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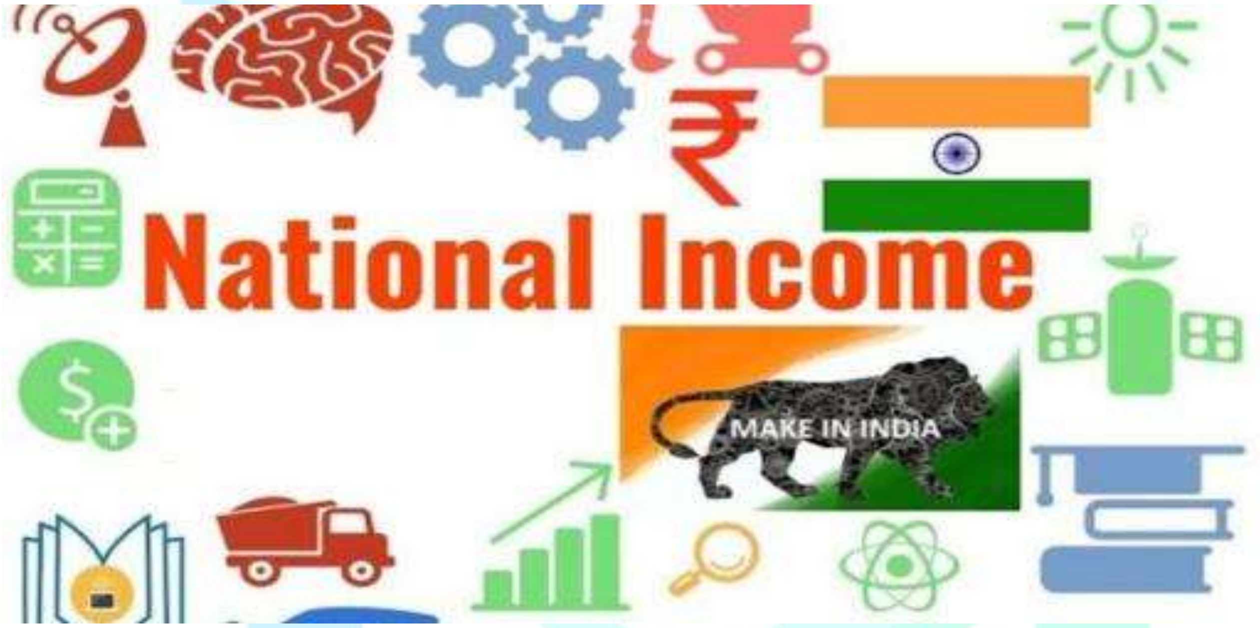
INDIAN ECONOMY

PART - I

CH:1 NATIONAL INCOME OF INDIA

HISTORY OF NATIONAL INCOME



The National income committee defines national income as "the value of commodities and services produced in an economy during a given period, counted without duplication." Estimates of National Income:

PRE-INDEPENDENCE ESTIMATES OF NATIONAL INCOME:

- Since there was no official body in India to prepare National Income estimates before Indian Independence, the same was prepared by some eminent personalities in their personal capacity.
- Dadabhai Naoroji, fondly called the Grand Old Man of India, was the pioneer in this field.
- He prepared the first estimates of National income in 1876.
- He estimated the national income by first estimating the value of agricultural production and then adding a certain percentage as non-agricultural production.
- However, such method can only been called as a non-scientific method.
- The first person to adopt a scientific procedure in estimating the national income was Dr. VKRV Rao in 1931.

HE DIVIDED THE INDIAN ECONOMY INTO TWO PARTS:

i. Agricultural Sector which included agriculture, forests, fishing and hunting.
ii. Corporate Sector which included industries, construction, business, transport and public services.

METHODS USED FOR ESTIMATING THE INCOME:

i. Product method was used for estimating income in agricultural sector
ii. income method was used for estimating income in the corporate sector.

iii. Finally, Net Factor Income earned from abroad was added to the sum of the above two to obtain national income.

ESTIMATES OF NATIONAL INCOME AFTER INDEPENDENCE

- The Government of India appointed National Income Committee in 1949. The committee was chaired by Prof. P.C. Mahalanobis and had Prof D.R. Gadgil and Dr. V.K.R.V. Rao as members .
- The first report of the committee was presented in 1951. According to the first report, the National Income of India for 1948-49 was Rs. 8,710 crore and the per capita income was Rs. 225.
- Since 1955 the national income estimates are being prepared by Central Statistical Organisation.
- The Central Statistical Organisation has divided Indian economy into three basic sector for the purpose of evaluation of various data.

THEY ARE:

→ Primary sector comprising agriculture, forestry, fishing, mining and quarrying.
→ Secondary sector comprising manufacturing, power generation, gas and water supply and
→ Tertiary sector comprising transport, communication and trade, banking insurance, computer software, public administration, defence and external trade.

- The CSO uses different methods like the Product Method, Income Method and Expenditure method for various sectors in the process of estimating the National Income.
- National Income may be calculated on current prices or at constant prices. Currently, the base year for measuring national income and per capita income at constant prices is 2004 - 05, introduced in Jan 2010.

NATIONAL INCOME DOES NOT INCLUDE DATA FROM THE FOLLOWING ACTIVITIES:

- Income from illegal activities like smuggling, gambling etc.
- Income from work done without remuneration like domestic work by housewives.
- Black Money

CONCEPTS OF NATIONAL INCOME

There are various concepts of National Income, such as GDP, GNP, NNP, NI, PI, DI, and PCI which explain the facts of economic activities.

