoP&amp;NG and DGCI&amp;S.</p> <p>(v) MoP&amp;NG would provide details of all acquisitions of oil fields or equity abroad by PSUs and acquisition of equipment abroad to RBI. For non-transactions, the RBI should devise a system of separately capturing the trade component of this in their database.</p> <p>(vi) The RBI may evolve a system of capturing detailed information on the acquisition of a ship abroad and its entry into Indian waters, and information on acquisition of aircrafts on lease/ outright purchase through the filing of B/E separately for the purposes of reconciliation.</p>	<p>The recommendations are only partially implemented.</p>
<p>Report of Consultant to the Reserve Bank of India on Balance of Payments Data, August 2007 (Mr. Neil Patterson)</p>	<p>(i) Develop and publish an annual reconciliation statement between Customs and banking channel data.</p> <p>(ii) Ensure that aircraft acquired under financial lease are adequately reflected in BoP statistics.</p> <p>(iii) Encourage the adoption of measures to reduce the time in the reporting of Customs exports and imports and improving the method of collection. In the interim, adopt sound procedures to adjust for under-coverage in the provisional quarterly Customs exports figure. Consultation between DGCI&amp;S is critical to this process.</p>	<p>(i) Implemented.</p> <p>(ii) Yet to be implemented.</p> <p>(iii) Implemented</p>
<p>Expert Committee for Improving the Quality of External Trade Data, 2008 (Chairman: Dr. S.K.Nath)</p>	<p>(i) There should be a monthly comparison of BoP data of the RBI with the customs data of the DGCI&amp;S to establish basic trends and detect significant variations, if any.</p>	<p>(i) To be implemented</p>

## CHAPTER IV: SERVICES, INCOME AND TRANSFERS

### ***Introduction***

4.1. The current account in India's BoP statistics distinguishes between merchandise and non-merchandise transactions and, accordingly, comprises two major heads — a “visible” (merchandise) account and an “invisibles” (non-merchandise) account. Invisibles, in turn, have three sub-categories, *viz.*, services, transfers and income.

4.2. Traditionally, a distinction is made between goods and services in the current account to take into account the differences in the nature of their production and international trade. While in the case of goods, international trade is conducted separately from production, in the case of services, the two are closely linked, as the production process of services involves a resident and non-resident. There may be exceptions as in the case of knowledge-based products such as computer software and other intellectual property products where they are traded separately from their process of production, like goods. In fact, the boundaries between goods and services sometimes get blurred; items classified as goods may include some element of services and *vice versa*. Notably, in the goods and services account of BoP, the valuation of goods includes transport within the exporting economy as well as wholesale and retail services which are indistinguishable from the price of goods. Similarly, the value of a few service items may include the values of some goods, as in the case of “travel”, “construction”, and “government goods and services, *n.i.e.* (not included elsewhere)”. Some services, particularly manufacturing services, maintenance and repair services, and freight transport also relate to goods.

4.3. As unprecedented growth in the volume of international trade in services necessitated changes in the treatment and classification of different transactions under the BoP, considerable disaggregation was progressively introduced over the years in the classification of international services transactions. As a general principle, the classification of services is mainly guided by the product-based system (except for travel, construction and government goods and services *n.i.e.* which are transactor-based), wherein the type of services rather than the type of unit-making provision for these services determines their categorisation. Many attempts have been made internationally to improve the coverage and classification of



services in recent years. OECD designed the Extended Balance of Payments Services (EBOPS) as an extension of the standard classification of services recommended in IMF's BPM5. It involved disaggregating the standard components of services recommended under BPM5 into sub-components which are of major economic importance. The United Nations' Manual on Statistics of International Trade in Services (MSITS), 2002 recommended the adoption of EBOPS. Accordingly, the IMF issued guidelines to its member countries to comply with EBOPS. The BPM6 further strengthened the concepts and classifications for greater harmonisation with other statistical systems. The BPM6 introduced changes in the measurement of financial services, such as insurance and pension services, and revised the treatment accorded to goods for processing and goods under merchanting. Consistent with the revised classification of services under BPM6, MSITS too has now recommended enhanced disaggregation of different types of services. This has been done to capture services transactions under all four modes of supply, namely, (i) cross-border supply, (ii) consumption abroad, (iii) commercial presence, and (iv) presence of natural persons. The broad mapping of standard components of services with the four modes of supply is given in Table IV.1 below.

<b>Table IV.1: Mapping of BoP Category of Services with Modes of Supply</b>	
Supply Mode	BoP Service Categories
<b>Mode 1</b> Cross-border supply	Transportation, communication services, insurance services, financial services, royalties and licence fees <b>Part of:</b> computer and information services, other business services, and personal, cultural and recreational services
<b>Mode 2</b> Consumption abroad	Travel (excluding goods bought by travellers)
<b>Mode 3</b> Commercial presence	Construction services
<b>Mode 4</b> Presence of natural persons	<b>Part of:</b> computer and information services, other business services, and personal, cultural and recreational services; labour-related flows (under supplementary information)
<i>Source:</i> Report of the Technical Group on Statistics of International Trade in Services, RBI, March 2002.	

4.4. The above table shows that most services categories under the BoP relate to Modes 1 and 2, while the other two modes of supply of services are partly covered. For instance, regarding Mode 3 (*i.e.*, commercial presence which concerns domestic operations of foreign affiliates), MSITS recommends the collection of certain additional statistics such as (i) Foreign Affiliate's Trade Statistics (FATS) covering the number of enterprises, value added,

sales, exports, imports, *etc.*; (ii) complete FDI statistics; and (iii) compilation of statistics on trade in services by the partner country. In India, these statistics are partially covered as part of the foreign collaboration survey conducted by the Reserve Bank.

4.5. With a view to aligning the BoP statistics with the SNA and the central product classification (CPC) and also to meet data requirements for international trade negotiations, transfers and income components have been clearly distinguished from services. Income flows between residents and non-residents have been segregated into two heads as “compensation of employees” and “investment income”. Similarly, “transfers” have also been disaggregated into “current transfers” (comprising workers’ remittances and general government transfers) and “capital transfers”, as a departure from the earlier practice. Concurrently, the current account of BoP has been redefined to exclude capital transfers, which are included in an expanded and renamed “capital and financial account”. This separate treatment of various items is introduced to strengthen the links between income and financial flows, on the one hand, and between BoP and IIP on the other, and thereby to increase the analytical usefulness of the international accounts.

4.6. With a view to further refining and widening the coverage of transfers, the BPM6 introduced new concepts for the measurement of international remittances by replacing “workers’ remittances” with “personal transfers” and showing workers’ remittances as an “*of which*” or supplementary item. Personal transfers is, thus, defined as consisting of all current transfers in cash or in kind made or received by resident households to or from non-resident households. Workers’ remittances are defined as current transfers made by employees to residents of another economy. Similarly, income is reclassified into “primary income” and “secondary income”. While “primary income” represents the return received for the contribution made to the production process (through the provision of labour, financial assets and renting of natural resources), “secondary income” captures the redistribution of income through current transfers that are effected by governments or charitable organisations.

4.7. A comparative picture of the standard components of services as between those recommended under BPM5 and BPM6 and those as per India’s BoP compilation is provided in Table IV.2. It may be observed from the table that BPM6 has continued with the broad framework of classification set out in BPM5, but has improved the classifications by taking into account changes in global production processes and the emergence of new financial

services. Thus, it has introduced two new categories of services, namely, “manufacturing services on physical inputs owned by others” and “maintenance and repair services”.

**Table IV.2: Mapping of Coverage of Services: BPM5, BPM6 and India's BoP**

	<b>BPM5/EBOPS</b>	<b>India's BoP @</b>	<b>BPM6</b>
1	Transportation Sea/Air/Other transport * Passenger/freight/other	Yes Yes (Article) Yes (BOPSY)	Same as BPM5 ^, but includes postal and courier services under all modes; Passenger further broken to payable by seasonal/border workers, etc.
2	Travel Business Seasonal and border workers/Others Personal Health/Education/Others	Yes Yes, FETERS (debit) No Yes, FETERS (debit) Yes, FETERS (debit)	Same as BPM5, but further break-up for business and personal in terms of goods, local transport, accommodation, food, and others
3	Communications services Postal and Courier (separately)/Telecommunications	Yes Yes (BOPSY)	<b>No separate category</b> Telecom clubbed with computer & information; Postal & courier with transportation separately
4	Construction services Abroad/in the compiling economy/services provided/purchases by construction companies	Yes (Only compiling economy)	Same as BPM5, but Construction Abroad/ and in the reporting economy only
5	Insurance services Life insurance & pension funding/freight/ reinsurance Other direct insurance/ auxiliary services	Yes Yes (except pension) Yes (FETERS)	<b>Insurance &amp; pension services ^</b> Direct insurance/ reinsurance/ auxiliary insurance/ pension and standardised guarantees
6	Financial Services Financial intermediation except investment banking/ investment banking and related services/ services auxiliary to financial intermediation	Yes Yes (FETERS) Yes (FETERS) Yes (FETERS)	Same as BPM5, but Explicitly charged and others/ and Financial intermediation services indirectly measured (FISIM) only
7	Computer and information services Computer services Information services <i>Of which</i> News agency/others	Yes (as software) No No Yes	<b>Telecommunications, computer and information services</b> (Separately only the three) Part of information
8	Royalties and licence fees Franchises and similar rights/Others	Yes Yes (FETERS)	Same as BPM5 ^, but <b>renamed as Charges for the use of intellectual property n.i.e</b>
9	Other business services Merchanting and other trade-related services/ Operational leasing services/ Misc. business, professional & technical services #	Yes Yes (Article) Yes (Article) Yes (Article)	Same as BPM5 ^, but Research and development/ Professional and management consultancy/ Technical, trade-related and other business services \$
10	Personal, cultural and recreational services Audiovisual and related services/ Other personal, cultural and recreational services <i>Of which</i> Educational/health/others	Yes Yes (FETERS) Yes (FETERS) No	Same as BPM5 ^ Same as BPM5 Same as BPM5 No
11	Govt. services n.i.e	Yes	Same as BPM5, but Govt. goods and services n.i.e ^
New	-	-	<b>Manufacturing services on physical inputs owned by others</b> -Goods for processing in reporting -Goods for processing abroad
New	-	-	<b>Maintenance and repair services n.i.e</b>
	<b>Total 11 Categories</b>	<b>Total 11 Categories</b>	<b>Total 12 Categories</b>

@: The current position of India is based on data availability as per either standard BoP presentations, or Invisibles Article in RBI Bulletin, or supply of data for the BOPSY of the IMF.

^: Further details in EBOPS as per MSITS Annex II.

\*: Other transport includes space, rail, road, inland waterways, pipeline and other auxiliary transport.

#: Miscellaneous business is further broken into legal, accounting and auditing, management consultancy, advertising, research and development, architectural and engineering, agricultural, mining and on-site processing, others and services between related parties.

\$: Instead two new categories, namely, "manufacturing services" and "maintenance and repair services n.i.e" are introduced in BPM6.

FETERS: Foreign Exchange Transactions Reporting System, BOPSY: Balance of Payments Statistics Yearbook.

## **Services Account**

### *Data Sources, Coverage and Compilation Method of Services in India's BoP*

4.8. Compilation of the Invisibles account in India's BoP follows the procedure recommended by RBI's "Technical Group on Statistics of International Trade in Services", 2002 (Chairman: Shri Deepak Mohanty). The Group recommended the adoption of standard components of services as per BPM5 as well as the EBOPS classification of services with suitable modifications to capture important items in India's international transactions in services. Accordingly, disaggregated data on services in India's current account of BoP in line with the standard format of BPM5 and EBOPS classifications is presented in the annual article in the RBI Bulletin titled "Invisibles in India's Balance of Payments: An Analysis of Trade in Services, Remittances and Income" and the same data are also supplied to the IMF for the Balance of Payments Statistics Yearbook (BOPSY).

### *Data Sources*

4.9. As part of the administrative requirements under the Foreign Exchange Management Act (FEMA, 1999), AD branches that are authorised to deal in foreign exchange need to report to the RBI all foreign exchange transactions put through by them on a fortnightly basis. The reporting is done in the manual (paper) as well as the electronic mode. Manual reporting in the form of "R-Return" is a statutory requirement and contains broad totals relating to foreign exchange transactions. Electronic reporting, which is far more detailed as per purpose-wise codes, is made through FETERS. Under FETERS, foreign exchange transactions for both receipts and payments giving the break-up of purpose (receipt purpose code beginning with the letter *P* and payments purpose code beginning with the letter *S*), transaction date, currency, amount, *etc.* are reported to the RBI. The detailed list of the purpose codes used to report forex transactions is given in Attachment III. All transactions relating to exports, non-exports, imports, non-imports, intermediary exports, and intermediary imports are reported under FETERS. However, individual non-export receipts of value below Rs. 5 lakh are not reported separately. All transactions below this threshold are aggregated and reported in a lump sum. Internationally too, such practices of fixing a bench-mark for collection of data are not uncommon.

4.10. The purpose-wise details of the transactions involved in the amount reported in the lump sum, which are called unclassified receipts, are estimated on the basis of surveys so as to minimise the processing cost and reduce the reporting burden for ADs. As per the recommendations of the Technical Group on Statistics of International Trade in Services, the Unclassified Receipt Survey (URS) is being conducted more frequently, and only critical branches which report non-export receipts of at least Rs.5 crore in a year are covered. Further, as the unclassified receipts comprise “foreign currency” receipts as well as “rupee receipts”, samples of branches are drawn separately for “Foreign Currency Receipts” and “Rupee Receipts”, as the coverage of purposes under these two categories could be significantly different. These selected AD branches are required to report purpose-wise details of all individual receipts under Rs.5 lakh for two days randomly selected in a fortnight. The survey details are submitted by the AD branches to the RBI along with other data files through FETERS on a fortnightly basis. Based on the survey receipts, the total unclassified receipts are distributed over various purposes under services, income and transfers.

4.11. Under the FETERS system, AD branches submit the following five files to the RBI electronically, either through mail or on a floppy on a fortnightly basis:

(i) **BoP file:** This file consists of purpose-wise disaggregated information on trade in services, goods, transfers and income; those involving financial claims on and liability to the rest of the world and those classified as transfers, which involve offsetting entries to balance the one-sided transactions. All individual transactions pertaining to export, import, non-export, non-import, intermediary export and intermediary import are reported in the BoP file. As stated above, in the case of non-export receipts, all transactions equivalent to or above Rs. 5 lakh are reported individually in the BoP file and those of value below Rs. 5 lakh are reported in a lump sum.

(ii) **ENC file:** Transactions related to exports are reported in this file based on the documents submitted by the exporters to ADs for collection /negotiation /discount /purchase of the export bills. The data captured in this file are based on the negotiation date and not the shipment date.

(iii) **QE file:** This file contains currency-wise consolidated figures of exports, non-exports, imports, non-imports, intermediary exports, intermediary imports, inter-bank transactions, opening balances and closing balances.

(iv) **URS file:** This file reports the findings of the unclassified receipt survey (URS), giving the proportion of different purposes and enabling the distribution of unclassified receipts reported in lump sum over various components of services, income and transfers.

(v) **Schedule3 to Schedule6 file:** In this file, realised transactions related to exports are reported. This is useful from the point of view of reconciling the exports based on shipments and actual exports proceeds received. In fact, the Foreign Exchange Department relies on this statement to monitor the realisation of exports proceeds.

4.12. Of the five files submitted by ADs, the QE file and Sch.3 to Sch.6 files are not used for BoP compilation, but are used only for monitoring purposes. Since the item-wise total of transactions given in the BoP file agree with the corresponding item of QE totals, QE data reported through FETERS enables a consistency check. For compilation of data for BoP purposes, the BoP file and URS file along with the quick estimates generated from R-returns are used<sup>4</sup>.

### *Coverage and Compilation Methods*

4.13. In India's standard BoP format, trade in services comprises commercial services categorised into transportation, travel, insurance, government services not included elsewhere (GNIE) and other commercial services under the head "miscellaneous services". Miscellaneous services comprises the following sub-categories: communication, construction, financial services, software services, news agency services, royalties, copyright and licence fees, business services, personal, cultural and recreational services, and others. This classification of miscellaneous services along with the details of "Business services", though not disseminated individually in the standard presentation of India's BoP, are published in the Invisibles articles in the RBI Bulletin, which are also provided to the IMF for the BOPSY. The details of the sub-categories of services as recommended in the BPM6 and

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<sup>4</sup> With the stabilisation of the FETERS system by 2004, banks now need to submit only the consolidated R-Return rather than individual bank branch-wise statements.

the Indian practice in terms of coverage, classification and presentation with respect to different components of services are discussed below.

## Transportation

4.14. “Transportation” records receipts and payments on account of the carriage of goods and natural persons from one location to another as well as related supporting and auxiliary services. In the standard classifications of the IMF, transport is classified in both dimensions—modes of transport (sea, air or others) and carriages (passengers/freight). Further, the BPM6 has suggested including postal and courier services in transportation and recommends its break-up under all the modes.

4.15. In India, transportation accounts represent receipts from transportation of India’s exports or payments for freight separately paid on imports; receipts include receipts of Indian steamship/ airline companies in respect of third-country trade (cross-trade) and passage fare earnings for carrying foreign travellers in India’s ships and planes or passage fares paid by Indian residents to foreign shipping and airline companies for their international travel. More specifically, transportation credit (receipts) covers: (i) estimated freight included in exports (ii) receipts of surplus freight/passenger fare by Indian shipping as well as Indian airline companies operating abroad; (iii) purchases on account of operating expenses of foreign shipping and foreign airline companies operating in India; (iii) purchases on account of operational leasing (with crew) of shipping and airline companies; and (iv) receipts on account of other transportation services (stevedoring, demurrage, port-handling charges, *etc.*).

4.16. On the other hand, transportation debit (payments) includes: (i) payments for surplus freight/ passenger fare by foreign shipping and airline companies operating in India; (ii) payment for operating expenses of Indian shipping and airline companies operating abroad; (iii) freight on imports and exports of shipping and airline companies; (iv) operational leasing (with crew) of shipping and airline companies; (v) booking of passages abroad by shipping and airline companies; and (vi) payments on account of stevedoring, demurrage, port-handling charges, *etc.* The freight and insurance on exports are estimated based on the results thrown up by a survey conducted by the RBI. According to this survey, the share of freight and insurance on exports comes to 3.8 per cent and 0.5 per cent, respectively. As freight and passengers are clubbed together in the FETERS purpose code, for EBOPS the bifurcation of



transportation services between passengers and freight is based on the assumption that all passenger traffic is through air, while transportation of all goods is by the sea route. For full compliance with international best practices (BPM6), two separate purpose codes under FETERS need to be introduced for passengers and freight. Further, estimates on freight need to be updated through regular surveys.

## Travel

4.17. Travel differs from other components of international services because it is a demand-oriented activity — the traveller moves to another territory (the economy visited) to acquire the goods and services. Thus, unlike other services, travel is not a specific type of service but a mixture of goods and services consumed by travellers and, therefore, it is not identified as a service in the CPC. However, travel is included as part of services in the BoP statistics. Stays of any length are considered as travel, provided there is no change of residence.

