BANKING AND INSURANCE

Coverage

18.1 The two main activities covered under this sector are banking and insurance which comprises of:

- commercial banks;
- banking department of Reserve Bank of India (RBI);
- public non-banking financial corporations;
- organised non-banking financial companies engaged in trading in shares, investment holdings, mutual funds, loan finance and the like activities;
- unorganised non-banking financial institutions/undertakings such as professional money lenders and pawn brokers;
- post office savings banks including operations concerning cumulative time deposits and national saving certificates;
- co-operative credit societies; and
- life and non-life insurance activities.

18.2 Under the NIC 1998, this sector consists of codes 651-Monetary Intermediation, 659-Other financial intermediation, 660-Insurance and pension funding, except compulsory social security, 671- Activities auxiliary to financial intermediation, except insurance and pension funding, and 672-Activities auxiliary to insurance and pension funding.

Methods of Estimation of GVA and Sources of Data

Estimates at Current Prices

18.3 Annual Reports/Accounts of the public sector banks, companies and corporations like Life Insurance Corporation (LIC), State Financial Corporations etc. are major sources of data. The budget documents of Department of Posts provide the necessary data in the case of post office savings and postal life insurance. (Appendix 18.1)

18.4 **Banks:** The gross output of banks and similar financial institutions is estimated in two components viz., actual service charges and the imputed service charges. The concept of imputed service charge and its methodology of estimation are discussed in the subsequent paragraphs. The GDP from this sector is estimated by income method using readily available source material for each of the sub-sectors.

18.5 Financial intermediaries incur liabilities on their own account on financial markets by borrowing funds which they lend on different terms and conditions to other institutional units. Thus, they intermediate between lenders and borrowers by channeling funds from one to other, putting them at risk in the process.

18.6 Some financial intermediaries raise most of their funds by taking deposits; others do so by issuing bills, bonds or other securities. They lend funds by making loans or advances, or by purchasing bills, bonds or other securities. The pattern of their financial assets is different from that of their liabilities and in this way transform the funds they receive in ways more suited to the requirements of borrowers. Financial intermediaries also provide auxiliary financial services like currency exchange, advice about investments, purchase of real estate or taxation. The output of such services is valued on the basis of the fees or commissions charged, in the same way as other services. However, many financial intermediaries do not charge explicitly for the intermediation services which they provide to their customers so that there may be no receipts from sales (for example issue of cheque books) which can be used to value these services. Therefore, it becomes difficult to value the output of financial intermediation for which no explicit charges are made and for which there are no sales receipts. Such output is valued indirectly through financial intermediation services indirectly measured (FISIM). The financial intermediaries are able to provide services for which they do not charge explicitly by paying or charging different rates of interest to borrowers and lenders. They pay lower rates of interest to those from whom they borrow and charge higher rates of interest from those whom they lend. The resulting net receipts of interest are used to defray their expenses and provide an operating surplus. This scheme of interest rates avoids the need to charge their customers individually for services provided. The total value of FISIM is measured in the System of National Accounts as the total property income receivable by financial intermediaries minus their total interest payable, excluding the value of any property income receivable from the investment of their own funds; as such income does not arise from financial intermediation.

18.7 In other words, the banking enterprises render services to their customers in the form of maintaining their accounts and advising them on financial matters. In return for these services, customers are charged a nominal amount which is substantially smaller than the expenses of the enterprises. On the other hand, the banks provide loans and advances and the returns on such transactions are much higher than the payments made to depositors. This net return accruing to banks is large enough to meet their expenses and to earn a profit. If the financial enterprises are treated like any other productive enterprise, their income in the production account would only be limited to the charges made on customers which would mean that the banks would have a negative operating surplus and most likely negative value added. To circumvent this difficulty, an imputed income equivalent to interest and dividend receipts of banking and financial enterprises net of interest paid to depositors is defined income earned in return for services rendered and is entered as a receipt item in the production account.

18.8 A similar argument can be extended in the case of insurance enterprises where the premium for insurance constitutes the main source of income and they receive income from investment as well. In the case of general insurance, imputed service charges are measured as the receipts on account of premia plus interest and dividends earned less expenditure on account of claims paid.

