SUMMARY OF FINDINGS
AND CONCLUSIONS
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"It will not do merely to listen
to great principles
you must apply them
in the practical field,
turn them into constant Practice"

... VIVEKANANDA

6.1 INTRODUCTION

The foregoing chapters made an attempt to present the concept of balance of payments, the problem of terms of trade and trade balances, the growing current account deficits of different regions of developing countries, the fluctuating overall balances of those regions and the balance of payments situation of India since 1970. The present chapter is set out to place the summary of findings of the previous chapters and conclusions drawn thereon.

6.2 TERMS OF TRADE AND TRADE BALANCES

The emergence of the large trade deficits are causing concern regarding the prospects of developing countries balance of payments. The direction of developing countries trade statistics showed that the industrial countries account for
nearly Sixty per cent of developing countries trade. As against this trade among developing countries accounts for about thirty per cent even though the per cent distribution reveals that exports and imports among developing countries are increasing every year, still it lags behind compared to the trade with industrial countries. It is also evident that among developing countries Asia is the single largest region which accounts for nearly twenty per cent of trade.

Developing countries exhibited wide fluctuations in their export and import trade. Computed growth rates of exports of different regions among developing countries and developing countries as a group show that Asia recorded a high growth rate and Africa recorded a low growth rate. The t-values are significant at one per cent and five per cent levels revealing that the growth in exports of all regions is significant except in the case of Middle East where t-values are less than the table value. Though growth rate of Asia is high its C.V. is also high indicating less consistency and contrary is the case with Africa. Hence, the first hypothesis of the study is rejected as there is a significant difference in the growth rates of trade balances of different groups of developing countries over a period of two decades 1971-90. The wide variation in export and import growth of different regions explain partly their balance of payments difficulties.
The trade in export unit value indices indicate that because of higher degree of commodity concentration in their exports, these countries are very sensitive to fluctuations in prices than developed countries. Higher fluctuations in prices will have serious effects on an average developing economy.

Africa and Asia have been paying higher prices for imports as they have registered higher import unit values. Thus, the developing countries as a whole received 94.3 per cent of unit value for their imports in 1989 and have paid 105.1 per cent to their imports in the same year. Consequently they experienced set backs in their export earnings.

An examination of terms of trade of different regions reveal that on the whole developing countries are facing unfavourable terms of trade notwithstanding the favourable position of some regions as some other regions are faced with unfavourable terms of trade.

Multiple regression analysis is pressed into service to know the cause and effect relationship between the trade balances and terms of trade and foreign exchange reserves show that in the case of developing countries as a group trade
balances are affected 20 per cent by changes in terms of trade and foreign exchange reserves. This is in the order of 24, 29, 38, 67 and 78 in the case of Africa, Asia, Middle East, Western Hemisphere and Europe respectively. The relationship between trade balances and the two explanatory variables is high in Europe and Western Hemisphere. The t-values are significant in foreign exchange reserves in the case of Europe at 1 per cent and 5 per cent levels showing a significant relationship between trade balances and foreign exchange reserves. And in Western Hemisphere there is a significant relationship between trade balances and terms of trade as the calculated t-value is greater than the table value at both 1 and 5 per cent levels. Whereas in foreign exchange reserves it is significant only at 5 per cent level. For all other regions t-values are not significant at both the levels.

A further examination of trade problems and policies of developing countries reveals that one of the main economic problems which developing countries are facing is instability in their export earnings. Instability in exports might affect a country's development adversely as the domestic income, consumption, savings, investment, tax revenues, balance of payments and the capacity to import may decline.
"TRADE NOT AID" has become a popular aphorism in developing countries in recent years as they argue that international aid arrangements are unsatisfactory. Also, aid is used by the developed countries as a political weapon which goes to the developing countries who fall in line with the political ideologies and military strategies of the developed countries giving that aid.

Large part of export earnings of developing countries is used to debt service payments. Balance of payments constraint and shortage of foreign exchange resources can be an obstacle to the development of developing countries. Even though international liquidity and monetary arrangements discriminate against the developing countries the IMF is not putting pressures on the developed countries to adopt policies which will help them to get rid of their surpluses.

In view of these problems some programmes of action have been put forth either by developing countries or for them. They are, indexation, export-led growth, French Plan, buffer stock schemes, restrictions schemes, Price compensation agreements and Income Compensation Schemes. The motive behind all these programmes is to see that developing countries should get rid of their trade problems by stabilising prices,
maintaining the purchasing power of commodity prices that is preventing a deterioration in terms of trade of primary commodities, increasing efficiency in production, providing IMF's assistance and alike. Further to remove the existing imbalances between developed and developing countries and removing or lowering of tariff and trade barriers organisations such as GATT, UNCTAD and NIEO have been established.