4.18. According to BPM6, travel credits cover goods and services for own use or to give away those goods acquired from an economy by non-residents during their visit. Travel debits cover goods and services for own use or to give them away in their own economy. Travel excludes goods for resale, which are included in general merchandise. Travel also includes goods or services acquired by persons while undertaking study or medical care outside their territory of residence. It excludes the acquisition of valuables (such as jewellery), consumer durable goods (such as cars and electronic goods), and purchases of other consumer articles for own use or to give away that are included in customs data in excess of customs thresholds; they are included in general merchandise. Travel includes local transport (*i.e.*, transport provided by a resident within the economy being visited), but excludes international transport (which is included in passenger services under transportation).

4.19. Travel is broken down into two standard components — business and personal travel. According to BPM6, business travel includes “the goods and services acquired for personal use by persons whose main purpose of travel is for business (including goods and services for which business travellers are reimbursed by employers) but not the sales or purchases that they may conclude on behalf of the enterprises they represent”. Government employees and employees of international organisations on official travel are distinguished from employees

stationed or living, respectively, in the country (in which case their purchases are included in GNIE).

4.20. Personal travel covers “goods and services acquired by persons going abroad for purposes other than business, such as vacations, participation in recreational and cultural activities, visits with friends and relations, pilgrimage, and education and health-related purposes”. The most common heads of travel expenses are goods, food and beverages, local transport, accommodation, and other services consumed within the economy visited. The BPM6 recommends a further break-up of personal travel into health-related, education-related and other personal travel.

4.21. In India, “travel” represents all expenditure by foreign tourists in India on the receipts side and all expenditure by Indian tourists abroad on the payments side. Accordingly, receipts under travel include: the purchases of foreign exchange by ADs from clients towards travel (including purchases of foreign TCs, currency notes *etc.* over the counter by hotels, hospitals, emporia, educational institutions, *etc.*) as well as the amount received by TT/SWIFT transfers or debit to Non-Resident accounts. The travel receipts (credit) reported under FETERS by the ADs are inadequate to the extent that they do not capture all types of inward remittances on account of travel. Therefore, travel receipts at present are estimated based on data on tourist arrivals available from the Ministry of Tourism, Government of India multiplied by the estimated per capita expenditure of foreign tourists. It may, however, be noted that this does not change the total receipts reported through all purposes under FETERS and, hence, the adjustment takes place in “other miscellaneous services” receipts so as to keep the grand total receipts reported under FETERS unaltered. Apart from introducing new purpose codes on the receipts side under FETERS to capture health- and education-related as well as personal travels individually, there may be a need for surveys on foreign tourist spending in India to better capture travel services. On the debit side, however, detailed purpose codes on travel payments are available — which include payments for business travel, travel under basic travel quota, pilgrimage, medical treatment, education and other travel, including international credit cards.

## Telecommunications, Computer and Information Services

4.22. The latest IMF Manual has re-classified the category “Telecommunications, Computer and Information Services” by merging “Telecommunications”, which is a part of “Communications services”, with “Computer and Information services”. The other part of “Communications services”, that is, “Postal and Courier services” has been included under transportation services as a separate item. The basic principle followed by the IMF in re-grouping the above services is that computer and telecommunications services are defined in terms of the nature of the service and not by the method of delivery. Accordingly, computer services consist of hardware- and software-related services and data-processing services, while information services includes news agency services such as the provision of news, photographs, and feature articles to the media. “Other information provision services” includes (i) database services in the form of database conception, data storage, and the dissemination of data and databases provided either online or through magnetic, optical or printed media and (ii) services provided through web search portals.

4.23. As per the current practice of BoP compilation and presentation in India, “telecommunications, computer and information services” are not presented as a single category as suggested by BPM6. Rather, in India’s standard BoP formats, “communication”, “software” and “news agency” services are shown separately. Data on credit and debit in respect of each of these items are reported through FETERS. “Communication services” includes postal, courier, and satellite services, apart from telecommunications services. “Software services” receipts (credit) corresponds to “computer services” and includes (i) hardware consultancy and implementation, (ii) software consultancy and implementation, (iii) database and data processing charges, and (iv) repair and maintenance of computers and software. The category of “News agency services” includes news agency services and other information services, such as subscription to newspapers and periodicals.

4.24. With regard to “computer services” (software services), for the purpose of BoP compilation, instead of FETERS data on “software services” receipts, data sourced from NASSCOM, which include both IT services and ITES-BPO services, are used, while on the debit side it reflects the payments captured through the FETERS purpose codes under the category “computer and information services”. This is done in view of full coverage under NASSCOM and inadequate reporting of data on software services under FETERS as some of

the IT-enabled services are reported to have been covered under miscellaneous receipts. It may, however, be noted that the use of alternative sources of data does not change the purpose-wise totals reported under FETERS and, hence, the necessary adjustment takes place in “other miscellaneous services” to ensure that the aggregate receipts reported under FETERS are not changed.

4.25. Moving away from the present practice of presentation to comply with the BPM6 standard would require: (i) fully switching to banking channel data on receipts and payments reported through the FETERS purpose codes for software services, and using industry sources (*i.e.*, NASSCOM) data only for validation purposes; (ii) appropriately classifying “communication services” by taking out postal and courier services, and including them as part of transportation services, and (iii) combining “news agency services”, “other information services” and “database and data processing charges” available under FETERS on both the receipts and payments sides to arrive at “information services”.

4.26. In the interim, there is a need to reconcile the two sources of data (NASSCOM and FETERS) on software services. Further, since NASSCOM data, available on an annual basis, are used for BoP compilation at present, there is a need to get the quarterly break-up of the same from NASSCOM for compilation of quarterly BoP. Apart from quarterly data, country-wise and purpose-wise break-up of software exports are also important from the perspective of trade negotiations.

### **Construction Services**

4.27. The category of “Construction services” covers work, generally of a short-term nature, performed on construction projects and installations by employees of an enterprise in locations outside the economic territory of the enterprise. According to the latest IMF Manual, construction covers “the creation, renovation, repair, or extension of fixed assets in the form of buildings, land improvements of an engineering nature, and other such engineering constructions as roads, bridges, dams, *etc.*”. Construction also includes related installation and assembly work as well as management of construction projects. Goods and services acquired by the enterprises undertaking the construction work from residents at the location of the construction work are also recorded under “construction”. Construction services are further disaggregated into construction abroad and construction in the compiling

economy to facilitate recording them on a gross basis, *i.e.*, including goods and services used as inputs to construction work as well as other costs of production and the operating surplus accruing to the contractor.

4.28. In India, at present, receipts on construction services include receipts (credit) on account of goods and services acquired in India from resident enterprises by non-resident construction enterprises, whereas payments include construction of projects abroad by Indian companies including import of goods at the project site and payments for cost of construction, *etc.* of projects executed by foreign companies in India. Thus, on the credit side the coverage is inadequate and does not capture receipts on account of construction projects undertaken by Indian companies abroad. This would require introducing a new purpose code in FETERS on the receipt side.

### **Insurance and Pension Services**

4.29. The latest IMF Manual has re-classified the existing category “insurance services” as “insurance and pension services” to adequately capture the growth of pension services. Insurance services cover the provision of various types of insurance to non-residents by resident insurance enterprises and *vice versa*. According to the Manual, insurance and pension services include services of providing life insurance and annuities, non-life insurance, reinsurance, freight insurance (*i.e.*, insurance on goods that are in the process of being exported or imported), pensions, standardised guarantees, and auxiliary services to insurance, pension schemes, and standardised guarantee schemes. The Manual suggests further break-up of insurance and pension services into direct insurance, reinsurance, auxiliary insurance services, and pension and standardised guarantee services.

4.30. In India’s BoP statistics, credit under “insurance services” includes receipts on account of freight insurance (*i.e.*, relating to import and export of goods), premium on life and non-life policies, reinsurance premium from foreign insurance companies as well as receipts on account of settlement of claims and auxiliary services (*i.e.*, commission on insurance). The reverse holds good for debit under “insurance services” for these purposes. Thus, the FETERS purpose codes on both the receipts and payments sides adequately capture the insurance services under BPM6. However, pension services are not covered separately at present and, therefore, full compliance with BPM6 standards would require introduction of

separate purpose codes for pension and standardised guarantee services on both the receipts and payments sides.

## Financial Services

4.31. Financial services cover financial intermediary and auxiliary services (except insurance and pension funds services) conducted between residents and non-residents. According to the latest IMF Manual, these services include those usually provided by banks and other financial corporations such as deposit taking and lending, letters of credit, credit card services, commissions and charges related to financial leasing, factoring, underwriting, and clearing of payments. This category also includes other services such as financial advisory services, custody of financial assets or bullion, financial asset management, monitoring services, liquidity provision services, risk assumption services other than insurance, merger and acquisition services (like hedging), credit-rating services, stock exchange services, and trust services.

4.32. Financial services exclude pure interest (which represents the return on investment and, hence, are part of primary income; for instance, interest on NRI deposits in India is included as inflows in the capital account with a contra entry in the investment income payments in the current account), dividends, life insurance and pension services, other insurance services, non-financial advisory services provided by banks (which are included under other business services), and holding gains and losses on purchases and sales of financial instruments (which are treated as revaluation as they arise from changes in their prices and/or the exchange rates and do not represent transactions).

4.33. In India's BoP compilation and standard presentation at present, financial services includes financial intermediation services (*viz.*, bank charges, collection charges, LC charges, cancellation of forward contracts, commission on financial leasing, *etc.*), investment banking services (*viz.*, brokerage, under-writing commission, *etc.*) and auxiliary services (*viz.*, charges on operation & regulatory fees, custodial services, depository services, *etc.*) on both the receipts (credit) and payments (debit) side. Thus, India's BoP compilation of financial services largely conforms to international standards except for risk assumption services like hedging and other financial derivatives, which are not covered. Moreover, there is a need to

cover financial intermediation services indirectly measured (FISIM) to conform fully to international classifications.

### **Charges for the Use of Intellectual Property n.i.e**

4.34. The latest IMF Manual has introduced a new category of services named “Charges for the use of Intellectual Property n.i.e” to replace the existing category of “Royalties and licence fees” under BPM5, although the underlying classifications are the same. As per the Manual, “charges for the use of intellectual property n.i.e. include: (a) charges for the use of proprietary rights (such as patents, trademarks, copyrights, industrial processes and designs including trade secrets, franchises), and (b) charges for licences to reproduce and/or distribute intellectual property embodied in produced originals or prototypes (such as copyrights on books and manuscripts, computer software, cinematographic works, and sound recordings) and related rights (such as for live performances and television/ cable/ satellite broadcast)”.

4.35. In India’s BoP statistics, transactions relating to intellectual property rights are covered under “royalties and licence fees”, which is shown separately under the miscellaneous account in the Invisibles article in the RBI Bulletin. There are two purpose codes for “royalties and licence fees” under FETERS on both the receipts and payments sides — one for franchisee services covering patents, copyrights, trademarks, industrial processes, franchises *etc.* and the other for the use of licensing arrangements of produced originals or prototypes (such as manuscripts and films). Therefore, compliance with the best international standards would only require renaming the existing category of services.

### **Other Business Services**

4.36. As per BPM5, “other business services” provided by residents to non-residents and *vice versa* covers merchanting and other trade-related services; operational leasing services; and miscellaneous business, professional, and technical services. The grouping was part of harmonisation efforts by the IMF and other international organisations involved in the expansion and improvement of data on international service transactions. As per the latest IMF Manual on BoP (BPM6), “other business services” are classified under three broad heads: Research and development services, Professional and management consultancy services and Technical, trade-related and other business services. Moreover, merchanting

services are treated as part of “goods under merchanting” rather than under services as discussed in Chapter III.

4.37. In India’s BoP statistics, these “other business services” are presented as “business services” in the standard format and are adequately covered under the appropriate heads as FETERS provides the necessary details on both the receipts and payments sides. On both the credit and debit side, the category “business services” includes trade-related services (*i.e.*, commission on exports and imports); operational leasing services; merchanting services; legal services; accounting, auditing, book keeping and tax consulting services; business and management consultancy and public relations services; advertising, trade fair, market research and public opinion polling services; research & development services; architectural, engineering and other technical services; agricultural, mining and on-site processing services; inward remittances for maintenance of offices in India; and environmental services. However, merchanting services, which at present are part of business services, have to be re-classified and appropriately included, with suitable descriptions, under “goods under merchanting” as per the latest IMF Manual (for details, see Chapter III). Moreover, it would only require some reclassification to conform to the standard presentation under the three heads as suggested in BPM6.

### **Personal, Cultural, and Recreational Services**

4.38. According to BPM6, personal, cultural, and recreational services cover (i) audiovisual and related services and (ii) other personal, cultural and recreational services provided by residents to non-residents and *vice versa*. Audiovisual and related services comprise services and fees related to the production of motion pictures (on film, videotape, disk, or transmitted electronically, *etc.*), radio and television programmes (live or on tape), and musical recordings. Other personal and cultural services are classified as health services, education services, and others. Health services comprise services provided by hospitals, doctors, nurses, and paramedical and similar personnel, as well as laboratory and similar services, whether they are rendered remotely or on-site. However, health services provided to non-residents at the time when they are present in the territory of the service provider are included under travel.



4.39. In India's BoP statistics, "personal, cultural and recreational services" are broadly covered under the head "miscellaneous services", but shown separately in the Invisibles article. This category, both under credit and debit, covers "audiovisuals and related services" (*i.e.*, services and associated fees related to the production of motion pictures, rentals, fees received by actors, directors, producers and fees for distribution rights) and "other personal, cultural services" (*i.e.*, those related to museums, libraries, archives and sporting activities and fees for correspondence courses of Indian universities/institutes). Since separate codes for sub-categories are not available under FETERS, the data are at present published only at the aggregate level. Therefore, new purpose codes need to be introduced under FETERS to extract the necessary information. At the same time, it is important to explore the possibility of getting such disaggregated information on health and education services (other than those included under Travel) from the respective Ministries.

#### **Government Goods and Services Not Included Elsewhere (G.n.i.e)**

4.40. The standard BoP format has a category "Government goods and services not included elsewhere (G.n.i.e)" which covers all goods and services (such as expenditures of embassies and consulates) associated with government sectors or international and regional organisations and not classified under other items. The supply of goods and services to embassies, consulates, military units or bases, defence agencies, and other official entities is included as G.n.i.e credits, while the acquisition of goods and services by such entities of the government of the compiling economy in other territories are included as G.n.i.e debits. Charges for visas and other services provided by embassies and consulates, supply and purchase of goods and services by international organisations and acquisition of goods and services for joint military arrangements, peacekeeping forces, and other services, such as those provided by the United Nations, are also included under G.n.i.e.

4.41. In India's BoP statistics, G.n.i.e receipts represent inward remittances towards maintenance of foreign embassies and diplomatic missions, and offices of international/regional institutions in India, while G.n.i.e. payments record remittances on account of maintenance of Indian embassies and diplomatic missions abroad and remittances by foreign embassies on their account.

## Manufacturing Services on Physical Inputs Owned by Others

4.42. This new category of services introduced in BPM6, as noted earlier, covers processing, assembly, labelling, packing, *etc.*, undertaken by enterprises that do not own the goods concerned (*i.e.*, processor) and, hence, only the fee charged by the processor to the owner is included under this item. As the ownership of the goods does not change in these cases, in none of these cases is the general merchandise transaction recorded between the processor and the owner. Thus, manufacturing services on physical inputs owned by others refers to all work done on goods by a resident of an economy for the owner of goods who is a non-resident (*i.e.*, a resident in another economy). The treatment of these services does not depend on whether or not the goods were previously or subsequently in the physical possession of the owner. Examples include oil refining, liquefaction of natural gas, assembly of clothing and electronics, assembly (excluding assembly of prefabricated constructions, which is included under construction), labelling, and packing (excluding that incidental to transport, which are included in transport services). The BPM6 points out that the value of goods (received for processing and dispatched after processing) could be reported either by the customer or supplier of manufacturing services, or sourced from customs data. It further suggests a bifurcation between goods for processing in the reporting economy and goods for processing abroad.

4.43. India's BoP statistics do not cover this item at present. Implementation of this category of services in the Indian context would require introducing a new purpose code on both the receipts and payments sides, with suitable descriptions, under FETERS reporting by ADs.

## Maintenance and Repair Services n.i.e

4.44. This is the second new category of services introduced in BPM6 to take into account the changing nature of production processes. This covers maintenance and repair work by residents on goods that are owned by non-residents and *vice versa*. It includes repairs whether performed at the site of the repairer or elsewhere. Repairs and maintenance on ships, aircraft, and other transport equipment are included in this category. Cleaning of transport equipment is not included in this item but is included in transport services. Construction maintenance and repairs (included under construction services) and maintenance and repairs of computers

(included under computer services) are excluded from this category. The value recorded for maintenance and repairs captures the value of the work done and not the gross value of the goods before and after repairs. As per the BPM6, goods leaving from, arriving in, and returning to a territory for repair, processing, or other activity without a change of ownership are excluded from general merchandise.

4.45. At present, India's BoP does not cover this item. In India, a new purpose code on both the receipts and payments sides may be required to capture exclusively "maintenance and repair services n.i.e" under FETERS reporting by ADs.

### ***Income: Primary Income***

4.46. The details of the standard components of primary income as recommended in the BPM6 and Indian practice in terms of coverage, classification and presentation is discussed below.

4.47. Earlier (in BPM5), the income head covered two types of transactions between residents and non-residents: (i) those involving compensation of employees, which is received from or paid to non-resident workers (*e.g.*, border, seasonal, and other short-term workers of less than one year), and (ii) those involving investment income receipts and payments on external financial assets and liabilities. As per the latest BoP manual (BPM6), these two types of incomes that are associated with the production process are regrouped as primary income account. Thus, primary income represents the return that accrues to institutional units for their contribution to the production process (*e.g.*, compensation of employees) or for the provision of financial assets (investment income) and renting natural resources to other institutional units (property income). Taxes and subsidies on products and production are also accounted for as income related to production, and categorised as "other primary income".

4.48. According to BPM6, compensation of employees represents total remuneration (in cash or kind) in return for the contribution of labour inputs to the production process by an individual in an employer-employee relationship with the enterprise. Compensation of employees has three main components: (i) wages and salaries in cash, (ii) wages and salaries in kind, which also include foregone interest and allocation of shares to employees like

employee stock options (ESOPs) and (iii) employers' social contributions. Investment income is the return for providing financial assets and consists of dividends and withdrawals from income of quasi-corporations, reinvested earnings, and interest. The investment income account includes receipts and payments on direct investment, portfolio investment, other investment, and receipts on reserve assets. Property income represents the return for providing financial assets and renting natural resources.

4.49. In India's BoP statistics, "investment income" together with "compensation of employees" constitutes the "income account", which is in line with international best practices. "Compensation of employees" received from (credit) or paid to (debit) non-residents is being shown under the head of "income" with effect from 1997-98, which was earlier recorded under the head "Services – miscellaneous".

4.50. Transactions relating to investment income are in the form of interest, dividend, profit and others for servicing of capital transactions. Interest payments represent servicing of debt liabilities, while dividend and profit payments reflect the servicing of non-debt (FDI and portfolio investments) liabilities. Investment income receipts (credit) comprise interest received on loans to non-residents; dividend/profit received by Indians on foreign investment; reinvested earnings of Indian FDI companies abroad; interest received on debentures, floating rate notes (FRNs), Commercial Papers (CPs), fixed deposits and funds held abroad by ADs out of foreign currency loans/export proceeds; payment of taxes by non-residents/refunds of taxes by foreign governments to residents; interest/discount earnings on RBI's investment of its foreign currency assets (FCAs) abroad; and interest/remuneration on SDRs holdings.