18.9 Whenever the production of output is recorded in the system the use of that output must be explicitly accounted for elsewhere in the System of National Accounts. Hence FISIM must be recorded as being disposed of in one or more of the following ways– as intermediate consumption by enterprises, as final consumption by households & government, or as exports to non-residents. In principle, the total output should, therefore, be allocated among the various recipients or users of the services for which no explicit charges are made.

18.10 The imputed service charges which form a component of financial sector output are partly treated as intermediate consumption of industries and partly as the final consumption of government and the households. For determining these proportions the basic data on loans and deposits/sum assured relating to enterprises and consumers are used. These are taken from the same source material from which value added is estimated. The proportions of imputed service charges so worked out for the each of the industries, such as agriculture, forestry, manufacturing, services, etc., are treated as separate input items in the respective industries. In the case of households and government such charges are considered as an item of private and government consumption expenditure.

18.11 Data on income, expenditure and appropriation of commercial banks are available annually from the 'Statistical Tables relating to Banks in India' published by the RBI.

18.12 **Banking department of RBI:** The functions of the Issue Department of RBI are like that of a government department and for this reason it is treated as an administrative department of the Central Government. The rest of the activities of the RBI are considered under the Banking Department. The Annual Report of the RBI presents the balance-sheet of the Issue and Banking Departments separately. However, the profit and loss account of the two departments is presented in a combined form. Details regarding individual items of income and expenditure in respect of the two departments separately are collected directly from the RBI annually for the purpose of estimation of GDP.

18.13 **Non-banking financial enterprises**: There are about eighty public sector financial corporations and companies of Central and State Governments. The estimates of these enterprises are prepared from the details available in the annual reports which are analysed annually.

18.14 Non-Government Non-Banking Financial companies (NGNBFCs): The Reserve Bank of India (RBI) annually publishes a study on the *'Performance of Non-Government Financial and Investment Companies'* in its Bulletin. The study is based on the Annual Accounts of around eight hundred to one thousand companies. This number varies from year to year. The tables presented in the study include 'Combined Income, Expenditure and Appropriation Accounts' for the selected financial and investment companies. The same is being utilised to obtain the estimates of GVA at current prices of the non-banking financial companies.

18.15 The methodology followed for current price estimates of GVA and FISIM of this sub-sector is to estimate the GVA of the sample companies, by analysing the data on income, expenditure and profits provided in the RBI sample study. The ratio of the paid up capital of the population to the paid up capital of the sample forms the blowing up factor.

18.16 The RBI publishes the sample study on the non-government Financial and Investment Companies in the Bulletin every year. Each study presents the data for three consecutive financial years for a common set of companies.

18.17 Thus, for a particular year, three different estimates of GVA are derived based on the successive sample studies. It becomes very difficult at the time of revision of estimates to decide which study should be considered as representative. Whenever the results of a study are published, the temptation is to examine the estimates from the most recent study to revise the estimates. However, it has been observed that at times the results of the study for a financial year vary considerably and introduces volatility in the estimates of GVA and other aggregates. Further the growth rate based on PUC is always positive, while the sector itself may actually have a negative growth. Such situations give scope for arbitrariness in using a particular set of estimates.

18.18 In order to avoid the uncertainty, which stems from different estimates thrown by different sets of samples for the same year, the current price estimates of GVA of NGNBFCs are prepared by using the RBI study results of a particular year appearing in all the available studies in the current series of national accounts. This would mean the pooling of the sample companies to get a more stable estimate.