6.3 TRENDS IN CURRENT ACCOUNT BALANCES

There were wide fluctuations in the current account balances of all the regions. Middle East influences the balances of developing countries significantly. While Middle East and Developing countries as a whole experienced surpluses and deficits in their current account balances the other regions have shown deficits in almost all the years with the exception of only a few years.

The linear growth rates for the current account balances reveal that the balances are declining heavily in Asia for which LGR is -16.58 followed by Europe (-11.87), Western Hemisphere (-7.41), Middle East (-7.03) and the group comprising all the developing countries (-4.40). In Africa the balances are increasing at the rate of 4.52. The t-values are
not significant for all the regions except Europe and Middle East. Hence the growth rates are significant in the case of Europe and Middle East.

The null hypothesis namely that there is no significant difference in the growth rates of current account balances of different groups of developing countries in the study period is accepted in the case of Africa, Asia, Europe and the group "DEVELOPING COUNTRIES" and is rejected in the case of Europe and Middle East where the calculated t-values are higher than the table value.

The current account transactions reveal that "SERVICES" are influencing the current account balances significantly. Despite trade surpluses in all the years during 1984-91 developing countries have experienced deficits in their current account. This is a result of huge deficits in "SERVICE" account which offset the trade surpluses substantially. A moderate increase in the ratios of reserves to imports of goods and services in the developing countries is observed. The dual gap analysis performs the valuable service of emphasising the role of imports and foreign exchange in the development process. The role of foreign borrowing was seen as a supplement to
deficient domestic saving. If foreign exchange is the dominant constraint it points to the additional role of foreign borrowing in supplementing foreign exchange which is said to be the distinctive contribution of dual gap analysis.

Pressure on the balance of payments may become acute when the foreign debt has to be serviced. The average developing countries debt service ratio reached 27 per cent. For individual countries it ranges from 4.0 per cent to 50 per cent.

\( R^2 \) values indicate the influence of terms of trade and trade balances on current account balances. Their influence is 97 per cent, 96.5 per cent, 96 per cent, 88.8 per cent, 72.9 per cent and 39 per cent for the regions Middle East, Europe, Asia, Developing Countries, Africa and Western Hemisphere respectively. The t-values of trade balances are significant for all the regions whereas t-values of terms of trade are significant at 1 and 5 per cent levels in developing countries as a group and Middle East. But in the case of Europe it is significant only at 5 per cent level and it is not significant at both the levels in the case of Africa, Asia and Western Hemisphere. Hence it can be inferred that the influence of trade balance is more on current account balances. And the influence
of terms of trade is different in different regions of developing countries. Debt service is not influencing the current account balances as the $R^2$ values are negligible for all the regions except Europe. The t-values are also not significant for all the regions except for Europe where it is significant at 5 per cent level only.

6.4 OVERALL BALANCE OF PAYMENTS

The capital account of developing countries exhibits surplus throughout the study period except in 1980, 1988 and 1989. The linear growth rates explain that Asia's capital account balances are increasing at the rate of 6.44. The balances of all other regions are declining. But t-values are not significant for Asia and developing countries both at 1 and 5 per cent levels while it is significant only at 5 per cent level. For all other regions the t-values are significant at both the levels.

The overall balance account shows surplus from 1974 to 1980 and deficit from 1981 to 1989 except in 1987. The LGR is 35.29 for Asia and the t-value is significant at both land 5 per cent levels. For all other regions the overall balances are declining in varying degrees. This decline is the highest in
the case of Western Hemisphere (-58.88) and lowest in the case of Europe (-0.478). The t-values for Africa and Western Hemisphere are significant at both 1 and 5 per cent levels. It is significant only at 5 per cent level in the case of developing countries as a whole while they are not significant in the case of Europe and Middle East at both the levels.

The international debt crisis of the 1980s has spurred enormous research activity in search of innovative schemes to tackle the debt problem. The two oil shocks in 1970s resulted in massive foreign indebtedness for many developing countries. Also, there was an increase in general price levels in the developed countries. The reaction to this rise by the governments of the industrialised countries lies close to the heart of the problem. Real rates of interest facing developing countries were on average negative in the 1970s. To add to the misery of developing countries, foreign capital flows also fell sharply by two thirds, that is, from 2.8 per cent of the GDP in 1979 to 0.9 per cent in 1985.

The inappropriate domestic economic policies of developing countries aggravated their difficulties which resulted in borrowed capital being used to increase domestic consumption
to unsustainable levels. Also these governments were at fault for allowing their exchange rates to become hugely overvalued.