4.51. Investment income payments (debit) comprise payment of interest on non-resident deposits and interest on banks' overseas borrowings; payment of interest on loans from non-residents such as ECB, external assistance and interest on short-term credits including non-IOC short-term trade credit; payment of dividend/profit to non-resident shareholders; reinvested earnings of FDI companies in India; payment of interest on debentures, FRNs, CPs, fixed deposits, government securities, and charges on SDRs; interest paid on overdraft on Vostro account and overdraft on Nostro accounts; and payment of taxes by Indians/refund of taxes by the government to non-residents.

4.52. The major sources of data are from FETERS on both the receipts and payments sides, except for reinvested earnings and interest and discount on FCAs and interest on SDRs. Data on reinvested earnings of Indian companies abroad (investment income receipts) are sourced from the Annual Performance Report (received from the regional offices of the Foreign Exchange Department of the RBI), while data on reinvested earnings of FDI companies in India (investment income payment) are extracted from the Annual Survey of Foreign Liabilities and Assets (conducted by DSIM). Payments of reinvested earnings of unincorporated bodies (foreign banks in India) are culled from the balance sheets (*i.e.*, reserves and surplus) of foreign banks operating in India (from the Banking Research Division, DEPR, RBI). Data on interest and discounts earned on FCAs and interest received or paid by India to the IMF in SDRs are obtained from the Department of External Investment and Operations of the Reserve Bank.

### ***Transfers: Secondary Income***

4.53. Details of the standard components of secondary income as recommended in the BPM6 and Indian practice in terms of coverage, classification and presentation are discussed below.

4.54. According to BPM6, primary income (that entails allocation of income as defined above) is distinguished from secondary income; the latter captures the process of redistribution of income through current transfers between residents and non-residents (for example, by governments or charitable organisations). According to BPM6, a transfer is “an entry that corresponds to the provision of a good, service, financial asset, or other non-produced asset by an institutional unit to another institutional unit when there is no corresponding return of an item of economic value”. Transfers may be made in cash (which involves payment of currency or transferable deposits) or in kind (which involves transfer of ownership of a good or asset or the provision of a service). Transfers do not generally arise between commercial entities. A distinction is made between current and capital transfers in the BoP accounts. Current transfers directly affect the level of disposable income and influence the consumption of goods and services. Capital transfers, on the other hand, do not affect disposable income and, hence, are recorded in the capital account.

4.55. According to the broadened definition in BPM6, personal transfers constitutes all current transfers in cash or in kind made or received by resident households to or from non-resident households, independent of the source of income of the sender and the relationship between the households. Whether remittances made by workers abroad are to be treated as “compensation of employees” or “personal transfers” and classified under primary or secondary income account is determined by the residence status of the person (employee) concerned. It would be treated as personal transfers in the case of workers who are residents of the economy in which they are employed (which is generally determined by the length of stay or expected stay for a year or more). According to the residence status, workers staying abroad for *less than a year* are termed “cross-border workers” or “seasonal workers” or other short-term workers entrusted with a special task; remittances in this category are classified as “compensation of employees” and are recorded as part of the primary income account.

4.56. According to BPM6, “funds sent abroad by individuals who are residents in the economy in which they are employed, self-employed, or operating a business, for the purpose of making a deposit in his or her own account with a bank located abroad, represent a financial investment, which is recorded in the financial account, rather than as a personal transfer. But any withdrawals (locally) to provide resources to a relative or another person (without a *quid pro quo*) are recorded as a personal transfer”.

4.57. There is a subtle distinction between current and capital transfers. Current grants are in cash or in kind made by governments or international organisations to other institutional units, which results in an increase in income and consumption in the recipient economy, while investment grants are capital transfers for financing all or part of the costs of acquiring fixed assets. A transfer of cash is termed a capital transfer when it is linked to, or conditional on, the acquisition or disposal of a fixed asset by one or both parties to the transaction (*e.g.*, an investment grant). In other words, current transfers consist of all transfers that do not involve (i) transfers of ownership of fixed assets; (ii) transfers of funds linked to, or conditional upon, acquisition or disposal of fixed assets; or (iii) forgiveness, without any counterparts being received in return, of liabilities by creditors. All of these transfers in kind are termed capital transfers. The BPM6 suggests further classification of current transfers based on the institutional sectors receiving or providing the transfers in the compiling economy into two main categories: (i) general government and (ii) other sectors, which includes personal transfers (*e.g.*, workers’ remittances) and other current transfers (*e.g.*,

current taxes on income and wealth, contributions to social security schemes and benefits payable under social security and pension schemes, net non-life insurance premium, non-life insurance claims, *etc.*).

4.58. In India's BoP, transfers (private and official) represent one-sided transactions, *i.e.*, transactions that do not have any *quid pro quo*, such as grants, gifts, and migrants' transfers by way of remittances for family maintenance, repatriation of savings and transfers of financial and real resources linked to a change in the resident status of migrants. Official transfer receipts include grants, donations and other assistance (including PL-480 Title II) received by the government from bilateral and multilateral institutions. Similar transfers by the Indian government to other countries are recorded under official transfer payments. Data on external assistance (direct settlement and reimbursement) are sourced from the Controller of Aid, Accounts and Audit (CAAA) and the US Embassy in New Delhi (for grants under PL-480). Similar transfers by Government of India to other countries such as contributions/donations to international institutions (reported under FETERS) and transfers for technical and economic co-operations (sourced from Union Budget - Annual Financial Statement) are recorded under official transfer payments.

4.59. Private transfer receipts include (i) remittances for family maintenance, (ii) local withdrawals from Non-Resident Rupee Accounts (NRE and NRO), (iii) gold and silver brought through passenger baggage, and (iv) personal gifts/ donations to charitable/religious institutions. On the other hand, private transfer payments include remittances by non-residents towards (i) family maintenance and savings and (ii) personal gifts/ donations to charitable/religious institutions. The inflows from overseas Indians for deposits in NRI deposit schemes are treated as capital account transactions. However, local withdrawals/redemptions from NRI deposits (especially NRE and NRO rupee deposit schemes) are treated as forming part of private transfers.

4.60. Data on family maintenance and personal gifts/donations to charitable/religious institutions are captured through the FETERS purpose codes on both the receipts and payments sides, while local withdrawals are extracted from the STAT-8 returns. Data on gold and silver brought through passenger baggage are obtained from the DGCI&S.

4.61. In order to comply fully with the BPM6 standards of presentation on income and transfers, the various items covered under these heads at present need to be classified appropriately under the heads of primary income (covering investment income and compensation of employees) and secondary income (which deals with redistribution of income through current transfers, such as personal transfers and grants), which are current in nature, and received under external assistance.



## Chapter V: Capital and Financial Account

5.1. The capital and financial account of the BoP in the BPM5 is divided into two main categories namely, capital account and financial account. The capital account covers all transactions that involve receipts or payments of capital transfers and acquisition or disposal of non-produced non-financial assets. The financial account covers all transactions associated with changes of ownership in the foreign financial assets and liabilities of an economy. Such changes include the creation and liquidation of claims on, or by, the rest of the world. All changes that do not reflect transactions, such as valuation, reclassification and other adjustments are excluded from the capital and financial accounts. The BPM6 further states that not only “capital account” and “financial account” be separately presented but also suggests that capital account transactions be recorded on a gross basis, while financial account transactions (which also include reserve assets) be recorded on a net basis. The concepts and coverage under the “capital account” and “financial account” of BoP as recommended by the IMF Manual are discussed below:

### ***Capital Account***

5.2. According to BPM6, the capital account comprises capital transfers receivable and payable between residents and non-residents, and the acquisition and disposal of non-produced non-financial assets between residents and non-residents.

5.3. The recording of acquisition and disposal of non-produced non-financial assets and capital transfers receivable and payable are done separately on a gross basis, rather than on a net basis. Gross data are quite significant for cross-border analysis and facilitate the derivation of net flows. The recording of acquisition and disposal of non-produced non-financial assets is carried out at the time of change of ownership. Capital transfers are recorded on the fulfilment of all requirements and conditions for receiving them, with the receiving unit having an unconditional claim; however, its determination becomes complex if there is a wide variety of eligibility conditions that have various legal connotations/powers.

## Acquisition and Disposal of Non-produced Non-financial Assets

5.4. Non-produced non-financial assets include: (i) natural resources; (ii) contracts, leases, and licences; and (iii) marketing assets (and goodwill).

5.5. *Natural resources* consist of land, mineral rights, forestry rights, water, fishing rights, air space, and electromagnetic spectrum. International transactions in land arise when land for enclaves of international organisations and foreign governments is acquired or disposed. In the case of voluntary changes of sovereignty over a particular area, whether for a payment or as a transfer, international transactions deem to have occurred.

5.6. *Contracts, leases, and licences* include those contracts, leases, and licences that are considered economic assets. These assets, which are creations of society and its legal system, are sometimes called intangible assets, *e.g.*, marketable operating leases, permissions to use natural resources that are not recorded as outright ownership of those resources, permissions to undertake certain activities (including some government permits), and entitlements to purchase a good or service on an exclusive basis. Though transactions in these assets are recorded in the capital account, holdings of these assets are not recorded in the IIP as there is no counterpart liability. A marketable operating lease, which can be transferred or sub-leased, may only be treated as an asset when the lease specifies a predetermined price for the use of an asset that differs from the price at which the asset could be leased for. In a scenario where the lessee sells the right and realises the price difference, marketable operating lease asset flows are recorded in the capital account.

5.7. *Marketing assets* include items such as brand names, mastheads, trademarks, logos, and domain names. In a situation where they are sold separately from the entity that owns them, they are recorded as acquisitions and disposals of non-produced non-financial assets. Internet domain names are recognised as a marketing asset in some cases, especially when they command a premium value. Similarly, the fee for designing a new logo is considered a business service, while an amount paid for acquiring an existing logo would be included under marketing assets. Marketing assets would also include the sale of franchises or trademarks.

## Capital Transfers

5.8. According to BPM6, “capital transfers are transfers in which the ownership of an asset (other than cash or inventories) changes from one party to another; or which oblige one or both parties to acquire or dispose of an asset (other than cash or inventories); or where a liability is forgiven by the creditor”. Transfers are undertaken by governments, households, and non-profit institutions for providing benefit to another party. Transfers from enterprises include compulsory transfers to governments or other units under court orders, or voluntary transfers to non-profit institutions and other entities. Unlike governments, households, or non-profit institutions, there are only limited cases where a commercial entity provides a capital transfer to another commercial entity as these entities do not generally have the motivation to transfer resources to other entities for no return, and there are few cases of debt assumption and activation of one-off guarantees.

5.9. *Debt forgiveness* involves voluntary cancellation of all or part of a debt obligation within a contractual agreement between a creditor and a debtor. In the case of debt forgiveness, all or part of the principal amount outstanding, including interest arrears (interest payments that fell due in the past) and any other interest costs that have accrued, are cancelled or forgiven. However, the cancellation of future interest payments that have not yet accrued and have not yet fallen due are not included under debt forgiveness. Debt forgiveness, which is treated as a capital transfer transaction, is different from debt write-off, as debt forgiveness arises from an agreement between the parties to the debt with the intention to convey a benefit rather than a unilateral recognition on the part of the creditor about his inability to collect the amount. Thus, debt forgiveness is unlikely to arise between commercial entities where debt write-offs are more common.

5.10. *Non-life insurance claims* are generally classified as current transfers. However, in the case of exceptionally large claims resulting from events, such as a catastrophe, a portion of the claims may be recorded as capital transfers rather than current transfers. Since the identification of such events is quite difficult, as a simplifying convention all cross-border non-life insurance claims are classified as current transfers, unless it is considered necessary to record a capital transfer in order to be consistent with the national accounts.

5.11. *Investment grants* include capital transfers in cash or in kind made by governments or international organisations to other institutional units to finance the cost of acquisition of all or part of the fixed assets. The recipients may be other governments or other entities. Investment grants are generally tied to specific investment projects, such as large scale construction, and it is obligatory on the part of the recipients to use investment grants received in cash for purposes of gross fixed capital formation.

5.12. Grants for investment made by organisations other than the general government or international organisations are included under other capital transfers.

5.13. In the event of the investment project continuing over a long period of time, an investment grant in cash may be paid in instalments, which continues to be classified as capital transfers even though they may be recorded in a succession for different accounting periods. Investment grants in kind include transfers of transport equipment, machinery and other equipment by governments to non-resident units and also the direct provision of buildings or other structures for non-resident units. They also include transfers of military equipment in the form of weapons or equipment that are classified as fixed assets.

5.14. *One-off guarantees and other debt assumption*: The activation of one-off guarantee results in the occurrence of capital transfers and, in such a scenario, the guarantor acquires no claim on the debtor or a claim worth less than the value of the guarantee.

5.15. *Capital taxes* include taxes levied at irregular and infrequent intervals on the values of the assets or net worth owned by institutional units or on the values of assets transferred between institutional units as a result of legacies, gifts or other transfers.

5.16. *Other capital transfers*: Other capital transfers include major non-recurrent payments in compensation for extensive damages or serious injuries not covered by insurance policies. Such payments may be awarded by courts of law, by arbitration, or settled out of court and include payments of compensation for damages caused by major explosions, oil spillages, the side-effects of pharmaceutical products, *etc.*

5.17. Large gifts and inheritances (legacies), including those to non-profit institutions, which are made under wills or when the donor is still living, are also included under capital

transfers. For example, exceptionally large donations by households or enterprises to non-profit institutions to finance gross fixed capital formation, and gifts to universities to cover the costs of building new residential colleges, libraries and laboratories are included under capital transfers. Capital transfer also includes capital contributions to an international organisation or non-profit institution if it does not give rise to equity for the contributor.

## ***Financial Account***

5.18. According to BPM6, “the financial account records transactions relating to financial assets and liabilities and that take place between residents and non-residents”. Functional categories, sectors, instruments, and maturities used for net international financing transactions are indicated by the financial account. Some of the major components of financial accounts include direct investment, portfolio investment, financial derivatives (other than reserves) and employee stock options, other investments, reserve assets (monetary gold), equity and investment fund shares, debt instruments and other financial assets and liabilities.

5.19. The overall balance on the financial account is called net lending / net borrowing depending on the outflow or inflow of resources. Net lending means that, on a net basis, the economy is a supplier of funds to the rest of the world, taking into consideration the acquisition and disposal of financial assets and the incurrence and repayment of financial liabilities. (Net borrowing means the reverse.) Notwithstanding the lending-oriented terms, net lending / net borrowing denotes a balance of transactions which takes into account equity, financial derivatives, monetary gold, and debt instruments. Net lending / net borrowing is always equal to the balance on the financial account, which also includes reserve assets. Conceptually, the net inflow or outflow of resources as reflected in the financial account balance should be equal to the sum of net transactions under both the current and capital accounts, with the opposite sign. In the case of a surplus of credits over debits in the current and capital accounts put together, there is a balancing net acquisition of financial assets or reduction of liabilities shown in the financial account. Thus, the financial account shows net acquisition of financial assets or net incurrence of liabilities during a period.

5.20. Net recording in the financial account entails netting of all debit entries of a particular asset or a particular liability against all credit entries in the same asset or liability type. However, *changes in financial assets are not be netted against changes in liabilities*, except

in the case of financial derivatives. For example, the acquisition of a portfolio investment in equity is netted against the sales of that type of equity; new bonds issued are netted against redemption of bonds issued; *but acquisition of bond assets is not netted against incurrence of bond liabilities*. The principle of “net recording” is to be applied at the lowest level of classification of financial instruments with due recognition to the functional category, beneficiary type, maturity, and currency classifications, where applicable. While the financial account is recorded on a net basis, the current and capital accounts are recorded on a gross basis.

5.21. The recording of transactions involving financial assets is done when economic ownership changes. Some financial liabilities, such as trade credit and advances, result from a transaction in non-financial items. In such cases, the financial claim is deemed to arise when the corresponding non-financial flow occurs.

5.22. Financial account transactions are generally recorded at market values. The value of financial instruments is to be recorded after excluding any commissions, fees, service charges, regulatory levies, and taxes.

## **Direct Investment**

5.23. According to BPM6, “direct investment is a category of cross-border investment associated with a resident in one economy having control or a significant degree of influence on the management of an enterprise that is resident in another economy”. Apart from the equity that gives rise to control or influence, direct investment also includes investment in indirectly influenced or controlled enterprises, investment in fellow enterprises, debt, and reverse investment. Direct control or influence may be achieved by owning equity, which provides voting power in the enterprise, or could be achieved indirectly through acquiring voting power in another enterprise that has voting power in the enterprise in question. Immediate direct investment relationships entail direct ownership of equities by the direct investor to the extent of 10 per cent or more of the voting power in the direct investment enterprise. If a direct investor owns more than 50 per cent of the voting power in the direct investment enterprise, he is treated as controlling that enterprise. The existence of a significant degree of influence entails that the direct investor owns between 10 to 50 per cent of the voting power in the direct investment enterprise. Indirect direct investment

relationships arise when the investor owns voting power in one direct investment enterprise that owns voting power in another enterprise or enterprises, *i.e.*, through a chain of direct investment relationships, an entity is able to exercise indirect control or influence.

5.24. *Reinvestment of earnings*, which arises from a direct investor's equity in its direct investment enterprise, is recorded as an imputed financial account entry. Reinvestment of earnings is included as part of FDI (credit) in the financial account with a corresponding contra entry in the investment income component of the current account (debit). Reinvestment of earnings may be negative in some cases, *e.g.*, in cases where losses by the direct investment enterprise or dividends payable in a period are larger than net earnings in that period. While positive reinvested earnings are treated as an injection of equity into the direct investment enterprise by the direct investor, negative reinvested earnings are treated as a withdrawal of equity.

5.25. *Mergers* involve an agreement between two or more companies to combine into a single operation. *Acquisitions* arise when one company or a group of companies purchases another company or group of companies (though not all the shares may be acquired by the purchaser). Mergers and acquisitions data are not considered as standard components within direct investment, though such data may be of interest because the nature of mergers and acquisitions may differ from other direct investment.

5.26. *Corporate inversion* involves the corporate restructuring of a transnational enterprise group in such a manner that the original parent company in one economy ends up becoming the new parent's *subsidiary* in another economy. Additionally, there may be a shift in ownership of a group of enterprises to the new parent company. These types of arrangements may be called corporate relocations, headquarters relocations, or corporate restructuring. Corporate inversion leads to recording of financial transactions in the financial account. While corporate inversion results in a change in the economy of the direct investor, the operational structure and ultimate shareholders remain effectively unaffected, though the new parent company benefits from the taxation and regulatory environment of its economy of incorporation. In view of the fact that inversions can involve large values in the financial account but without much or no movement in resources, it may be of analytical interest to separate them from other direct investment.

5.27. *Super-dividends and liquidating dividends* are considered as a withdrawal of equity, rather than as income payable to the owners. Thus, these amounts are excluded from dividends and are shown as a reduction in equity in the financial account, just as in the case of any other withdrawal of equity.

5.28. *Borrowing for fiscal purposes*: Special rules are applicable in the case of an entity owned or controlled by the general government when that entity, which is resident in another territory, is used for fiscal purposes. The special approach for government entities is on account of the fact that unlike in the private sector, the non-resident entity undertakes functions at the behest of the general government for public policy and not for commercial purposes.