18.19 GVA from mutual funds (MFs): The Unit Trust of India is considered as a financial intermediary. In the 1993-94 series, the imputed value of services in respect of UTI was estimated in the same manner as that of banks and other financial intermediaries. The income side represents the income from assets, namely, equity as well as debt instruments. This income includes income from dividend, interest and profit on sale/redemption of investment. Since, MFs do not work on deposits of other sectors, the interest payments are either nil or negligible. The MFs work on the funds raised by collective investments made by its unit holders. Hence, the major returns to unit holders/shareholders are dividends, unlike the interest payments in the case of banks. The subtraction of only interest paid in the 1993-94 series (being insignificant in MFs) had resulted in an output of the MFs, which was not an appropriate measure of its implicit output, as the entire property income becomes the implicit output. In the new series the imputed value of services of UTI has been calculated as total income on account of dividend, interest, profit on sale/redemption of investment minus interest, dividend paid to the unit holders and undistributed profit.

18.20 **Unorganised non-banking financial institutions:** No direct data are available for measuring the volume of activity of unorganised non-banking financial undertakings and own-account money lenders. Efforts made to collect data on income and expenditure of the members of various stock exchanges in the country through mail enquiry resulted in very poor response. On the basis of discussions with the officials of the Delhi stock exchange and other knowledgeable authorities one-third of the gross/net value added in the organised activities have been assumed to be the corresponding estimates of the activities of the unorganised non-banking financial enterprises. The NSSO has taken up these activities along with other service activities in the 63rd survey (2006-07), the results of which are expected to provide information on unorganized financial services in the country.

18.21 **Post office savings bank**: Banking activities of the Department of Posts cover post office savings bank, cumulative time deposit account, national savings certificates, and other schemes. For these services, GVA is estimated as a proportion of management expenses, data on which are available from the budget documents. GVA, in this case, comprises compensation of employees and rent only. The proportion of GVA to management expenses is assumed to be the same as observed in respect of commercial banks.

18.22 **Co-operative credit societies**: The details of the factor incomes of co-operative credit societies are obtained directly from "*Statistical Statements Relating to Co-operative Movement in India, Vol. I Credit societies published by NABARD*". However, estimates of profits given in these publications are net of income tax whereas in the measurement of domestic product profits need to be gross of such taxes. To obtain these estimates, direct data are obtained on details of income and expenditure of a sample of co-operative credit societies.

18.23 **Insurance**: There are two types of insurance; life and non-life insurance. Life insurance is an activity whereby a policyholder makes regular payments to an insurer in return for which the insurer guarantees to provide the policyholder with an agreed sum, or an annuity, at a given date or earlier if the policyholder dies beforehand. Non-life insurance covers all other risks; accidents, sickness, fire etc. A policy that provides a benefit in the case of death within a given period but in no other circumstances, usually called term insurance, is regarded as non-life insurance because as with other non-life insurance, a claim is payable only if a specified contingency occurs and not otherwise.

18.24 The output of insurance represents the value of the service provided by insurance corporations in arranging payments of claims and benefits in exchange for the receipts of premiums and contributions. Premiums are usually paid regularly, often at the start of an insurance period, whereas claims fall due later. In the mean time between the payment of premiums being made and the claim being receivable, the sum involved is at the disposal of the insurance corporation to invest and earn income from it. The income thus earned allows the insurance corporations to charge lower premiums than would be the case otherwise. This income comes from the investment of the technical reserves of the insurance corporations, which are assets of the policyholders, and does not include any income from the investment of the insurance corporations' own funds. The technical reserves of an insurance corporation consist of pre-paid premiums, reserves against outstanding claims, actuarial reserves for life insurance and reserves for with-profit insurance. The output of the insurance activity, which represents the service provided to policyholders, is calculated separately for life and non-life insurance as:

- *Total actual premiums or contributions earned;*
- *Plus total premium or contribution supplements;*
- *Less claims or benefits due;*
- *Less increases (plus decreases) in actuarial reserves and reserves for with-profit insurance.*

18.25 Life insurance: The annual Report and Accounts published by the LIC give necessary details for preparation of the estimates of GVA. However, as regards profits, the LIC declares every two years, surplus derived as the balance after deducting net liabilities under Assurances and Life Annuity Contracts from Life Fund. In respect of private life insurance companies, data is available in their annual accounts and these are collected and analysed in the CSO.

18.26 The GVA by the life insurance business conducted by the Department of Posts is estimated by analysing the 'Appropriation Accounts' brought out by the same department. Profits and dividends are assumed to be nil.