It is observed from the trends in external debt of developing countries that the growth of external debt in these countries has been an aspect of their growing participation in the world economy.

During the first five years of the decade 1980s developing countries have experienced relative stagnation in economic growth, declining exports and increasing indebtedness. In this period the annual growth rate of the foreign debt of the developing countries has averaged 17 per cent, the domestic growth rate averaged only 3.2 per cent and exports declined by 1.7 per cent. During 1984-91 the external debt of developing countries has increased by 1.5 times or by $534.8 billion.

Reflecting the expansion of export volume the debt to export ratio for all developing countries continued to decline after 1987. Almost the similar trend is observed for other regions except for Europe. Asia's ratio of external debt to exports is quite low when compared with other regions which signifies their export performance. On the contrary Western Hemisphere is having high debt export ratios. The data on
total external debt relative to GDP reveals that at 23.9 per cent in 1990 it was lower than the 1986 level of 28.6 per cent, showing an improvement for the fourth consecutive year since 1986.

Hence in the period 1984-91 there is a significant change in debt overhang of developing countries.

Given current debt levels and balance of payments prospects, a number of countries are encountering debt servicing difficulties and will require a rescheduling of their obligations and more may join them. There are, broadly speaking, three ways to cope with the debt problem. The first is to modify economic policies so as to enhance the capacity to service debt. The second is to reduce the burden of debt servicing. And the third approach is some form of debt reduction.

A scrutiny of various plans of debt reduction has made it clear that there cannot be only one plan for the Third World Countries debt problem. All proposals have to work in cohesion to achieve the end of developing countries debt reduction.
Developing countries do hold reserves but their ability to finance balance of payments deficits may be more limited than that of developed countries. It is observed from the trends in various components of total reserves that developing countries improved their international reserves by virtue of their foreign exchange reserves rather than through SDRs and gold reserves. To put it in other words the share of foreign exchange reserves is high in the total reserves and they increased from SDR 18132 million in 1971 to SDR 215195 million in 1990 for developing countries. All other regions also recorded huge increases.

Hence, the second hypothesis of the study namely that there is no significant change in the foreign exchange reserves of different groups of developing countries is rejected.

From the results of ANOVA it is concluded that at five per cent level of significance the calculated F-value is greater than the table value. Hence rejecting the null hypothesis the alternative hypothesis namely that there is a significant difference in average volume of total reserves of different regions is accepted.

In view of the aforesaid discussion it can be inferred that the disequilibrium in the balance of payments of different
groups of developing countries is a transitory one.

6.5 INDIA's FISCAL AND BALANCE OF PAYMENTS DISEQUILIBRIUM

Over the years, the trade balance has been the dominant balance in India's external payments. The exports of India increased more than twenty one times during 1970-71 to 1990-91. However, the export growth was not uniform.

India's export structure presents a changing profile, indicative of the structural transformation that has been taking place in the economy. While the share of agro-based products has come down, the share of processed and manufactured goods increased substantially.

There were wide fluctuations in the rates of growth of imports. The linear and compound growth rates of India's exports and imports are significant at both 5 and 1 per cent levels. However, exports have shown moderately less consistency when compared to imports.
BY employing student t-test it is inferred that there is a significant difference in the average exports and average imports during the 20 years period.

Observing the composition of India's imports it can be said that the main impetus for the burgeoning growth of imports during the eighties came from the category of non-bulk items.

India's trade balances show that during the last two decades the deficits have increased by more than 107 times. This is obvious as the average growth in imports is more than the average growth in exports.

Broadly the trend in terms of trade of India is downwards in the seventies and upwards in the eighties. The export unit value index increased 2.3 times during seventies and 2.7 times in eighties whereas the import unit value index increased 3.2 times and 2.0 times respectively.
Multiple regression is run to find out the determinants of trade balance. \( R^2 \) value indicates that the influence of the three explanatory variables viz, terms of trade, GNP at current prices and foreign exchange reserves is as high as 83 per cent. However, the t-values are not significant at both 1 and 5 per cent levels in the case of terms of trade and foreign exchange reserves. While they are significant for GNP at both the levels.

The direction of India's trade shows that the industrial market economies have been gaining ground both as markets for India's exports as well as sources of India's imports. These countries account for more than 50 per cent of India's trade while India's trade with other developing countries account for around 30 per cent.

Since 1970s, with the exception of 1972-73 and 1976-77, India has been experiencing deficit in its balance of payments.
The large trade deficits, reductions in the surplus on invisibles account, the huge current account deficits, foreign exchange reserves have all done much to the increasing deficits in the overall balance of payments. Overall deficit has almost doubled during the period 1980-81 and 1989-90.