## **Portfolio Investment**

5.29. According to BPM6, “portfolio investment is defined as cross-border transactions and positions involving *debt* or equity securities, other than those included in direct investment or reserve assets”. The negotiability of securities is meant to facilitate trading, allowing them to be held by different parties during their lives. Negotiability facilitates portfolio diversification and ready withdrawal of investment on the part of investors. Investment fund shares/units (*i.e.*, those issued by investment funds) that are backed by securities and that are not included as part of reserve assets or direct investment are included under portfolio investment. Despite being negotiable instruments, exchange-traded financial derivatives are excluded from portfolio investment as they are represented as a separate category.

5.30. *Equity securities* include all *instruments* and records which acknowledge claims to the residual values of incorporated enterprises after the claims of all creditors have been met. Shares, stocks, participation, or similar documents (such as American Depositary Receipts) are examples of equity securities. Preferred stock or shares, which also provide for participation in the distribution of the residual value on dissolution of an incorporated enterprise, are included. Mutual funds and investment trusts also are included.

5.31. *Debt securities* cover (i) bonds, debentures, notes, *etc.* and (ii) money market or negotiable debt instruments. Bonds, debentures, notes, *etc.* usually confer unconditional rights on the holder to a fixed money income or contractually determined variable money



income. Except for perpetual bonds, bonds and debentures also provide the holder with the unconditional right to a fixed sum as a repayment of principal on a specified date or dates. This includes non-participating preferred stocks or shares, convertible bonds, and bonds with optional maturity dates, which is more than one year after issue. Negotiable certificates of deposit with maturities of more than one year; dual currency bonds; zero coupon and other deep discounted bonds; floating rate bonds; indexed bonds; and asset-backed securities, such as collateralised mortgage obligations and participation certificates are also included in this category. (Mortgages are not classified as bonds but are included under loans.)

5.32. *Money market securities* generally provide unconditional right to the holder to receive a stated, fixed sum of money on a *specified* date. These instruments are usually traded at a discount in organised markets with the quantum of discount being dependent on the interest rate and the time remaining to maturity. The instruments include treasury bills, commercial and financial paper, bankers' acceptances, negotiable certificates of deposit (with original maturities of one year or less), and short-term notes issued under note issuance facilities.

5.33. Some of the other components of portfolio investment, as discussed in BPM6, are set out below:

5.34. *Reinvestment of earnings in investment funds*: This includes undistributed earnings of portfolio investment in investment funds, which are imputed as being payable to the owners and then reinvested in the fund. The financial account entry for reinvestment of earnings is the corresponding entry to reinvested earnings of investment funds in the primary income account item of the current account (debit). The treatment and calculation of earnings are the same as in the case of reinvested earnings of direct investment enterprises. Reinvestment of earnings may be negative, for example, in cases where a fund has paid dividends out of realised holding gains, or when dividends are paid out of earnings accrued over previous periods.

5.35. *Convertible bonds*: On implementation of the option to convert the bond into shares, two entries are made, *viz.*, redemption of the bond and the issue/acquisition of shares.

5.36. *Debt defeasance*: Debt defeasance enables a debtor (whose debts are generally in the form of debt securities and loans) to remove certain liabilities from the balance sheet by

pairing irrevocable assets of equal value to the liabilities. Defeasance may be carried out (a) by placing the paired assets and liabilities in a trust account within the institutional unit concerned, or (b) transferring them to another institutional unit. In the first case, there are no transactions with respect to defeasance and the assets and liabilities are not excluded from the balance sheet of the unit. In the second case, the financial account of the economies concerned records transactions by which the assets and liabilities are moved to the second statistical unit, provided the units are resident of different economies, and are reported in the balance sheet of the unit that holds the assets and liabilities. Therefore, debt defeasance sometimes leads to a change in the institutional unit that records those liabilities.

5.37. *Share and debt buybacks*: Transactions which involve buying of its own shares by a corporation are classified as a reduction in the equity liability, rather than as an acquisition of an asset. Similarly, an issuer's purchase of its debt security is treated as redemption of the debt.

5.38. *Bonus shares*: Shares are sometimes restructured by corporations who offer their shareholders a number of new *shares* for each share previously held, which can be termed as stock splits or the issue of bonus shares. In contrast to the issue of new shares in return for additional funds, the issue of bonus shares does not involve provision of new resources and no transaction is recorded.

## **Financial Derivatives and Employee Stock Options**

5.39. A financial derivative contract is a financial instrument that is linked to another specific financial instrument or indicator or commodity, through which specific financial risks (such as interest rate risk, foreign exchange risk, equity and commodity price risks, and credit risk) can be traded in their own right in financial markets. Transactions and positions in financial derivatives are treated separately from the values of any underlying assets to which they are linked. Financial derivatives and employee stock options are financial assets and liabilities having similar features, such as a strike price, and some of the same risk elements. However, while both perform the function of transferring risk, employee stock options are also designed as a form of remuneration. The risk embodied in a financial derivative contract can be traded either by trading the contract itself, as in the case of options, or by creating a

new contract, which embodies risk characteristics that match, in a countervailing manner, those of the existing contract as in the case of forward markets.

5.40. There are two broad types of financial derivatives—options and forward-type contracts. In an option contract (option), the purchaser acquires from the seller the right to buy or sell [depending on whether the option is a call (buy) or a put (sell)] a specified underlying item at a strike price on or before a specified date.

5.41. A forward-type contract (forward) is an unconditional contract by which two counterparties agree to exchange a specified quantity of an underlying item (real or financial) at an agreed-upon contract price (the strike price) on a specified date. Futures are forward-type contracts, which are traded on organised exchanges. A swap contract, which involves the exchange of cash flows among the counterparties in accordance with pre-arranged terms based on the reference prices of the underlying items, is also classified as a forward-type contract. Currency swaps, interest-rate swaps, cross-currency interest-rate swaps, and cross-currency swaps are examples of swap contracts.

5.42. Financial account entries for derivatives should preferably be shown separately for each of the assets and liabilities, wherever possible, but in a situation when gross reporting is impractical, net settlements are acceptable. The value of the financial derivative should exclude any explicit or implicit service charges but, in view of the fact that distinguishing implicit service charges is usually not possible, the entire value of the financial derivative is classified as being for the financial asset.

5.43. *Employee stock options:* According to BPM6, “an employee stock option (ESOP) is created on a given date (the “grant” date), providing that an employee may purchase a given number of shares of the employer’s stock at a stated price (the “strike” price) either at a stated time (the “vesting” date) or within a period of time (the “exercise” period) immediately following the vesting date”. Transactions in ESOPs are recorded in the financial account as the corresponding entry to the compensation of employees. On exercise of the option, the difference between the market price of the equity and the price paid by the buyer for the equity is recorded in the financial account.

## Other Investments

5.44. Other investments cover one-off guarantees and other debt assumptions (including trade credits and loans). Debt assumption entails one party taking on the liability of another party. Debt may be assumed under a pre-existing guarantee, or without a guarantee, as in the case of the government wanting to assist a project or a direct investor assuming the liabilities of its direct investment enterprises for reputational reasons. One-off guarantees occur in a situation when conditions of the loan or of the security that is guaranteed are so particular that the calculation of the degree of risk associated with any degree of precision is impossible. These guarantees are recognised as economic assets only on activation, that is, on the occurrence of that event that makes the guarantor responsible for the liability. These are treated as contingent assets until activated. However, one-off guarantees granted by governments to corporations in financial distress and which are quite likely to be invoked are treated as if these guarantees are activated at inception.

5.45. *Trade credits* consist of claims and liabilities which arise when credit is directly extended by suppliers and buyers for transactions in goods and services and advance payments for work in progress (or to be undertaken) which is associated with such transactions. In the absence of actual data, trade credits may be measured by the difference between entries for the underlying transactions in goods and services, which are recorded when ownership changes, and the entries that are recorded when the payments relating to these transactions are made. Though trade credits are generally short-term in nature, trade credits and advances are sub-divided into short-term (with a maturity of a year or less) and long-term (with a maturity of more than one year) categories.

5.46. *Loans* comprise those financial assets that are created through the direct lending of funds by a creditor (lender) to a debtor (borrower) through an arrangement in which the lender either does not receive any security which shows that the transaction has taken place or receives a non-negotiable document or instrument. The categories of loans include loans to finance trade, other loans and advances (including mortgages), use of Fund credit and loans from the Fund, *etc.* Additionally, financial leases and repurchase agreements are also included under loans though, from a strictly legal point of view, these may not be considered loans. Loans are sub-divided into two categories, *viz.*, long- and short-term loans. Long-term loans and trade credits are recorded on a net basis though it is recommended by the Manual

that the recording of gross flows in respect of drawings and repayments on these instruments be provided as supplementary information. Such information is useful for analysing debt transactions and for reconciling the BoP data on debt with other sources of such information.

5.47. *Insurance, pension funds, and standardised guarantee transactions* need to be broken down into their various elements, viz., service, income, transfer, and financial account. In the case of non-life insurance, insurance technical *reserves*, which consist of prepayments of insurance premiums and outstanding claims, are recorded in financial accounts. Analogously, for life insurance, pension schemes, annuity funds, and standardised guarantee schemes, the changes in technical reserves on account of transactions are recorded in the financial account and consist of amounts of the estimated obligations to beneficiaries and holders which accrued during the period. Changes in technical reserves, which result from holding gains or losses, are not on account of transactions and are, therefore, not recorded in the financial account but included in the revaluation account.

5.48. *Special drawing rights*: The IMF's allocation of special drawing rights (SDRs) to its member countries is shown as the incurrence of a liability of the recipient under SDRs in other investment, with a corresponding contra entry under SDRs in reserve assets. Other acquisitions and sales of SDRs are included as transactions in reserve assets.

5.49. *Currency*: Transactions involving issued banknotes and coins are recorded under currency and deposits. Transactions by residents with non-residents involving domestically-issued banknotes and coins are recorded as liabilities, while transactions by residents with non-residents involving foreign-issued banknotes and coins are recorded as assets.

5.50. *Change of contractual terms*: In case the original terms of a debt (typically a loan or debt security, but also other debt items) are changed through re-negotiation between the parties, then the original liability is treated as repaid and a new liability is created.

## Reserve Assets

5.51. Transactions involving monetary gold are recorded in the financial account only in such cases when these transactions take place for reserve purposes between two monetary authorities or between a monetary authority and an international financial organisation.

Financial account transactions with the IMF pertain to reserve assets, reserve-related liabilities, other investments, and off-balance sheet liabilities.

### Arrears

5.52. The accumulation of arrears pertaining to exceptional financing, in cases when it occurs, needs to be included as a memorandum item to the financial account,

### ***Capital Account of India's Balance of Payments***

5.53. The present practice of BoP compilation in India is broadly in line with international best practices except for the presentation. The capital account part of “capital and financial account (as per IMF classification” is subsumed in the current account, and financial account is termed “capital account” in India’s BoP. The basic structure of the capital account of India’s BoP consists of assets and liabilities covering direct investment, portfolio investment, loans, banking capital, short-term credits and other capital. The data on capital account are compiled on the basis of various returns filed with the RBI by the entities (ADs) who are engaged in foreign exchange transactions. The reporting by ADs includes transactions related to foreign direct investment, foreign institutional investment/ADR/GDR, external commercial borrowings (ECBs)/foreign currency convertible bonds (FCCBs), trade credit, NRI deposits and other banking liabilities/assets. The data on external assistance are obtained from Government of India.

### Foreign Direct Investment in India

5.54. Foreign investment in India has two components, viz., foreign direct investment and portfolio investment. With regard to FDI, while as per the international definition, for an investment to qualify as FDI the foreign investor needs to have a 10 per cent or higher stake in a given company, in India this has not been strictly adhered to. Irrespective of the extent of holding in a particular company, it is considered as an FDI if the non-resident acquires shares in a company other than by way of acquisition from the stock market, *i.e.*, through initial public offerings (IPO) or through private arrangements (including private placements) in line with the requirements laid down in Schedule 1 of FEMA Notification No. 20 dated May 3, 2005. In the context of portfolio investment, there is an individual limit of 10 per cent equity holding by foreign institutional investors in any Indian company. The limit for all FIIs taken together is 24 per cent. This limit, however, could be raised up to the sectoral cap under the

extant FDI policy by way of corporate action (board resolution followed by a general body resolution). The acquisition of shares by FIIs is primarily through the secondary market. Further, portfolio investment by NRIs is subject to an individual cap of 5 per cent with an overall cap of 10 per cent for all NRIs. This cap can be increased up to 24 per cent by corporate action.

5.55. All FDI transactions reported to the RBI in terms of reporting requirements laid down in Schedule 1 of FEMA Notification No. 20 dated May 3, 2005 are treated as FDI. FDI, therefore, includes the following:

- Shares acquired by way of IPO
- Shares acquired by way of preferential allotment
- Shares acquired by way of offer for sale through private arrangement
- Transfer of shares by way of offer for sale through private arrangement

5.56. The initial investment by non-residents under FDI by issue of fresh share capital is reported in Form FC-GPR and the acquisition of shares in an existing company by way of transfer under FDI is reported in Form FC-TRS. In the case of FC-GPR, the reporting is done by the companies through the ADs, who consolidate and supply the data to the RBI on a monthly basis. Thus, the major portion of data on FDI is captured through FC-GPR and FC-TRS. The issue of shares has to be reported within 30 days, while transfer of shares has to be reported within 60 days.

5.57. The acquisition of shares of Indian companies by non-residents through private arrangement has been included as part of FDI since January 1996. It may be mentioned that FDI to and by India up to 1999-2000 comprised mainly equity capital. Subsequently, in line with international best practices and as recommended by the Technical Monitoring Group (TMG) on FDI Statistics, 2003, the coverage of FDI has been expanded since 2000-01 to include, besides equity capital, reinvested earnings (retained earnings of FDI companies) and “other direct capital” (inter-corporate debt transactions between related parties, *i.e.*, between direct investors and subsidiary branches and associates). Data on equity capital include equity of incorporated as well as unincorporated entities (mainly foreign bank branches in India and Indian bank branches operating abroad). The data on equity and other capital are compiled on a monthly and quarterly basis, respectively, based on the above returns. The reinvested earnings are compiled based on the data collected through the Annual Survey of India’s

Foreign Liabilities and Assets. Data on reinvested earnings for the latest year are estimated as an average of the previous two years as these data are available with a time lag of one year.

5.58. Thus, credit (inflows) under FDI 'to India' includes all types of investments in equities (investments made by non-residents in the shares/mandatorily convertible debentures/ preference shares of an Indian company), reinvested earnings of both incorporated and unincorporated bodies (mainly foreign bank branches operating in India) and other capital of FDI companies. "Other" under FDI includes inter-corporate loans given by parent companies to their affiliates. Debit (outflows) under FDI 'to India' includes repatriation of FDI in India in equity shares and real estates of incorporated enterprises. Other capital and reinvested earnings are recorded on a net basis.

### **Foreign Direct Investment Abroad**

5.59. In the Indian context, overseas direct investment in Joint Ventures (JVs) and Wholly Owned Subsidiaries (WOS) could be made both through the automatic route as well as the approval route. In the case of overseas direct investment, the RBI captures data on direct investment in equities, loans and guarantees extended. Under the automatic route, an Indian entity is permitted to make investment in overseas JVs/ WOS not exceeding 400 per cent of its net worth, subject to certain exemptions, such as investment made out of balances held in the Exchange Earners' Foreign Currency account of the Indian party or out of funds raised through ADRs/GDRs. The Indian party has to approach an Authorised Dealer Category-I bank with an application in Form ODI and the prescribed enclosures/documents to effect remittances towards such investments. Reporting is done electronically by the ADs to the Foreign Exchange Department of the RBI through Overseas Investment Application Software as and when remittance is made by the Indian company. Form ODI contains various sections which provide details of the Indian party's activities, the AD's certification of the activity of the Indian party, the purpose of investment, particulars of the JVs/WOS, enhancement of stake in the existing ODI arrangement, the gist of the amount that is being invested, a declaration of any investigation/ specific benefit, a certificate of statutory authority regarding 400 per cent net worth criterion, liquidation/ winding up as and when it takes place, *etc.* The approval route includes all such cases of direct investment abroad which do not satisfy the norms of automatic route and where prior approval of the Reserve Bank is required.



5.60. Credit under foreign investment abroad includes “repatriation of Indian investment abroad in branches and WOS”, “repatriation of Indian investment abroad in subsidiaries and associates” and “repatriation of Indian investment abroad in real estate”. Debit under foreign investment abroad includes direct investment by Indian companies in equities of foreign companies. It also includes investment in equity capital of unincorporated entities, *i.e.*, Indian bank branches operating abroad, which are captured by increment in equity capital during the year obtained from the balance sheets of individual banks. Besides, loans and standardised guarantees extended to foreign companies by Indian companies are included in the “other capital” component of FDI abroad. Reinvested earnings of Indian companies abroad are recorded on a net basis and included as a debit item (outflows).

5.61. Since the expansion of coverage of FDI in line with international best practices based on TMG’s recommendations in 2003, efforts have been made to expand the coverage by including non-cash acquisitions against technology transfer and plant and machinery as part of FDI. Some more items *viz.*, financial leasing, debt securities and investment in land and building have also been incorporated in the questionnaire used for the Annual Survey of India’s Liabilities and Assets. However, there are certain gaps in compiling the FDI data in a comprehensive manner. Indirect investments through WOS of foreign companies in Indian entities are not captured as such investments are reckoned as resident investments.

5.62. The standard components of capital and financial accounts as outlined in BPM6 and India’s status *vis-à-vis* these components is set out in Table V.1 below.

**Table V.1: Standard Components of Capital and Financial Accounts of Balance of Payments**

<b>Capital Account</b>			
		<b>BPM6</b>	<b>India</b>
1	Gross acquisitions (DR.) / disposals (CR.) of non-produced non-financial assets	Yes	No
2	Capital transfers	Yes	No
<b>Financial Accounts</b>			
<b>A. Foreign Direct Investment</b>			
1	Equity Capital	Yes	Yes
2	Reinvested Earnings	Yes	Yes
3	Other Capital	Yes#	Yes
<b>B. Portfolio Investment</b>			
<b>I. Equity</b>			
1	Central Bank	Yes	Not Applicable
2	Commercial Banks	Yes	Yes
3	Government	Yes	Yes
4	Other financial Corporations	Yes	Yes
5	Non-financial Corporations	Yes	Yes
6	Financial Derivatives	No@	No
<b>II. Debt</b>			
1	Central Bank	Yes	Not Applicable
2	Commercial Banks	Yes	Yes
3	Government	Yes	Yes
4	Other financial Corporations	Yes	Yes
5	Non-financial Corporations	Yes	Yes
6	Financial Derivatives	No@	No
<b>C. Other Investment</b>			
1	Other equity	Yes	No
2	Currency and Deposits	Yes	Yes*
3	Loans	Yes	Yes
4	Trade Credits	Yes	Yes
5	Insurance, pension, and standardised guarantee schemes	Yes	No
6	Other accounts receivable/payable —other	Yes	Yes
7	Special drawing rights	Yes	No

#: Classified as debt instruments in BPM6.

@: Financial derivatives are separately presented in the capital and financial accounts in BPM6 as “Financial derivatives (other than reserves) and employee stock options” and not as part of portfolio investment as in BPM5.

\*: NRI Deposits in the Indian case, which is a part of banking capital.