18.27 General insurance: Gross factor incomes are obtained by analysing the accounts given in the annual reports of the General Insurance Corporation and its subsidiaries viz., Oriental Insurance Company, United India Insurance Company, National Insurance Company and The New India Assurance Company. Similarly, the GVA in respect of private non-life insurance companies, is compiled from the details available in their annual accounts, which are collected and analysed in the CSO.

18.28 Employees State Insurance Corporation: It is treated as a casualty insurance enterprise and included under general insurance sector. The estimates are prepared using data from its annual reports.

18.29 **Estimates at Constant Prices**

The estimates of GVA at constant prices are prepared separately for each of the sub-sectors. In general, the base year estimates are carried forward using indicators measuring the volume of activity in the corresponding sub-sector. A suitable indicator is prepared in each case to measure the volume of activity. In cases where the volume of activity is measured in value terms i.e., at current prices, these are deflated by the wholesale price index of all commodities to obtain the corresponding quantum index. However, in the case of commercial banks, the estimates of GVA at current prices are deflated by the implicit GDP price deflator, in respect of commodity producing sectors. For the Banking Department of RBI, the deflator used is the implicit price deflator of commercial banks. Indicators used in the preparation of constant price estimates are presented at Appendix 18.2

Quality and limitations of data base

18.30 The overall position regarding the availability of data for this sector is satisfactory except in the case of unorganised non-banking financial enterprises and own-account money lenders. However, for some of the sub-sectors sufficient details are not available on the distribution of management expenses to enable direct measurement of the factor incomes. This is particularly true for private non-banking financial companies, co-operative societies and post office savings banks.

Appendix 18.1

SOURCE MATERIAL USED

Item	Sources of data
1. Commercial banks	Annual Reports/Account.
2. Banking department of RBI	RBI Annual Report.
3. Public sector financial corporations	Annual Reports.
4. Private non-banking financial companies	RBI bulletins.
5. Post office savings banks	Budget documents of Department of Post
6. Co-operative credit societies	Statistical statements relating to co-operative movement in India, Vol. I Credit societies (NABARD) and data on income and expenditure of sample co-operative societies obtained directly.
7. Life Insurance	i) Annual Reports and Accounts (LIC); ii) Annual Reports and Accounts of private life insurance companies; iii) Valuation Reports; and iv) Appropriation Accounts: Postal Services.
8. General Insurance	Annual Reports and Accounts.
9. Employees State Insurance Corporation	Annual Reports.

Appendix 18.2

INDICATORS USED IN THE PREPARATIONOF CONSTANT PRICE ESTIMATES

Item	Indicators
1. Commercial banks,	Estimates of GVA at current prices are deflated by implicit GDP price deflator of commodity producing sectors.
2. Banking Department of RBI,	Estimates of GVA at current prices are deflated by implicit GDP price deflator of commercial banks.
3. Post Office Savings bank	CPI index.
4. Non- banking financial companies and corporations	Total net receipts deflated by WPI.
5. Co-operative credit societies	Average of indices of deposits (deflated) and membership.
6. Life insurance corporation	Average of deflated indices of change in life fund and sum assured.
7. Postal life insurance	Average deflated indices of life fund and sum assured.
8. Non-life insurance	Deflated index of premium net of claims and surrenders.

Appendix 18.3

ESTIMATES OF GDP - BANKING AND INSURANCE, 1999-2000

(Rs. crore)

S. No.	Sector/Sub Sectors	1999-2000
1	**Gross Domestic Product**	**1,05,662**
1.1	**Banking**	**94,114**
1.1.1	Banks	40,485
1.1.2	Banking Deptt. of RBI	10,875
1.1.3	Post office saving banks	745
1.1.4	Non-banking financial cos. & Corpn. incl. UTI	34,088
1.1.5	Co-op. credit societies	7,733
1.1.6	E.P.F.O.	188
1.2	**Insurance**	**11,548**
1.2.1	Life insurance	5,930
1.2.2	Postal life insurance	75
1.2.3	Non-life insurance	5,543

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