Multiple regression analysis showed that terms of trade and current account balances are influencing the overall balances by more than 86 per cent. But the t-value is significant for current account balances at both 1 and 5 per cent levels whereas in the case of terms of trade it is not significant at both the levels.

The linear growth rates for trade balances, current account balances and overall balances of India are 232.55, 102.69 and 30.04 respectively and the t-values show that these growth rates are significant at 1 and 5 per cent levels.

Total debt service obligation is also mounting. The debt service ratio went up from around 8 per cent in 1979-80 to 23.0
per cent in 1988-89. Empirical evidence states that there is a positive relationship between trade gap and the magnitude of external debt of India through regression analysis.

The influence of saving investment gap, total budget deficit and trade balances on current account balances is tested by constructing regression lines. The result shows that this influence is more than 99 per cent. The t-values are significant at both 1 and 5 per cent levels for saving-investment gap and trade balances and for total budget deficit it is not significant.

Regression is employed to test the influence of gross fiscal deficit, saving-investment gap and trade balances. Here also, the influence is more than 99 per cent. The t-values are significant at 5 per cent level only for gross fiscal deficit and trade balances. And it is significant at both the levels in the case of saving-investment gap.

Since fiscal deficits, saving investment gap and trade balances are influencing the current account balances by more
than 99 per cent the fourth hypothesis of the study namely that there is no inter connection between fiscal and balance of payments disequilibrium in the Indian economy is rejected and accepting the alternative hypothesis it can be concluded that there is inter connection between fiscal deficit and balance of payments disequilibrium in the Indian economy.

India's foreign exchange reserves are fluctuating frequently. The coefficient of variation shows that gold reserves are stable when compared to SDRs and foreign exchange reserves. The linear growth rates for these three components are 3.31, -4.59 and 91.56 respectively while compound growth rates are 2.73, -4.68 and 17.27 respectively. The t-values are significant at 1 and 5 per cent levels for gold reserves and foreign exchange reserves not significant at both the levels for SDRs.

6.6 CONCLUSIONS

The time has now come to wind up the discussion about balance of payments problems. As discussed earlier, the trade
gap has to be bridged with a more serious effort to push up exports and to regulate imports through a well thought out process of elimination of redundant or substitutable items. In an expanding phase of the economy, it is idle to expect that a net reduction in imports can take place. Devaluation is one of the remedies for balance of trade ailments. It is primarily an expenditure-switching policy and works through the price effect of the traded goods. However, though devaluation is expected to augment export earnings it cannot be expected to contain the trade gap if the import intensity in the domestic production is not checked and import liberalisation policy continues.

Continuing current account deficits have necessarily resulted in increasing the outstanding debt.

Though the developing countries are doing a good job of managing their payments problems, the external debt problem is becoming an obstacle in its way.
The only way out seems to be is that the developed countries should transfer larger resources in non-debt form and at non-commercial interest rates.

A strategy for ensuring a viable balance of payments requires correction of the present fiscal imbalance. A reduction in the current account deficit means a reduction in the overall savings - investment gap of the economy. Since in the present Indian situation, the widening of the savings - investment gap is largely due to deterioration in budgetary savings, an improvement in the current account of balance of payments will require a substantial reduction in the budget deficit. The measures like acquiring foreign aid or disposing of foreign exchange reserves can be only a stop gap arrangement. Infact, these measures may only aggravate the problem later. One potential area to acquire foreign exchange reserves more is tourism. This is particularly true in the case of India. Foreign investment is to be encouraged more and more without, however, jeopardising our national priorities.

Terms of trade must be in favour of developing countries. Developed countries have to change their policies with a view to helping the developing countries to come out of
balance of payments problems. Developing countries should come together and negotiate in the international forums like GATT and UNCTAD that the terms of trade must be favourable to them. Developed countries should eliminate the tariff and non-tariff barriers on Third World trade.

To conclude, four broad areas for policy on developing countries balance of payments are identified. First, a policy to reduce the import intensity, increasing the export intensity at the same time. Infact, the present Indian Government has implemented policies in this direction which are yielding fruitful results. But, it is too early to pass on any judgement on these policies as their effect on balance of payments is to be seen in the long run. Secondly a policy that ensures the reduction in current account deficit significantly. Attention is to be paid on net invisibles in order to achieve this end. Thirdly, domestic economies are to be strengthened and reliance on external debt must come down. And finally, a policy to combine expenditure reducing and switching policies. In other words a strict vigil on monetary and fiscal discipline is to be kept. If, policies are geared in these directions they will help to increase the foreign exchange reserves and the balance of payments problems may certainly be reduced.