## Portfolio Investment

5.63. Portfolio investments mainly include (i) portfolio investment ‘in India’ covering FIIs’ investment and funds raised through GDRs/ADRs by Indian companies and through offshore funds and (ii) India’s portfolio investment abroad.

5.64. Portfolio investment 'in India' is subject to the policy guidelines framed by the Government of India from time to time in accordance with its Industrial Policy. It attracts provisions of Section 6 of FEMA and is regulated under FEMA 1999 in terms of Notification No. FEMA 20-RB/2000 dated May 3, 2000 as amended from time to time. Foreign portfolio investment is categorised under the following heads:

- i. Investment under the Portfolio Investment Scheme, *i.e.*, purchase of equity shares/convertible debentures by FIIs and NRIs in the secondary market;
- ii. Purchase of securities, *viz.*, dated securities/treasury bills, non-convertible debentures/bonds issued by Indian companies and units of domestic mutual funds by FIIs and NRIs in the secondary market.
- iii. Issue of ADRs/GDRs and investment through offshore funds is also included in Foreign Portfolio Investment.

### ***Portfolio Investment 'in India'***

#### Foreign Institutional Investments

5.65. FII investment in India, which is a part of portfolio investment, covers all portfolio investment by overseas pension funds, mutual funds, investment trusts, asset management companies, nominee companies, banks, institutional portfolio managers, university funds, endowments, foundations, charitable trusts, charitable societies, and trustees or power of attorney holders incorporated or established outside India proposing to make proprietary investments or investments on behalf of a broad-based fund (*i.e.*, a fund having more than 20 investors with no single investor holding more than 10 per cent of the shares or units of the fund). Investments by FIIs are mainly in debt and equity papers, both in the secondary as well as primary markets. FII investments are generally in existing companies. Data on FII investments in the Indian equity market are collected through custodians. All sales/purchases by FIIs are reported to the RBI by custodian banks on a daily basis. The RBI monitors FIIs' adherence to the overall cap of 24 per cent/ sectoral cap. The individual FII limit of 10 per cent/ NRI limit of 5 per cent is monitored by custodian banks. Purchases made by FIIs in both debt and equities in the Indian capital market are included under credit (inflows), while sales

by FIIs are included under debit (outflows). Thus, FII investment in India is recorded on a gross basis.

#### *ADRs/GDRs*

5.66. Depository Receipts (DRs) are negotiable securities issued outside India by a Depository bank on behalf of an Indian company; they represent the local Rupee-denominated equity shares of the company held as deposit by a Custodian bank in India. DRs are traded on stock exchanges in the US, Singapore, Luxembourg, London, *etc.* DRs listed and traded in US markets are known as American Depository Receipts (ADRs) and those listed and traded elsewhere are known as Global Depository Receipts (GDRs).

5.67. Indian companies can raise foreign currency resources abroad through the issue of ADRs/ GDRs, in accordance with the Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993 and guidelines issued by the Government of India in this context from time to time. The creation of ADR/GDR causes a capital inflow at the point of creation (credit). Data on funds raised through ADR/GDR are directly reported to the RBI by the companies as and when they raise fresh ADRs/GDRs or repatriate proceeds from thereunder.

#### *Portfolio Investment 'Abroad'*

5.68. Portfolio investment by India in overseas capital markets is captured through a statement which is submitted by the ADs to the RBI in terms of AP (Dir Series) Circular No. 66 dated January 13, 2008. However, the volume of such transactions is quite low. Indian corporate can make portfolio investments abroad up to 50 per cent of their net worth. Investment by mutual funds in overseas capital markets is captured separately by the ADs. Investments by Indian mutual funds in overseas markets are made in various instruments, *viz.*, ADRs/GDRs, debt instruments, equity, exchange traded funds (ETFs), mutual funds, *etc.* The reporting by the ADs to the RBI is done electronically on a monthly basis. ESOPs are also covered separately by the ADs and the reporting is done to the RBI on an annual basis. At present, these data are not being adequately captured in India's BoP compilation. At present, credit under portfolio investment abroad includes "repatriation of Indian investment abroad in debt securities" and debit includes "Indian investment abroad in debt securities".

## External Assistance

5.69. External assistance by India denotes loan and advances extended by India to foreign governments under various agreements (debit) and repayment of such loans (credit). External Assistance to India (credit) denotes multilateral and bilateral loans received under agreements between the Government of India and other governments/international institutions and repayments of such loans by India (debit), except for loan repayment to erstwhile “Rupee area” countries that are covered under the Rupee Debt Service. The data on external assistance to India for the purpose of BoP compilation are obtained from the CAAA, Ministry of Finance, Government of India, while data on external assistance by India is obtained from the Budget Document (Annual Financial Statement).

## External Commercial Borrowings

5.70. At present, Indian companies are permitted to access funds from abroad through four routes, *viz.*, ECB, FCCB, preference shares and foreign currency exchangeable bonds (FCEB).

5.71. ECB refer to commercial loans in the form of bank loans, buyers’ credit, suppliers’ credit, securitised instruments (*e.g.*, floating rate notes and fixed rate bonds, non-convertible, optionally convertible or partially convertible preference shares) availed of from non-resident lenders with a minimum average maturity of 3 years (*i.e.*, 3 years and above). ECB can be raised only for specific purposes, such as investment [such as the import of capital goods (as classified by DGFT in the Foreign Trade Policy), new projects, modernisation/expansion of existing production units] in the real sector — the industrial sector including small and medium enterprises (SME), the infrastructure sector and specific service sectors, namely hotels, hospitals and software — in India.

5.72. FCCB are bonds issued by an Indian company expressed in foreign currency, the principal and interest in respect of which are payable in foreign currency. Preference shares (*i.e.*, non-convertible, optionally convertible or partially convertible) for issue of which funds have been received on or after May 1, 2007 would be considered as debt and should conform to policy.

5.73. A Foreign Currency Exchangeable Bond (FCEB) means a bond expressed in foreign currency, the principal and interest in respect of which are payable in foreign currency, issued by an issuing company and subscribed to by a person who is a resident outside India in foreign currency and exchangeable into equity share of another company, called the Offered Company, in any manner, either wholly or partly or on the basis of any equity-related warrants attached to debt instruments.

5.74. ECB can be accessed under two routes, *viz.*, (i) Automatic Route and (ii) Approval Route. Data on ECBs are collected by the RBI. Under the approval route, borrowers are required to submit Form ECB through a designated AD bank to the Foreign Exchange Department, Reserve Bank of India along with the necessary documents. Under both the automatic and approval routes, borrowers are required to submit Form 83 to the designated AD bank for allotment of a Loan Registration Number (LRN), which is forwarded to the Department of Statistics and Information Management (DSIM) of the RBI. Form 83 captures details like the name and category of the borrower and lender, end-use, amount, currency, nature of the loan (whether it is a commercial loan, fixed rate bond, FRN, suppliers' credit, buyers' credit), interest rate, other charges, all-in-cost, drawdown and repayment schedules, average maturity period, *etc.* After obtaining the LRN, borrowers are required to submit an ECB-2 Return indicating the transaction details (amount disbursed, principal re-payment, interest payment, utilisation, *etc.*), duly certified by the designated AD bank on a monthly basis so as to reach the Department of Statistics and Information Management (DSIM), Reserve Bank of India within seven working days from the close of the month to which it relates. The details in respect of the Returns are processed in the Commonwealth Secretariat Debt Recording and Management System (CS-DRMS) and additionally in the Integrated Database Management System (IDBMS) of DSIM, Reserve Bank of India. The consolidated data are generated on a quarterly basis and are used for BoP as well as external debt compilation by the RBI and the External Debt Management Unit (EDMU), Department of Economic Affairs (DEA), Government of India.

5.75. Credit under ECB 'to India' includes disbursements under commercial borrowings, and debits include repayments thereof. Credit under ECB 'by India' includes repayments of loans extended to non-residents and debit includes loans extended to non-residents.

## Short-Term Loans

5.76. Trade credits refer to credits extended for imports directly by the overseas supplier, banks and financial institutions for a maturity of less than three years. Depending on the source of finance, such trade credits are classified as Suppliers' Credit or Buyers' Credit. Suppliers' credit relates to credit for imports into India extended by the overseas supplier, while buyers' credit refers to loans for repayment of imports into India arranged by the importer from a bank or financial institution outside India for a maturity of less than three years.

5.77. Short-term trade credits have three components, *viz.*, (i) suppliers' credit of up to 6 months, (ii) suppliers' credit of more than 6 months, and (iii) buyers' credit of up to three years. The latter two are clubbed and shown together as a single category in India's BoP statistics. The data on outstanding suppliers' credit up to 180 days, which are essentially embedded in import values, is compiled by the RBI based on the estimation made from the import data received from authorised dealers. AD branches report the payments made by them for import bills (against documents) as reported in the fortnightly FETERS data. This dataset collects information on the date of shipment and date of payment as well as information on the terms of credit (under LC or non-LC). The outstanding suppliers' credit up to 180 days at the end of a particular quarter, say, end-December 2009 is derived from those import transactions that have a difference of 180 days between the date of payment and the date of shipment (*i.e.*, shipments up to end-December 2009 and payments after end-December 2009 with the difference being equal to or less than 180 days). Additionally, all transactions with the difference between the payment and shipment date of less than or equal to 25 days are excluded for the purpose of estimating suppliers' credit up to 180 days to take into account the delay in reporting due to procedural bottlenecks. Moreover, as the ADs also arrange buyers' credit for their customers but seldom report the import payment on the due date of the import bill, there is an under-reporting of receipts and payments of buyers' credit and an over-estimation to the same extent in supplier's credit, which are adjusted to arrive at the estimates for suppliers' credit.

5.78. Based on this methodology, the quarterly estimates of the suppliers' credit up to 180 days for the next two quarters (*i.e.*, for the quarter ending March 2010 and June 2010 in the above example) are arrived at by multiplying the observed ratio (which is the ratio between

the outstanding suppliers' credit so derived, in this case as at end-December 2009, based on imports data reported through FETERS for the period January-June 2010, to the six-month imports data for the period July-December 2009 reported by DGCI&S ) with the DGCI&S actual imports of the past six months (*i.e.*, between Oct-2009 and March 2010) to estimate the suppliers' credit for the quarter ending March 2010, and with the DGCI&S actual imports data for the period January-June 2010 to estimate the suppliers' credit for the quarter ending June 2010. The present procedure provides the estimate of suppliers' credit up to 180 days with a minimum lag of 6 months. As regards buyers' credit, since buyers' credit of less than six months needs specific approval, these get included under the category of suppliers' credit of more than six months. Suppliers' credit up to 180 days are estimated on a net basis (a positive sign denotes credit and a negative sign denotes debit).

5.79. With regard to "suppliers' credit of more than six months and buyers' credit", ADs are permitted to approve trade credit (both suppliers' and buyers' credit) for imports into India up to US\$ 20 million with a maturity period of up to one year, and for imports of capital goods with a maturity period of more than one year and less than three years without the prior approval of the Reserve Bank. ADs are not permitted to approve trade credits exceeding US\$ 20 million per import transaction. ADs are required to furnish the details of each approval, drawal and repayment of trade credits granted by all its branches in a consolidated statement during the month in the given format (which includes currency-wise, item-wise, maturity-wise and lender-wise reporting of buyers' credit), so as to reach the Department of Economic and Policy Research of the RBI no later than the 10th of the following month. Total disbursement (credit) is arrived at by adding the disbursement figures reported by all ADs, and repayments (debit) is obtained by adding the principal amount excluding interest and other charges. The Indian Oil Corporation (IOC) also submits monthly data on oil imports under three categories, *viz.*, revolving line of credit, short-term credit, and buyers' credit (automatic route). The total disbursement and total repayment are derived by adding disbursement and repayment made by the ADs and the IOC in that particular month. The net short-term credit is the difference between disbursement and repayment.

## **Banking Capital**

5.80. Banking capital comprises three components: (a) foreign assets of commercial banks (ADs), (b) foreign liabilities of commercial banks (ADs), and (c) others. "Foreign assets" of



commercial banks consist of (i) foreign currency holdings, and (ii) rupee overdrafts to non-resident banks. “Foreign liabilities” of commercial banks consist of (i) non-resident deposits, which comprise receipt and redemption of various non-resident deposit schemes, and (ii) liabilities other than non-resident deposits, which comprise rupee and foreign currency liabilities to non-resident banks and official and semi-official institutions. “Others” under banking capital include movement in balances of foreign central banks and international institutions like the IBRD, IDA, ADB, IFC, IFAD, *etc.*, maintained with the Deposit Accounts Department (DAD) of the RBI as well as movement in balances held abroad by the Embassies of India in London and Tokyo. Increase in balances maintained by foreign central banks and international institutions with the RBI represents credit in the case of “Others” under banking capital, while a decrease in balances represents debit.

5.81. Regarding the data sources, the Banking Assets & Liabilities (BAL) statement provides information on the foreign assets and liabilities of the banking sector in India. The movement of banking capital is captured, through the BAL statement, by the balances in the Nostro (banks resident in India having accounts outside India) and Vostro accounts (banks resident outside India having accounts in India) maintained by ADs. Under Nostro accounts, the BAL statement captures information on foreign currency balances held abroad, which includes information in respect of credit and debits of the current account of banks, and investment by banks in fixed deposits, securities, loans and treasury bills, with corresponding currency and country details. Under Vostro accounts, the BAL statement includes information in respect of credit and debits of the current accounts of the overseas branches and correspondents in non-resident accounts with corresponding currency and country details. An increase in assets or a decrease in liabilities represents an outflow of capital (debit), and a decrease in assets or an increase in liabilities represents an inflow of capital (credit) in the case of Nostro accounts. In the case of Vostro accounts, it is the reverse.

5.82. The Head/Principal Office of each Authorised Dealer Category-I is required to submit a statement in Form BAL in duplicate (submitted under Section 11(2) of FEMA, 1999). This statement is submitted on a fortnightly basis so as to reach the Regional Office of the Reserve Bank of India under whose jurisdiction the Head / Principal Office is situated within seven calendar days from the close of the reporting period to which it relates. However, with the implementation of the Online Returns Filing System (ORFS), AD banks have been

submitting balance statement information in digital form through ORFS since April 2006 and submission of hard copies of the BAL statement has been discontinued.

5.83. Data on non-resident accounts, *viz.*, FCNR(B), NRE and NRO accounts, is reported in electronic format through the Non-Resident Deposits–Comprehensive Single Returns (NRD-CSR) package, which is mandatory under FEMA and provides the outstanding position of NRI deposits on a fortnightly basis. Additionally, STAT-5 and STAT-8 Returns are used to estimate the flows in NRI accounts during the month. Banks which are authorised to deal with NRI deposits are required to submit Stat-5 and Stat-8 Returns on a monthly basis to the RBI. The Stat-5 Return provides information on the opening balance at the beginning of the month, inflows/outflows during the month and the amount outstanding at the end of the month of deposits under the Foreign Currency (Non-Resident) Accounts (Bank) [FCNR(B)] Scheme, while the Stat-8 Return captures the same information under the Non-Resident (External) Rupee [NRE(R)A] Accounts and Non-Resident Ordinary (NRO) Rupee Accounts. While Stat-5 provides data relating only to fixed deposit accounts, Stat-8 provides separate data on both fixed deposits as well as combined data pertaining to savings bank and current account deposits.

5.84. As per FEMA guidelines, banks authorised to deal in non-resident deposits are required to submit soft copies of Stat-5 and Stat-8 Returns. Both the Stat Returns are filed to the RBI through e-mail within 10 days of the following month in the prescribed Microsoft Excel format. A hard copy of the above Returns is also submitted to the RBI; these data are used for quarterly BoP compilation by the RBI. However, despite Stat-5 and Stat-8 being mandatory Returns, there are problems in terms of inadequate coverage/under-reporting. Receipts under various NRI deposit schemes represent credit and redemptions or withdrawals represent debit.

### **Rupee Debt Service**

5.85. Rupee debt service includes principal repayments on account of civilian and non-civilian debt in respect of Rupee Payment Area (RPA) and interest payment thereof. The principal repayments / interest payments (debit) are effected by the Deposit Accounts Department (DAD) of the Reserve Bank of India based on the repayment schedule received from the Government of India. In the case of Rupee debt service, principal repayments and

interest payments cannot be separately identified. Therefore, they are shown together as a single payment in India's BoP under "Rupee debt service". There are no inflows (credit) under this account.

## Other Capital

5.86. "Other capital" comprises mainly the leads and lags in export receipts as estimated (leads appear with a positive sign and lags with a negative sign). Other items included under "other capital" are funds held abroad (debit), India's subscription to international institutions, quota payments to the IMF and SDR allocation (data maintained by the Department of External Investments and Operations, RBI), remittances towards recouping the losses of branches/ subsidiaries reported by ADs under FETERS and residual items of other capital transactions not included elsewhere. Debit (outflows) includes ADRs/GDRs held abroad, ECBs held abroad, software funds held abroad by software companies, advance payments against imports, *etc.* Credit (inflows) includes total funds brought in, *i.e.*, ADRs/GDRs repatriated, ECB funds held abroad brought in, India's subscription to international institutions, SDR allocations and residual items of other capital receipts.

5.87. There is a need to restructure the presentation of the BoP statistics to make it comparable with international best practices. For instance, at present India's BoP statistics are presented under the "current account" and "capital account", whereas as per the guidelines of the IMF the capital account needs to be bifurcated into "capital account" (covering transactions only in capital transfers and non-produced non-financial transactions) and "financial account" (covering transactions under foreign investments, derivatives and other investments). This entails identifying and excluding capital transfers, as defined in the Manual, from the current account of India's BoP and including them explicitly in capital account transactions.

5.88. The latest IMF Manual (BPM6) has carried forward the process of disaggregation of data in light of developments and innovations that have taken place in the financial sector in the past two decades. The emergence of new financial instruments and arrangements among institutional units necessitates significant changes in India's BoP presentation to make it more meaningful and inclusive. The BPM6 requires separate treatment of new instruments, such as financial derivatives, employee stock options (ESOPs), securitisation, index-linked securities,

and gold accounts. These instruments have become quite significant in recent years and it is essential to capture financial derivative transactions explicitly in the financial accounts to make the BoP presentation more representative and accurate. As outlined in BPM6, there is a need to include innovative institutional arrangements like special purposes entities and complex, multi-economy corporate structures. This calls for collecting more disaggregated data and new categories of data hitherto not captured by our extant reporting mechanism.

5.89. In the context of financial accounts, as recommended by BPM6, there is a need to improve the coverage and data integrity of direct investment, especially in cases of long and complex chains of ownership. In this regard, timely reporting of data once the transaction is over is of paramount significance. Revised/disaggregated treatment of insurance and other financial services has to be done expeditiously. As recommended in the Manual, expanded treatment on the issues of loan impairments, debt reorganisation, guarantees, and write-offs, which entails more disaggregated data is needed. Further, better reporting of such financial transactions, will have to be attempted. All these steps will bring India's BoP presentation broadly in line with the IMF's revised format and will facilitate international comparisons.

## Chapter VI: Foreign Exchange Reserves

6.1. Reserve assets constitute an important component of the financial account in the BoP statistics and an essential element in the analysis of the economy's external position. As per BPM6, reserve assets are defined as “those external assets that are readily available to and controlled by monetary authorities for meeting BoP financing needs, for intervention in exchange markets to affect the currency exchange rate, and for other related purposes (such as maintaining confidence in the currency and the economy, and serving as a basis for foreign borrowing).”

6.2. Reserve assets comprise foreign exchange assets (currency, deposits, securities and financial derivatives), monetary gold, SDR holdings, reserve position in the IMF and other claims (loans and other financial instruments).

### ***Concept and Coverage***

#### **Foreign Exchange Assets**

6.3. This includes deposits that are available on demand and redeemable at very short notice without unduly affecting the value of the deposit. Deposits that form part of reserve assets are those held in foreign central banks, the BIS, and other non-resident deposit-taking corporations, as well as deposit agreements with IMF Trust Accounts that are readily available to meet a BoP financing need.

6.4. Equity and debt securities issued by non-residents that are liquid and marketable form a part of reserves. Unlisted securities, unless liquid, are, in principle, excluded.

6.5. Financial derivatives that (i) pertain to the management of reserve assets, (ii) are integral to the valuation of such assets, and (iii) are within the effective control of the monetary authorities, are recorded as reserves provided their underlyings are foreign exchange assets. These positions are recorded on a net basis (assets less liabilities) at market value.

## Monetary Gold

6.6. Monetary gold is defined as gold to which the monetary authorities have title and is held as reserve assets. It comprises gold bullion and unallocated gold accounts with non-residents that give title to claim the delivery of gold. Gold accounts must be readily available upon demand to the monetary authorities to qualify as reserve assets.

6.7. Gold bullion can be a financial asset (monetary gold) or a good (non-monetary gold), depending on the holder and the motivation for holding. Monetisation is the change in the classification of gold bullion from non-monetary to monetary. Demonetisation is change in the classification of gold bullion from monetary to non-monetary. Transactions involving monetary gold are recorded in the financial account only if they occur between two monetary authorities for reserve purposes or between a monetary authority and an international financial organisation. When a monetary authority sells gold bullion that is a reserve asset to a non-resident entity which is not a monetary authority or international financial organisation, an entry for non-monetary gold is recorded in the goods and services account.

## Special Drawing Rights (SDRs)

6.8. SDRs are international reserve assets which are created by the IMF and are periodically allocated to members of the IMF in proportion to their quotas. SDR balances are equivalent to liquid balances in convertible currencies in almost every aspect. The values of SDRs are determined by the IMF on a daily basis by taking the weighted average of a basket of currencies. The basket and weights are subject to revision from time to time. SDRs can be used to acquire other members' currencies, to settle financial obligations, and to extend loans. Changes in the SDR holdings of the central bank may occur on account of (i) transactions involving SDR payments to or receipts from the IMF, other participants in the SDR Department of the IMF, or other holders, or (ii) allocation or cancellation. According to BPM5, transactions specified under (i) are included in the BoP, while allocations or cancellations are not included in the BoP but are shown in the international investment position. The allocation of SDRs by the IMF creates foreign assets which add to the holding of official foreign exchange reserves of the member country participating in the SDR account

of the IMF; the item showing allocation (credit) forms the counterpart that offsets the increase in the holding of official foreign exchange reserves as a result of such an allocation.

### ***Treatment of SDRs under BPM6***

6.9. As per BPM6, new allocations of SDRs to participants are recorded as increases in gross reserve assets (holdings of SDRs) and under long-term debt liabilities of the authorities (allocations of SDRs). The main changes in the treatment of SDRs under the updated standards are the recognition of the SDR allocation as a long-term debt liability and the recording of transactions in both assets and liabilities, instead of valuation adjustments to international investment positions when there are new allocations of SDRs. The value of the SDR allocation and loans from the IMF to monetary authorities are included in reserve-related liabilities. Thus, SDR allocations should be treated as liabilities to non-residents (foreign liabilities) and reported as liabilities under “other investments” of the financial account of the BoP.

6.10. According to BPM6, “reserve-related liabilities are defined as foreign currency liabilities of the monetary authorities that can be considered as direct claims by non-residents on the reserve assets of an economy.” These liabilities are not identified as such in the standard components of the BoP and the IIP, and are included in other categories (portfolio and other investment). Apart from SDR allocation, other reserve-related liabilities include foreign currency loans and deposit liabilities of the monetary authorities to non-residents, including those on account of foreign currency swaps with other central banks, and loans from BIS and other deposit-takers. It also includes foreign currency loan liabilities to non-residents associated with securities that the monetary authorities have repo-ed out; foreign currency securities issued by the monetary authorities and owed to non-residents; and other foreign currency liabilities to non-residents, including foreign currency accounts payable and financial derivatives.

### **Reserve Position in the IMF**

6.11. Reserve tranche positions (RTP) in the IMF are, in simple terms, liquid claims of members on the IMF that arise not only from the reserve asset payments for quota

subscriptions but also the member country's lending to the IMF under the General Resources Account.

6.12. The subscription of the quota consists of two components: (i) foreign exchange component and (ii) domestic currency component. Under the foreign exchange component, a member is required to pay 25 per cent of its quota in SDRs or in foreign currencies acceptable to the IMF (*i.e.*, hard currencies). This is termed “reserve position in the IMF or reserve tranche” and is part of the member country’s reserve assets. In the BoP, such subscription is shown as a transaction involving a reduction in other reserve assets (credit), and is offset by an increase in the reserve tranche position in the IMF (debit). The remaining 75 per cent of the quota is payable either in cash or securities denominated in the member country’s own currency (*i.e.*, domestic currency component) and normally held within the country at a designated depository, normally the country’s central bank in the IMF A/C No. 1 and No. 2 or IMF Securities Account, as the case may be. The domestic currency component of the quota is considered in economic terms to be of a contingent nature and so is not classified as an asset or liability in the international accounts and, hence, is not recorded in the country’s BoP or IIP.

### **Other Claims**

6.13. Other claims include loans to non-resident non-deposit-taking corporations, long-term loans to an IMF Trust Account that are readily repayable to meet a BoP financing need, loans arising from a reverse repo (unless classified as deposits), and other financial assets not included previously but that are foreign currency assets that are available for immediate use (such as non-negotiable investment fund shares or units).

### ***Treatment of Reserves in India’s Balance of Payments***

6.14. India’s foreign exchange reserves consist of external assets which are readily available to and controlled by the RBI for meeting balance of payment financing needs, for intervention in exchange markets to stem the volatility of exchange rate of the Rupee, and for other related purposes. At present, India’s foreign exchange reserves include foreign currency assets held by the RBI, gold, SDRs and RTP in the IMF. In India, SDRs are held in government books and, therefore, are not part of the foreign currency assets of the RBI but a



component of foreign exchange reserves. RTP has been included in foreign exchange reserves from April 2, 2004 as per international best practices. A change in reserves serves as the financing item in India's BoP. The overall balance (sum of the current account balance, capital account balance and errors & omissions) corresponds to the change in reserves with the opposite sign. In other words, the net credit/debit position in the overall balance is matched by the opposite entry in the reserves to denote an increase in reserves (debit) and or a decline in reserves (credit), respectively.

6.15. Generally, the movement in reserves is extracted from the stock of reserves. The stock figures include both 'real' changes in reserves as well as the valuation effects. The foreign currency assets of the RBI, though expressed in terms of US dollars, comprise other hard currencies such as the Euro, Sterling, Yen, *etc.* Therefore, movement in the cross-currency exchange rates of these currencies affects the stock of foreign currency assets of the RBI, which are expressed in US dollars. In the case of gold, valuation arises on account of changes in the international prices of gold, as gold held as reserves are valued at 90 per cent of the average London market price of gold during the month, while movement in the SDR/ US\$ exchange rate affects the valuation of SDR holdings and the RTP. As the BoP only records actual changes in the reserves, the valuation effect embedded in the stock has to be removed. The valuation effect is worked out by finding the difference between the stock of reserves at the end of the reference period expressed in terms of the current exchange rate and the same stock expressed at the exchange rate prevailing at the beginning of the reference period.

6.16. Gold (*i.e.*, monetary gold) is an asset owned by the RBI and is interpreted to be at least 9995/9999 pure. Transactions in gold occur only between the RBI and its counterparts, such as the central banks of other countries, or between the RBI and international monetary organisations. Gold is a reserve asset for which there is no outstanding financial liability. As per extant practice, in the case of purchase (or sale) of gold by the Reserve Bank from an entity other than a central bank or an international organisation, the acquisition/ sale of gold is recorded as an import (debit)/export (credit) under goods in the current account, and with contra credit/debit entries in the reserve (monetary gold) account. The BPM6, however, has suggested that only gold transactions with non-resident entities should be captured under the BoP (no transactions should be recorded under BoP if the counterparty is a resident). As a result, if the gold is acquired by the RBI from the government, it will not be recorded

henceforth in India's BoP; they were earlier recorded under “non-monetary gold” (credit) under merchandise with a contra entry (debit) under monetary gold (reserves).

6.17. As regards RTP arising out of subscription to the IMF quota increase, the 25 per cent of the quota paid in hard currency forming part of RTP is shown in India's BoP as a debit entry against “IMF Quota” with a credit entry (decrease in assets) under foreign currency reserves (either under foreign currency assets of the RBI or SDR holdings, as the case may be). This does not change the level of foreign exchange reserves as the loss of reserves, either under foreign currency assets or under SDR holdings, is fully offset by an increase in the reserve position in the IMF as the latter is also a part of foreign exchange reserves. The remaining 75 per cent of India’s quota is paid in non-negotiable non-interest bearing government securities by depositing them in IMF Account No. 1 held with the RBI, which was hitherto shown as a debit entry against “IMF quota” with a contra entry under “miscellaneous or other capital receipts”. So, the entry against IMF quota (debit) depicted the whole amount of the quota increase paid to the IMF (both the foreign currency component and the rupee securities issued in favour of the IMF for the domestic currency component of the quota subscription) with a contra entry (credit) under (i) “reserves” (for the foreign currency component), and (ii) “Miscellaneous or other capital receipts” (for rupee securities issued to the IMF) to show that India's liabilities to the IMF have gone up as these securities are owned by the IMF though held in India.

6.18. The rupee securities issued to the IMF were considered as both assets and liabilities. This treatment was in conformity with the earlier guidelines of the IMF. However, as per the latest edition of the Manual (BPM6), the domestic currency component of the IMF quota payment, which is paid either in the domestic currency or securities, does not entail any impact on the BoP or IIP on a net basis, since such securities are both assets and liabilities. Therefore, henceforth the domestic currency component of the IMF quota payment will not be shown in India's BoP statistics.

6.19. The allocation of SDRs by the IMF to India is included as a credit entry in “other capital” of the capital account of India’s BoP to show the increase in India's liabilities to the IMF, with a counter debit entry in the SDR holdings under reserve assets showing an increase in India's foreign exchange reserves.

6.20. At the beginning of the current decade, the IMF designated India as a creditor country under its Financial Transaction Plan (FTP) as India had a surplus BoP position. Under the scheme, the domestic currency (securities) held by the IMF under the quota subscription is converted into foreign currency, as a result of which the share of the foreign currency component (RTP) goes up with a corresponding decline in the share of the domestic currency component of the quota, without altering the total amount of quota subscription by the country in question. India's participation in FTP also enabled the IMF to replace its rupee holdings under India's quota contribution with hard currency. India made the contribution to the FTP by way of making a payment to the IMF in hard currency by debiting the Government account held with it for the rupee-equivalent amount, which is realised by encashing the rupee securities issued earlier to the IMF towards quota payment. As a result, there was an increase in the reserve tranche position with the IMF with an equivalent decline in the foreign currency assets of the RBI, implying that the level of foreign exchange reserves remained unaltered. However, the rupee component of the IMF quota subscription came down with a corresponding increase in the share of hard currency in the total quota subscription. These entries were reversed when India received these contributions back from the IMF consequent on the completion of India's participation in the scheme when the borrowing countries repaid their loans to the IMF.

## Attachment I: Constitution of the Group

### RESERVE BANK OF INDIA

#### Working Group on Balance of Payments Manual for India

The Reserve Bank had last published Balance of Payments Compilation Manual in 1987. The methodology of compilation has evolved subsequently with the improvement and availability of disaggregated data on Balance of Payments (BoP). In the meanwhile, the International Monetary Fund (IMF) has come out with its revised Balance of Payments Manual 6 (BPM6) in 2009.

2. In view of the above, it is proposed to constitute a 'Working Group on Balance of Payments Manual for India' to draft a comprehensive manual/guidelines on the definition, methodology, coverage and compilation of Balance of Payments (BoP) in India consistent with the international best practices.

3. The tentative Terms of Reference of the Working Group are as under:

- (a) To review the existing methodology for compilation of Balance of Payments Statistics in India consistent with the IMF's Balance of Payment Manual (BPM6).
- (b) To prepare a Manual for compilation of the balance of payments statistics for India in line with international best practices.
- (c) To examine the issue of divergence between the merchandise trade data on customs basis released by the Directorate General of Commercial Intelligence and Statistics (DGCI&S), Ministry of Commerce and Industry, and the banking channel data on payments basis released by the Reserve Bank of India and suggest measures to reconcile the two.
- (d) To explore the feasibility of capturing of possible international transactions at a disaggregated level that may arise in future as a result of ongoing liberalization of financial markets and innovation of financial instruments.


4. The constitution of the Group would be as follows:

Shri Deepak Mohanty, Executive Director, RBI: Chairman  
Shri Anil Bisen, Adviser, Ministry of Finance, GOI: Member  
Controller, Aid, Accounts and Audit (CAA&A) Division, GOI: Member  
Shri Nilachal Ray, Director General, DGCI&S: Member  
Shri Salim Gangadharan, CGM-in-Charge, FED, RBI: Member.  
Dr. Balwant Singh, Adviser, DSIM, RBI: Member  
Dr. R.K.Pattnaik, Adviser, DEAP, RBI: Member  
Dr. Rajiv Ranjan, Director, DIF, DEAP, RBI: Member-Secretary

5. The Working Group may co-opt any other Member as may be necessary.

6. The Division of International Finance (DIF), DEAP would provide secretarial assistance to the Working Group.

7. The Working Group is expected to submit its Report along with the revised BoP Manual for India within six months from its first meeting.

  
(Rakesh Mohan)  
Deputy Governor  
May 12, 2009

## **Attachment II: Minutes of Meetings**

### **First Meeting of the Working Group on Balance of Payments Manual for India held on July 17, 2009 at RBI, Central Office, Mumbai - Minutes**

The first meeting of the Working Group on Balance of Payments Manual of India was held on July 17, 2009 at the Reserve Bank of India, Central Office, Mumbai. Members/ representatives from Directorate General of Commercial Intelligence and Statistics (DGCI&S), Controller of Aid, Accounts and Audit (CAA&A), Government of India and concerned Departments of the Reserve Bank of India attended the meeting. Shri G. Bhujabal, Economic Adviser, Ministry of Commerce & Industry, Dr. J. Poddar, Director, DGCI&S and a representative from NASSCOM attended the meeting as special invitees. The list of the participants is enclosed at Annex.

At the outset, Shri Deepak Mohanty, Executive Director, welcomed the members and participants and highlighted the need for compiling a comprehensive Balance of Payments (BoP) Manual for India in the light of ongoing changes and innovations in the international financial transactions and consistent with the IMF's Balance of Payments Manual, sixth edition, (BPM6) published recently. A brief presentation was made by the officials of RBI highlighting the historical background, recent challenges in BoP compilation and data related issues, rationale behind revising the earlier Manual (1987) in line with the BPM6 of the IMF and a tentative chapter scheme for the proposed Manual.

Shri D. Sinha, Director General, DGCI&S, in his introductory remarks said that the recommendations of the Report of the S. K. Nath Committee are yet to be implemented. The major reason for divergence between the DGCI&&S and RBI data is due to non-availability of data particularly from shipping, civil aviation, small ports, and SEZs. There is a need to establish a channel so as to minimize the loss of data from the sources of reporting and the flow of the data to be made regular to the DGCI&S. Shri J. Podar, DGCI&S, added that even there seems to be loss of data reported by the customs that are collected manually from the small ports and SEZs. Once it is streamlined, the data gap could be reconciled. Shri D. Mishra, FED, noted that the accuracy of data depends on the quality of information reported by the Authorised Dealers (ADs). He also pointed out that the divergence in the data could also be because of reporting of advance payments and trade credit in the banking channel data. Shri G. Bhujabal, Ministry of Commerce and Industry, GOI, said that

there is a need to put in place a system of revision of monthly data corresponding to the cumulative data. He also highlighted the need to formulate a policy of data revision and dissemination of information.

Shri Balwant Singh, DSIM, pointed out that the issue of misclassification while reporting the services data especially in miscellaneous component has come down in recent years. On the issue of survey on outward portfolio investments, Shri A. P. Gaur, DSIM, said that the large value transactions of high net-worth individuals are not being included. He also informed that DSIM has conducted a survey on the software exports and the results are satisfactory and is consistent with NASSCOM data. Ms. Diksha Nerurkar informed that NASSCOM compiles data on software exports through survey of software companies. On capturing the data, there are two major issues *viz.*, definitional and categorization of information, that needs to be addressed. Shri S. D. Sharma, CAA&A, informed that as regards to the external debt data, there are problem in reconciliation of rupee debt with that of the World Bank due to exchange rates.

The major highlights/action points of the discussion are as follows:

- (i) It was suggested that the annual data on BoP since 1948-49 may be placed on the CDBMS data warehouse of the RBI.
- (ii) A survey may be conducted to find out a factor for adjusting DGCI&S export data for valuation and timing, which is now taken as 2 per cent.
- (iii) It was also suggested to re-examine the difference in data between DGCI&S RBI for the year 2008-09 based on the final data with late receipts.
- (iv) It was suggested to rationalize the classification of purpose code for reporting the data from banks/ ADs keeping in view the usefulness of the reporting system and also the comfort of Ads.
- (v) It was suggested that the IIP and the BoP could be brought out on the same day. It was agreed in the meeting that DEAP would provide necessary data in advance to DSIM so as to facilitate the simultaneous release.
- (vi) It was agreed that some surveys on a regular basis could be conducted to supplement the reporting by the ADs under FETERS.
- (vii) It was suggested that the Report of the Working Group may be structured in two parts. Part I of the Report would present reviews, findings and recommendations of the Group, while Part II of the Report would provide a Comprehensive Manual on Balance of Payments for India for the compilers.

## **List of Participants**

### **A. Government of India**

1. Shri G. Bhujabal, Economic Adviser, Ministry of Commerce & Industry, GOI
2. Dr. D. Sinha, Director General, DGCI&S, GOI
3. Shri S. D. Sharma, Joint Controller, CAA&A, GOI
4. Dr. J. Poddar, Director, DGCI&S, GOI

### **B. NASSCOM**

5. Ms. Diksha Nerurkar, Manager, Research, NASSCOM
- 6.21.

### **C. Reserve Bank of India**

6.22.

6. Shri Deepak Mohanty, Executive Director, RBI
7. Dr. Balwant Singh, Adviser, DSIM, RBI
8. Shri D. Mishra, Chief General Manger, FED, RBI
9. Shri S. V. S. Dixit, Adviser, DEAP, RBI
10. Shri A. P. Gaur, Director, BPSD, DSIM, RBI
11. Dr. Rajiv Ranjan, Director, DIF, DEAP, RBI
12. Smt. Rekha Misra, Director, DIT, DEAP, RBI
13. Shri V. K. Srivastava, Assistant Adviser, DEAP, DIF, RBI
14. Shri Binod B. Bhoi, Research Officer, DEAP, DIF, RBI
15. Shri Harendra Behera, Research Officer, DEAP, DIF, RBI

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## **Meeting on Trade in Services held in RBI on May 18, 2010: Minutes**

A meeting was held at RBI, Mumbai on May 18, 2010 between the officials from Department of Commerce (DoC), DGCI&S, and RBI to deliberate on issues related to compilation of disaggregated data on trade in services in line with the extended balance of payment statistics (EBOPS) of the IMF. The following action points emerged from the meeting:

1. **Travel Receipts:** it was agreed that data on travel receipts would be provided at more disaggregated level. In view of the present constraint in reporting under the FETERS purpose code followed by the RBI, it was felt that other alternatives should be explored. In this regard, it was suggested by RBI in the meeting that Department of Commerce could coordinate with Bureau of Immigration, Ministry of Home Affairs to gather the necessary information. Also, to get disaggregated data on tourist expenses in India, Ministry of Tourism should be advised to conduct surveys on expenditure pattern of tourists coming to India on a regular basis.

**(Action: Department of Commerce)**

2. **Transportation:** Disaggregated data provided to IMF by the RBI in the form of freight and passenger receipts separately would be incorporated in the invisibles articles as well.

**(Action: RBI, DEAP)**

It was agreed that the actual data on freight and insurance available separately with the Department of customs should be used for bifurcating freight and passenger receipts. In this regard, DSIM/DGCI&S were requested to follow up with the Department of customs to get the consolidated data on freights.

**(Action: DGCI&S; RBI, DSIM)**

3. **Communication:** Disaggregated data on communication services would be provided as per the FETERS purpose code.

**(Action: RBI, DEAP)**

4. **Construction:** A need was felt for disaggregated data on construction services to be reported under EBOPS. In this context, it was explained by the RBI that while the current form of reporting captures data in the compiling country, there is no provision for capturing data on construction abroad. Accordingly, it was agreed that a new purpose code under FETERS would be introduced under receipts side when the purpose code revised by the RBI.

**(Action: RBI, DSIM)**

5. **Insurance:** Disaggregated data would be provided as per the FETERS purpose code. Regarding covering the pension funds, it was agreed to explore the possibility of getting data from alternative sources such as pension funds regulatory authority of India (PFRDA).

**(Action: RBI, DEAP)**



**6. Financial Services:** Disaggregated data would be reported as per the FETERS purpose code.

**(Action: RBI, DEAP)**

7. Findings of the survey on international trade in banking Services conducted regularly by the RBI may also be provided as annex in the article on invisibles published by the RBI.

**(Action: RBI, DEAP)**

**8. Royalty and License Fee:** Disaggregated data would be reported as per the FETERS purpose code covering franchisee services.

**(Action: RBI, DEAP)**

**9. Personal, Cultural and Recreational Services:** A need was felt for disaggregated data especially on health and on education under this category. As the RBI data only provides consolidated position, DoC was requested to explore the possibility of getting such disaggregated information on health services and education services from the respective ministries. However, it was agreed that when RBI revises its purpose code, a separate code would be assigned to extract necessary information.

**(Action: Department of Commerce, RBI, DSIM)**

10. **Country wise data:** It was agreed that DSIM would provide the country-wise data under 11 Standard categories to the Ministry regularly. Ministry may use this information internally and for their trade negotiations purpose taking in to account the limitations of the data. It was also agreed that the confidentiality of these data would be maintained and would not be released to the public by the MoC.

**(Action: Department of Commerce; RBI, DSIM)**

**11. Manufacturing Services not included elsewhere:** IMF's balance of payment manual-VI<sup>th</sup> Edition (BPM-6) suggests the inclusion of these services in the standard BOP presentation. Accordingly, Department of Customs would be requested to include a new code in their reporting system to capture such data. The matter would be taken up with the Department of Customs.

**(Action: RBI, DEAP)**

12. **IT & ITES:** Findings of the Survey on IT & ITES conducted and published by DSIM may also be provided as annex in the article on invisibles published by RBI.

**(Action: RBI, DEAP)**

13. Foreign collaboration survey: Results of the comprehensive foreign collaboration survey launched by the RBI for the years 2007-08, 2008-09 and 2009-10 which will also provide country wise and sector wise details, when available, to be published by the RBI on its website. These results will provide useful information on trade through commercial presence (mode 3).

**(Action: RBI, DSIM)**

14. Concordance table between GNS/W/120, CPC Provisional, EBOPS and Purpose Codes: RBI agreed to examine and complete the concordance developed by DG, DGCI&S between GNS/W/120, CPC Provisional, EBOPS and Purpose Codes used by RBI.

**(Action: RBI)**

15. **Medium term and Long term issues of collecting data on Trade in Services through Surveys:** In accordance with the international best practices with regard to collection of statistics on trade in services, India should supplement the information on foreign exchange transactions reported through banking channel with regular surveys / census to gather the necessary details. Therefore DOC may explore the possibility of holding subject based surveys in cooperation with Department of Statistics, concerned Ministries such as Health, Education, Urban Development, Tourism, Telecom etc. and other stakeholders.

**(Action: Department of Commerce, DGCI&S)**

**List of Officers who attended the meeting on ‘Trade in Services’ held at  
Conference Room No 3 on May 18, 2010 and their contact details**

<b>Name</b>	<b>Designation/Organisation</b>	<b>Contact No.</b>	<b>E-mail id</b>
Shri S V S Dixit	Adviser, DEAP, RBI	022-22610824	svsdixit@rbi.org.in
Shri AP Gaur	Adviser, DSIM, RBI	9820422295	apgaur@rbi.org.in
Dr. Dipankar Sinha	Director General, DoC, DGCI&S	033-22485702	drdsinha@rediffmail.com
Smt. Sushmita Dasgupta	Addl. Economic Adviser, DoC, GoI	011-23061746 9818244035	sushmita.dg@nic.in
Shri Rajan Goyal	Director, DEAP, RBI	022-22610828	rgoyal@rbi.org.in
Smt. Aparna Sinha	Joint Director, DoC, GoI.	011-23062286	jd1tpd-doc@nic.in
Smt Anita Mehta	Assistant General Manager, FED, RBI	022-22603000, Extn. 4503	anitamehta@rbi.org.in
Shri Binod B. Bhoi	Assistant Adviser, DEAP, RBI	022-22602236	binodbhoi@rbi.org.in
Shri A K Jha	Research Officer, DEAP, RBI	022-22601000 Extn. 2720	akjha@rbi.org.in
Shri Harendra Behera	Research Officer, DEAP, RBI	022-22601000 Extn. 2261	harendra@rbi.org.in
Shri Rajesh Kavediya	Research Officer, DSIM, RBI	022-26571265 Extn. 7340	rkavediya@rbi.org.in
Shri Vivek Kumar	Research Officer, DSIM, RBI	022-26572695	vivekkumar@rbi.org.in
Shri Vishal Maurya	Research Officer, DSIM, RBI	022-26571261 Extn. 7230	vmaurya@rbi.org.in
Smt. Usha Prabhu	Asst. Manager, DEAP, RBI	022-22601000 Extn. 2738	uaprabhu@rbi.org.in
Shri R S Potdar	Asst. Manager, FED, RBI	022-22603000 Extn. 4515	rspotdar@rbi.org.in

## **Second Meeting of the Working Group on Balance of Payment Manual held at RBI Mumbai on June 28, 2010: Minutes**

The second meeting of the Working Group on Balance of Payments Manual was held at RBI, Mumbai on June 28, 2010 to discuss on the draft chapters of the Manual. The meeting was chaired by the Executive Director, Shri Deepak Mohanty. Members/representatives from DGCI&S, Department of Economic Affairs, Department of Commerce, Department of Civil Aviation, NASSCOM, DSIM attended the meeting. A detailed list of participants is attached in the annex.

At the outset, ED(DM) welcomed the participants and briefed on the structure of the manual and sought comments from the members/participants on the draft chapters. A brief presentation was made on the draft chapters, which was followed by discussions. The major highlights/action points of the discussions are as follows:

In order to comply with the presentation of merchandise trade data as per the IMF's Balance of Payment Manual Sixth Edition (BPM-6), the group felt the need for presenting data on imports on FOB basis in line with international best practices. In order to move away from the present practice of reporting of imports on CIF basis to FOB basis, freight and insurance on imports needs to be adjusted for. Accordingly, it was felt that DGCI&S would explore the possibility of estimating freight and insurance from the DTR returns. It was also felt that ideally a survey would be appropriate to capture these information.

**(Action: DGCI&S)**

In order to comply with the presentation of exports as per the BPM-6, it was suggested by Dr. D Sinha, Director General, DGCI&S, that an additional code for re-export will have to be introduced at the custom's end. The group felt that DGCI&S will pursue with the custom authorities in this regard. **(Action: DGCI&S/Department of Customs)**

Apart from DGCI&S pursuing the matter with the Customs, ED(DM) suggested that introduction of a purpose code for re-export under FETERS may be explored. The possibility of conducting a survey in this regard was also suggested. Adviser (APG) pointed out that merchanting under FETERS covers only commission part and therefore, the issue of covering net exports under merchanting and re-exports under FETERS need further examination.

**(Action: DSIM, RBI)**

Additionally, ED(DM) desired that a preliminary exercise may be done to find out the number of countries reporting such disaggregated data to the IMF for IFS.

**(Action: DEAP, RBI)**

Shri Anil Bishen, Adviser, DEA, MOF highlighted the need for bringing out the discrepancies the DGCI&S and RBI data on merchandise trade. Adviser (SVSD) agreed to incorporate this aspect appropriately in the manual. In this regard, it was noted that various earlier Committees had examined the issue of discrepancies between the two sources of data and suggested ways for reconciliation of the same. It was pointed out that aircraft on financial lease was one of the sources of such discrepancies earlier. The representative from Department of Civil Aviation noted that such data are now being covered by the DGCI&S.

**(Action: DEAP, RBI)**

During the presentation, attention was drawn to the introduction of two new service categories namely 'Manufacturing services on physical inputs owned by others' and 'Maintenance and repair services n.i.e.' under the BPM-6. In order to comply with this standard form of presentation, the group felt that two new purpose codes with suitable description to capture these services need to be introduced under FETERS.

**(Action: DSIM, RBI)**

Regarding software services, attention was drawn to differences between NASSCOM and FETERS data. In this context, it was explained that banking channel data represent about 80-85 per cent of NASSCOM data. In this context, the group felt the need for reconciliation of two sources of data. Ms. Nerurkar of NASSCOM pointed out that there should not be much difference between the two sources and NASSCOM would be willing to resolve any data related issues with RBI. Since NASSCOM data are used for BOP compilation, which is available on annual basis and therefore, a need was also felt for quarterly break down of the same for compilation of quarterly BOP. Accordingly, NASSCOM was requested to look in to the feasibility of providing such break-ups.

**(Action: NASSCOM/DSIM, RBI)**

Dr. Sinha, DGCI&S, pointed out that country wise and purpose wise breakup of software exports is important from the perspective of trade negotiations. Further, Shri Bishen enquired whether information on front-end and back-end activity of software services would be available with NASSCOM. In this regard, NASSCOM clarified that they are having region wise details but purpose wise details are not readily available. In view of the importance of India's software service exports, NASSCOM was requested to explore the feasibility of providing country wise and purpose wise information.

**(Action: NASSCOM)**

The group felt that eventually there should be shift towards using banking channel data (FETERS) for the purpose of BOP compilation and using the NASSCOM data for cross validation.

**(Action: DSIM/DEAP, RBI)**

The group felt that eventually there should be shift towards using banking channel data (FETERS) for the purpose of BOP compilation and using the NASSCOM data for cross validation.  
**(Action: DSIM/DEAP, RBI)**

It was pointed out that while the banking channel was adequately capturing travel related payments, there are deficiencies as far as reporting of travel receipts are concerned. Accordingly, the group felt that the present practice of using estimates for travel receipts needs to be strengthened further supported by periodic surveys. In this context, the group pointed out that the Ministry of Tourism is the appropriate agency to conduct the survey in this regard. Attention was drawn to the special meeting on Disaggregation of Trade in Services held in RBI on May 18, 2010, where it was agreed that Department of commerce would follow up the matter with the Ministry of Tourism.

**(Action: Department of Commerce)**

The group felt that eventually there should be shift towards using banking channel data (FETERS) for the purpose of BOP compilation and using the NASSCOM data for cross validation.  
**(Action: DSIM/DEAP, RBI)**

6.23. As suggested in BPM-6, the group felt the need for switching to standard format of presentation of the capital and financial account of BoP separately in line with international best practices. ED(DM) pointed out that such bifurcation would only need reclassification and renaming of many items that are already being captured presently for compilation of capital account. In this context, Shri Bishen suggested that the manual should provide clear explanations for the switch.  
**(Action: DEAP, RBI)**

It was pointed out that, the present definition used for classifying the Foreign Direct Investment (FDI) in India is at variance with the definition suggested in the BPM-6 to the extent that the threshold limit of 10 per cent is not strictly adhered to. In turn, the threshold is reached indirectly through segregating the portfolio investment. In this regard, ED(DM) noted that if our definition is broad enough to cover appropriately the concept of lasting interest and control in our country context, we need not simply follow the threshold as followed internationally. ED(DM) also suggested to find out whether there are any other country practices that differs from the criterion of threshold for classifying FDI.

**(Action: DEAP, RBI)**

In view of the growing importance of financial derivatives in international transactions, it was felt that such information should be adequately captured in our BoP, which is not being captured at present. In this context, Shri Bishen suggested that a separate Committee be set up to look in to the details of capturing such transactions in BoP. ED(DM) agreed that a separate group should study the matter in detail and recommends for their incorporation in the BoP.

**(Action: DEAP, RBI)**

6.24. In order to comply fully with the standard form of presentation of financial account as suggested in the BPM-6, it was suggested that we should explore the possibility of recording financial transactions on a net basis. ED(DM) mentioned that this aspect may be examined further.

6.25. **(Action: DEAP/DSIM/FED, RBI)**

There was a broad agreement on the proposed structure of the BoP manual for India. However, the Group felt that the manual may be appended as an annex to the Group's Report, which would be a synoptic report of about 10-15 pages providing the rationale for the new manual, the standard form of presentation of BoP in line with the international best practices, the compilation procedures followed in India and the data sources as well as the recommendations of the Group in detail. It was also agreed that the implementation schedule in a phased manner may also be spelled out in line with BPM-6 implementation schedule. ED(DM) noted that the draft report may be circulated among the members for their comments before finalization.

**(Action: DEAP, RBI)**

### Attachment III: Standard Format of BoP Presentation

Standard Presentation of BoP in India as per BPM6			
Item	Credit	Debit	Net
<b>1. Current Account (1.A+1.B+1.C)</b>			
<b>1.A Goods and Services (1.A.a+1.A.b)</b>			
<b>1.A.a Goods (1.A.a.1+1.A.a.2+1.A.a.3)</b>			
1.A.a.1 General merchandise on a BOP basis			
<i>Of which: 1.A.a.1.1 Re-exports</i>			
1.A.a.2 Net exports of goods under merchanting			
1.A.a.2.1 Goods acquired under merchanting (negative credits)			
1.A.a.2.2 Goods sold under merchanting			
1.A.a.3 Nonmonetary gold			
<b>1.A.b Services (1.A.b.1+1.A.b.2+1.A.b.3+1.A.b.4+1.A.b.5+1.A.b.6+1.A.b.7+1.A.b.8+1.A.b.9+1.A.b.10+1.A.b.11+1.A.b.12)</b>			
1.A.b.1 Manufacturing services on physical inputs owned by others			
1.A.b.1.1 <i>Goods for processing in reporting economy</i>			
1.A.b.1.2 <i>Goods for processing abroad</i>			
1.A.b.2 Maintenance and repair services n.i.e.			
1.A.b.3 Transport			
1.A.b.3.1 Sea transport			
1.A.b.3.1.1 Passenger			
1.A.b.3.1.2 Freight			
1.A.b.3.1.3 Other			
1.A.b.3.2 Air transport			
1.A.b.3.2.1 Passenger			
1.A.b.3.2.2 Freight			
1.A.b.3.2.3 Other			
1.A.b.3.3 Other modes of transport			
1.A.b.3.3.1 Passenger			
1.A.b.3.3.2 Freight			
1.A.b.3.3.3 Other			
1.A.b.3.4 Postal and courier services			
1.A.b.3.4.1 Sea transport			
1.A.b.3.4.2 Air transport			
1.A.b.3.4.3 Other modes of transport			
1.A.b.3.0.1 Passenger			
1.A.b.3.0.2 Freight			
1.A.b.3.0.3 Others			
1.A.b.4 Travel			
1.A.b.4.1 Business			
1.A.b.4.2 Personal			
1.A.b.4.2.1 Health-related			
1.A.b.4.2.2 Education-related			
1.A.b.4.2.3 Other			



1.A.b.5 Construction			
1.A.b.5.1 Construction abroad			
1.A.b.5.2 Construction in the reporting economy			
1.A.b.6 Insurance and pension services			
1.A.b.6.1 Direct insurance			
1.A.b.6.2 Reinsurance			
1.A.b.6.3 Auxiliary insurance services			
1.A.b.6.4 Pension and standardized guarantee services			
1.A.b.7 Financial services			
1.A.b.7.1 Explicitly charged and other financial services			
1.A.b.7.2 Financial intermediation services indirectly measured (FISIM)			
1.A.b.8 Charges for the use of intellectual property n.i.e.			
1.A.b.9 Telecommunications, computer, and information services			
1.A.b.9.1 Telecommunications services			
1.A.b.9.2 Computer services			
1.A.b.9.3 Information services			
1.A.b.10 Other business services			
1.A.b.10.1 Research and development services			
1.A.b.10.2 Professional and management consulting services			
1.A.b.10.3 Technical, trade-related, and other business services			
1.A.b.11 Personal, cultural, and recreational services			
1.A.b.11.1 Audiovisual and related services			
1.A.b.11.2 Other personal, cultural, and recreational services			
1.A.b.12 Government goods and services n.i.e.			
<b>1.B Primary Income (1.B.1+1.B.2+1.B.3)</b>			
1.B.1 Compensation of employees			
1.B.2 Investment income			
1.B.2.1 Direct investment			
1.B.2.1.1 Income on equity and investment fund shares			
1.B.2.1.2 Interest			
1.B.2.2 Portfolio investment			
1.B.2.2.1 Investment income on equity and investment fund shares			
1.B.2.2.2 Interest			
1.B.2.3 Other investment			
1.B.2.4 Reserve assets			
1.B.3 Other primary income			
<b>1.C Secondary Income (1.C.1+1.C.2)</b>			
1.C.1 General government			
1.C.2 Financial corporations, nonfinancial corporations, households, and NPISHs			
1.C.2.1 Personal transfers (Current transfers between resident and non-resident households) <i>Of which:</i> 1.C.2.1.1 Workers' remittances			
1.C.2.2 Other current transfers			
<b>2. Capital Account (2.1+2.2)</b>			
2.1 Gross acquisitions (DR.)/disposals (CR.) of non-produced			

nonfinancial assets			
2.2 Capital transfers			
2.2.1 General government			
2.2.1.1 Debt forgiveness			
2.2.1.2 Other capital transfers			
2.2.2 Financial corporations, nonfinancial corporations, households, and NPISHs			
2.2.2.1 Debt forgiveness			
2.2.2.2 Other capital transfers			
<b>3. Financial Account (3.1+3.2+3.3+3.4+3.5)</b>			
3.1 Direct Investment			
3.1.1 Equity and investment fund shares			
3.1.1.1 Equity other than reinvestment of earnings			
3.1.1.1.1 Direct investor in direct investment enterprises			
3.1.1.1.2 Direct investment enterprises in direct investor (reverse investment)			
3.1.1.1.3 Between fellow enterprises			
3.1.1.2 Reinvestment of earnings			
3.1.2 Debt instruments			
3.1.2.1 Direct investor in direct investment enterprises			
3.1.2.2 Direct investment enterprises in direct investor (reverse investment)			
3.1.2.3 Between fellow enterprises			
3.2 Portfolio Investment			
3.2.1 Equity and investment fund shares			
3.2.1.1 Central bank n.a.			
3.2.1.2 Deposit-taking corporations, except the central bank			
3.2.1.3 General government n.a.			
3.2.1.4 Other sectors			
3.2.1.0.1 Equity securities other than investment fund shares			
3.2.1.0.2 Investment fund shares/units			
<i>Of which:</i> 3.2.1.0.2.1 Reinvestment of earnings			
3.2.2 Debt securities			
3.2.2.1 Central bank			
3.2.2.2 Deposit-taking corporations, except the central bank			
3.2.2.3 General government			
3.2.2.4 Other sectors			
3.3 Financial derivatives (other than reserves) and employee stock options			
3.3.1 Central bank			
3.3.2 Deposit-taking corporations, except the central bank			
3.3.3 General government			
3.3.4 Other sectors			
3.4 Other investment			
3.4.1 Other equity			
3.4.2 Currency and deposits			
3.4.2.1 Central bank			
3.4.2.2 Deposit-taking corporations, except the central bank			

3.4.2.3 General government			
3.4.2.4 Other sectors			
3.4.3 Loans			
3.4.3.1 Central bank			
3.4.3.2 Deposit-taking corporations, except the central bank			
3.4.3.3 General government			
3.4.3.4 Other sectors			
3.4.4 Insurance, pension, and standardized guarantee schemes			
3.4.4.1 Central bank			
3.4.4.2 Deposit-taking corporations, except the central bank			
3.4.4.3 General government			
3.4.4.4 Other sectors			
3.4.5 Trade credit and advances			
3.4.5.1 Central bank			
3.4.5.2 General government			
3.4.5.3 Deposit-taking corporations			
3.4.5.4 Other sectors			
3.4.6 Other accounts receivable/payable—other			
3.4.7 Special drawing rights			
3.5 Reserve assets			
3.5.1 Monetary gold			
3.5.2 Special drawing rights n.a.			
3.5.3 Reserve position in the IMF n.a.			
3.5.4 Other reserve assets			
3.5.4.1 Currency and deposits			
3.5.4.2 Securities			
3.5.4.3 Financial derivatives			
3.5.4.4 Other claims			
3. Total assets/liabilities			
<i>Of which: (by instrument):</i>			
3.0.1 Equity and investment fund shares			
3.0.2 Debt instruments			
3.0.3 Other financial assets and liabilities			
<b>4. Net errors and omissions</b>			

**Attachment IV: New Purpose Codes For Reporting Forex Transactions  
(FETERS)**

**PAYMENT PURPOSES**

<b>Gr. No.</b>	<b>Purpose Group Name</b>	<b>Purpose Code</b>	<b>Description</b>
00	Capital Account	S0001	Indian investment abroad -in equity capital (shares)
		S0002	Indian investment abroad -in debt securities
		S0003	Indian investment abroad -in branches & wholly owned subsidiaries
		S0004	Indian investment abroad -in subsidiaries and associates
		S0005	Indian investment abroad -in real estate
		S0006	Repatriation of Foreign Direct Investment in India- in equity shares
		S0007	Repatriation of Foreign Direct Investment in India- in debt securities
		S0008	Repatriation of Foreign Direct Investment in India- in real estate
		S0009	Repatriation of Foreign Portfolio Investment in India- in equity shares
		S0010	Repatriation of Foreign Portfolio Investment in India- in debt securities
		S0011	Loans extended to Non-Residents
		S0012	Repayment of long & medium term loans with original maturity above one year received from Non-Residents
		S0013	Repayment of short term loans with original maturity above one year received from Non-Residents
		S0014	Repatriation of Non-Resident Deposits (FCNRB/NRERA etc)
		S0015	Repayment of loans & overdrafts taken by ADs on their own account.
		S0016	Sale of a foreign currency against another foreign currency
		S0017	Purchase of intangible assets like patents, copyrights, trade marks etc.
		S0018	Other capital payments not included elsewhere
01	Imports	S0101	Advance payment against imports
		S0102	Payment towards imports- settlement of invoice
		S0103	Imports by diplomatic missions
		S0104	Intermediary trade
		S0190	Imports below Rs. 500,000- (For Cover Page only)
02	Transportation	S0201	Payments for surplus freight/passenger fare by foreign shipping companies operating in India.
		S0202	Payment for operating expenses of Indian shipping companies

<b>Gr. No.</b>	<b>Purpose Group Name</b>	<b>Purpose Code</b>	<b>Description</b>
			operating abroad.
		S0203	Freight on imports – Shipping companies
		S0204	Freight on exports – Shipping companies
		S0205	Operational leasing (with crew) – Shipping companies
		S0206	Booking of passages abroad – Shipping companies
		S0207	Payments for surplus freight/passenger fare by foreign Airlines companies operating in India.
		S0208	Operating expenses of Indian Airlines companies operating abroad
		S0209	Freight on imports – Airlines companies
		S0210	Freight on exports – Airlines companies
		S0211	Operational leasing (with crew) – Airlines companies
		S0212	Booking of passages abroad – Airlines companies
		S0213	Payments on account of stevedoring, demurrage, port handling charges etc.
03	Travel	S0301	Remittance towards Business travel.
		S0302	Travel under basic travel quota (BTQ)
		S0303	Travel for pilgrimage
		S0304	Travel for medical treatment
		S0305	Travel for education (including fees, hostel expenses etc.)
		S0306	Other travel (international credit cards)
04	Communication Service	S0401	Postal services
		S0402	Courier services
		S0403	Telecommunication services
		S0404	Satellite services
05	Construction Service	S0501	Construction of projects abroad by Indian companies including import of goods at project site
		S0502	Payments for cost of construction etc. of projects executed by foreign companies in India.
06	Insurance Service	S0601	Payments for Life insurance premium
		S0602	Freight insurance – relating to import & export of goods
		S0603	Other general insurance premium
		S0604	Reinsurance premium
		S0605	Auxiliary services (commission on insurance)
		S0606	Settlement of claims
07	Financial Services	S0701	Financial intermediation except investment banking – Bank charges, collection charges, LC charges, cancellation of forward contracts, commission on financial leasing etc.

<b>Gr. No.</b>	<b>Purpose Group Name</b>	<b>Purpose Code</b>	<b>Description</b>
		S0702	Investment banking – brokerage, under writing commission etc.
		S0703	Auxiliary services – charges on operation & regulatory fees, custodial services, depository services etc.
08	Computer & Information Services	S0801	Hardware consultancy/implementation
		S0802	Hardware & Software implementation (other than those covered in SOFTEX form)
		S0803	Data base, data processing charges
		S0804	Repair and maintenance of computer and software
		S0805	News agency services
		S0806	Other information services- Subscription to newspapers, periodicals
09	Royalties & License Fees	S0901	Franchises services – patents, copyrights, trade marks, industrial processes, franchises etc.
		S0902	Payment for use, through licensing arrangements, of produced originals or prototypes (such as manuscripts and films)
10	Other Business Services	S1001	Merchanting services –net payments (from Sale & purchase of goods without crossing the border)
		S1002	Trade related services – commission on exports / imports
		S1003	Operational leasing services (other than financial leasing) without operating crew, including charter hire
		S1004	Legal services
		S1005	Accounting, auditing, book keeping and tax consulting services
		S1006	Business and management consultancy and public relations services
		S1007	Advertising, trade fair, market research and public opinion polling service
		S1008	Research & Development services
		S1009	Architectural, engineering and other technical services
		S1010	Agricultural, mining and on–site processing services – protection against insects & disease, increasing of harvest yields, forestry services, mining services like analysis of ores etc.
		S1011	Payments for maintenance of offices abroad
		S1012	Distribution Services
		S1013	Environmental Services
		S1019	Other services not included elsewhere
11	Personal, Cultural & Recreational services	S1101	Audio-visual and related services – services and associated fees related to production of motion pictures, rentals, fees

<b>Gr. No.</b>	<b>Purpose Group Name</b>	<b>Purpose Code</b>	<b>Description</b>
			received by actors, directors, producers and fees for distribution rights.
		S1102	Personal, cultural services such as those related to museums, libraries, archives and sporting activities; fees for correspondence courses abroad.
12	Govt. not included elsewhere (G.n.i.e.)	S1201	Maintenance of Indian embassies abroad
		S1202	Remittances by foreign embassies in India
13	Transfers	S1301	Remittance by non-residents towards family maintenance and savings
		S1302	Remittance towards personal gifts and donations
		S1303	Remittance towards donations to religious and charitable institutions abroad
		S1304	Remittance towards grants and donations to other governments and charitable institutions established by the governments.
		S1305	Contributions/donations by the Government to international institutions
		S1306	Remittance towards payment / refund of taxes.
14	Income	S1401	Compensation of employees
		S1402	Remittance towards interest on Non-Resident deposits (FCNRB/NRERA/ NRNRD /NRSR etc.)
		S1403	Remittance towards interest on loans from Non-Residents (ST/MT/LT loans)
		S1404	Remittance of interest on debt securities –debentures / bonds /FRNs etc.
		S1405	Remittance towards interest payment by ADs on their own account (to Vostro a/c holders or the OD on Nostro a/c.)
		S1406	Repatriation of profits
		S1407	Payment / repatriation of dividends
15	Others	S1501	Refunds / rebates / reduction in invoice value on account of exports
		S1502	Reversal of wrong entries, refunds of amount remitted for non-exports
		S1503	Payments by residents for international bidding
		S1504	Notional sales when export bills negotiated/ purchased/ discounted are dishonoured/ crystallized/ cancelled of bills and reversed from suspense account
		S1590	Outward remittances below Rs500,000- (for Cover page only)

**NEW PURPOSE CODES FOR REPORTING FOREX  
TRANSACTIONS  
B. RECEIPT PURPOSES**

<b>Gr. No.</b>	<b>Purpose Group Name</b>	<b>Purpose Code</b>	<b>Description</b>
00	Capital Account	P0001	Repatriation of Indian investment abroad in equity capital (shares)
		P0002	Repatriation of Indian investment abroad in debt securities.
		P0003	Repatriation of Indian investment abroad in branches & wholly owned subsidiaries
		P0004	Repatriation of Indian investment abroad in subsidiaries and associates
		P0005	Repatriation of Indian investment abroad in real estate
		P0006	Foreign direct investment in India in equity
		P0007	Foreign direct investment in India in debt securities
		P0008	Foreign direct investment in India in real estate
		P0009	Foreign portfolio investment in India in equity shares
		P0010	Foreign portfolio investment in India in debt securities including debt funds
		P0011	Repayment of loans extended to Non-Residents
		P0012	Long & medium term loans with original maturity above one year from Non-Residents to India
		P0013	Short term loans with original maturity upto one year from Non-Residents to India
		P0014	Receipts o/a Non-Resident deposits (FCNRB/NRERA etc.) ADs should report these even if funds are not “swapped” into Rupees.
		P0015	Loans & overdrafts taken by ADs on their own account. (Any amount of loan credited to the Nostro account which may not be swapped into Rupees should also be reported)
		P0016	Purchase of a foreign currency against another currency.
		P0017	Sale of intangible assets like patents, copyrights, trade marks etc. by Indian companies
		P0018	Other capital receipts not included elsewhere
01	Exports (of Goods)	P0101	Value of export bills negotiated / purchased/discounted etc. (covered under GR/PP/SOFTEX/EC copy of shipping bills etc.)
		P0102	Realisation of export bills (in respect of goods) sent on collection (full invoice value)
		P0103	Advance receipts against export contracts, which will be covered later by GR/PP/SOFTEX/SDF (export of goods)



Gr. No.	Purpose Group Name	Purpose Code	Description
			only)
		P0104	Receipts against export of goods not covered by the GR/PP/SOFTEX/EC copy of shipping bill etc.
		P0105	Export bills (in respect of goods) sent on collection.
		P0106	Conversion of overdue export bills from NPD to collection mode
		P0107	Realisation of NPD export bills (full value of bill to be reported)
02	Transportation	P0201	Receipts of surplus freight/passenger fare by Indian shipping companies operating abroad
		P0202	Purchases on account of operating expenses of Foreign shipping companies operating in India
		P0205	Purchases on account of operational leasing (with crew) – Shipping companies
		P0207	Receipts of surplus freight/passenger fare by Indian Airlines companies operating abroad.
		P0208	Receipt on account of operating expenses of Foreign Airlines companies operating in India
		P0211	Purchases on account of operational leasing (with crew) – Airlines companies
		P0213	Receipts on account of other transportation services (stevedoring, demurrage, port handling charges etc).
03	Travel	P0301	Purchases towards travel (Includes purchases of foreign TCs, currency notes etc over the counter, by hotels, hospitals, Emporiums, Educational institutions etc. as well as amount received by TT/SWIFT transfers or debit to Non-Resident account).
		P0308	FC surrendered by returning Indian tourists.
04	Communication Service	P0401	Postal services
		P0402	Courier services
		P0403	Telecommunication services
		P0404	Satellite services
05	Construction Service	P0501	Receipts for cost of construction of services projects in India
06	Insurance Service	P0601	Receipts of life insurance premium
		P0602	Receipts of freight insurance – relating to import & export of goods
		P0603	Receipts on account of other general insurance premium
		P0604	Receipts of Reinsurance premium
		P0605	Receipts on account of Auxiliary services (commission on insurance)
		P0606	Receipts on account of settlement of claims
07	Financial Services	P0701	Financial intermediation except investment banking – Bank charges, collection charges, LC charges, cancellation of

<b>Gr. No.</b>	<b>Purpose Group Name</b>	<b>Purpose Code</b>	<b>Description</b>
			forward contracts, commission on financial leasing etc.
		P0702	Investment banking – brokerage, under writing commission etc.
		P0703	Auxiliary services – charges on operation & regulatory fees, custodial services, depository services etc.
08	Computer & Information Services	P0801	Hardware consultancy/implementation
		P0802	Software consultancy/implementation (other than those covered in SOFTEX form)
		P0803	Data base, data processing charges
		P0804	Repair and maintenance of computer and software
		P0805	News agency services
		P0806	Other information services- Subscription to newspapers, periodicals, etc.
09	Royalties & License Fees	P0901	Franchises services – patents, copy rights, trade marks, industrial processes, franchises etc.
		P0902	Receipts for use, through licensing arrangements, of produced originals or prototypes (such as manuscripts and films)
10	Other Business Services	P1001	Merchanting Services – net receipt (from sale and purchase of goods without crossing the border).
		P1002	Trade related services – Commission on exports/imports.
		P1003	Operational leasing services (other than financial leasing and without operating crew) including charter hire
		P1004	Legal services
		P1005	Accounting, auditing, book keeping and tax consulting services
		P1006	Business and management consultancy and public relations services
		P1007	Advertising, trade fair, market research and public opinion polling services
		P1008	Research & Development services
		P1009	Architectural, engineering and other technical services
		P1010	Agricultural, mining and on –site processing services – protection against insects & disease, increasing of harvest yields, forestry services, mining services like analysis of ores etc.
		P1011	Inward remittance for maintenance of offices in India
		P1012	Distribution Services
		P1013	Environmental Services
		P1019	Other services not included elsewhere
11	Personal, Cultural & Recreational services	P1101	Audio-visual and related services – services and associated fees related to production of motion pictures, rentals, fees received by actors, directors, producers and fees for

Gr. No.	Purpose Group Name	Purpose Code	Description
			distribution rights.
		P1102	Personal, cultural services such as those related to museums, libraries, archives and sporting activities and fees for correspondence courses of Indian Universities/Institutes
12	Govt. not included elsewhere (G.n.i.e.)	P1201	Maintenance of foreign embassies in India
		P1203	Maintenance of international institutions such as offices of IMF mission, World Bank, UNICEF etc. in India.
13	Transfers	P1301	Inward remittance from Indian non-residents towards family maintenance and savings
		P1302	Personal gifts and donations
		P1303	Donations to religious and charitable institutions in India
		P1304	Grants and donations to governments and charitable institutions established by the governments
		P1306	Receipts / Refund of taxes
14	Income	P1401	<b>Compensation of employees</b>
		P1403	Inward remittance towards interest on loans extended to non-residents (ST/MT/LT loans)
		P1404	Inward remittance of interest on debt securities –debentures / bonds /FRNs etc.
		P1405	Inward remittance towards interest receipts of ADs on their own account (on investments.)
		P1406	Repatriation of profits to India
		P1407	Receipt of dividends by Indians
15	Others	P1501	Refunds / rebates on account of imports
		P1502	Reversal of wrong entries, refunds of amount remitted for non-imports
		P1503	Remittances (receipts) by residents under international bidding process.
		P1590	Receipts below \$10,000 (say Rs 5,00,000)

**NEW PURPOSE CODES FOR REPORTING FOR FOREX  
TRANSACTIONS**

**C. COVER PAGE PURPOSES**

Gr. No.	Purpose Group Name	Purpose Code	Description
99	Cover Page Total	P0091	Purchase from Reserve Bank of India (Currency-wise Totals)
		P0092	Purchase from other ADs in India (Currency-wise Totals)
		P0093	Purchase from Overseas banks & correspondents (Currency-wise Totals)
		P0094	debit from the Vostro a/c of overseas bank or correspondents (Country-wise Totals)
		P0095	Aggregate Purchases at Branches (Currency-wise Totals)
		P0100	Exports (Totals) {N/P/D + Collection bills Realised during Fortnight + Advance received during Fortnight} (Purchases from Public against exports (Currency-wise Totals))
		P0144	Purchases from Public against third country exports (Currency-wise Totals)
		P1590	receipts below \$ 10000 say (Rs. 500000) (Currency-wise Totals)
		P1591	Non-Exports equivalent & above US\$ 10,000 (say Rs. 5,00,000)
		S0091	Sales to Reserve Bank of India (Currency-wise Totals)
		S0092	Sales to other ADs in India (Currency-wise Totals)
		S0093	Sales to Overseas banks & correspondents (Currency-wise Totals)
		S0094	credit to the Vostro a/c of overseas bank or correspondents (Country-wise Totals)
		S0095	Aggregate Sales at Branches (Currency-wise Totals)
		S0144	Sales to Public against Imports into other countries (Currency-wise Totals)
		S0190	Imports below Rs. 500000 (Currency-wise Totals)
		S0191	Imports equivalent & above Rs. 5 Lakhs (Currency-wise Totals)
		S1590	Non-Imports Totals payment below Rs 500000 (Currency-wise Totals)
		S1591	Non-Imports equivalent & above Rs. 5 Lakhs (Currency-wise Totals)
	Cover Page Balance	P2088	Opening Balance (Debit Balance in Mirror/Debit Balance in Vostro)
		P2199	Closing Balance (Debit Balance in Mirror/Debit Balance in Vostro)
		S2088	Opening Balance (Credit Balance in Mirror/Credit Balance in Vostro)
		S2199	Closing Balance (Credit Balance in Mirror/Credit Balance in Vostro)