1. **GDP at market price:** Is money value of all goods and services produced within the domestic domain with the available resources during a year.

GDP = (P*Q)

Where,

GDP = gross domestic product

P = Price of goods and services

Q= Quantity of goods and services

GDP is made up of 4 Components

- consumption
- investment
- government expenditure
- net foreign exports of a country

GDP = C+I+G+(X-M)
Where,
C=Consumption
I=Investment
G=Government expenditure
(X-M) =Export minus import

1. **Gross National Product (GNP):** Is market value of final goods and services produced in a year by the residents of the country within the domestic territory as well as abroad. GNP is the value of goods and services that the country's citizens produce regardless of their location.

GNP=GDP+NFIA or,

GNP=C+I+G+(X-M) +NFIA

Where,
C=Consumption
I=Investment
G=Government expenditure
(X-M) =Export minus import

NFIA= Net factor income from abroad.

1. **Net National Product (NNP) at MP:** Is market value of net output of final goods and services produced by an economy during a year and net factor income from abroad.
   NNP=GNP-Depreciation
   or, NNP=C+I+G+(X-M) +NFIA- IT-Depreciation

Where,
C=Consumption
I=Investment
G=Government expenditure
(X-M) =Export minus import

NFIA= Net factor income from abroad.

IT= Indirect Taxes

1. **National Income (NI):** Is also known as National Income at factor cost which means total income earned by resources for their contribution of land, labour, capital and organisational ability. Hence, the sum of the income received by factors of production in the form of rent, wages, interest and profit is called National Income.

Symbolically,

NI=NNP +Subsidies-Interest Taxes
or, GNP-Depreciation +Subsidies-Indirect Taxes
or, NI=C+G+I+(X-M) +NFIA-Depreciation-Indirect Taxes +Subsidies

1. **Personal Income (PI):** Is the total money income received by individuals and households of a country from all possible sources before direct taxes. Therefore, personal income can be expressed as follows:
   PI=NI-Corporate Income Taxes-Undistributed Corporate Profits- Social Security Contribution +Transfer Payments.
2. **Disposable Income (DI) :** It is the income left with the individuals after the payment of direct taxes from personal income. It is the actual income left for disposal or that can be spent for consumption by individuals.

Thus, it can be expressed as:

DI=PI-Direct Taxes

1. **Per Capita Income (PCI): Is c**alculated by dividing the national income of the country by the total population of a country.

Thus, **PCI=Total National Income/Total National Population**

MEASUREMENT OF NATIONAL INCOME

There are three methods to calculate National Income:

1. Income Method
2. Product/ Value Added Method
3. Expenditure Method

- **INCOME METHOD**

In this National Income is measured as flow of income.

We can calculate NI as:

NET NATIONAL INCOME = Compensation of Employees + Operating surplus mixed (w +R +P +I) + Net income + Net factor income from abroad.

Where,

W = Wages and salaries

R = Rental Income

P = Profit

I = Mixed Income

- **Product/ Value Added Method**

→ In this National Income is measured as flow of goods and services.
→ We can calculate NI as:
→ NATIONAL INCOME = G.N.P – COST OF CAPITAL – DEPRECIATION – INDIRECT TAXES

- **Expenditure Method**

- In this National Income is measured as flow of expenditure.
- We can calculate NI through Expenditure method as:
- National Income=National Product=National Expenditure.

Comparing Nominal GDP & Real GDP

Basis For Comparison	Nominal GDP	Real GDP
Meaning	Nominal GDP is Sum-total of economic output produced in a year valued at current market price	Real GDP is Sum-total of economic output produced in a year valued at a pre-determined base market price
Effect of Inflation	Nominal GDP doesn't take inflation into account	Real GDP is a Inflation-Adjusted GDP
Expressed in	Current Market Price	Base Year's Market Price
Value of GDP	Is much higher since current market changes are taken into effect	Is much lower since market price of the base year is taken into consideration
Uses	Can be compared with various quarters of the given year	Can be compared with two or more financial years
Economic Growth	From Nominal GDP, economic growth can't be analysed easily	Real GDP is a Good Indicator of economic growth

Courtesy: Investyadna.com

NET DOMESTIC PRODUCT (NDP):

NDP is the value of net output of the economy during the year. Some of the country's capital equipment wears out or becomes obsolete each year during the production process. The value of this capital consumption is some percentage of gross investment which is deducted from GDP. Thus Net Domestic Product = GDP at Factor Cost – Depreciation.

Now the general price level of the year for which real GDP is to be calculated is related to the base year on the basis of the following formula which is called the deflator index:

Suppose 1990-91 is the base year and GDP for 1999-2000 is Rs. 6, 00,000 crores and the price index for this year is 300.

Thus, Real GDP for 1999-2000 = Rs. 6, 00,000 x 100/300 = Rs. 2, 00,000 crores

GDP Deflator:

GDP deflator is an index of price changes of goods and services included in GDP. It is a price index which is calculated by dividing the nominal GDP in a given year by the real GDP for the same year and multiplying it by 100.

Thus,

It shows that at constant prices (1993-94), GDP in 1997-98 increased by 135.9% due to inflation (or rise in prices) from Rs. 1049.2 thousand crores in 1993-94 to Rs. 1426.7 thousand crores in 1997-98.

GROSS NATIONAL PRODUCT (GNP):

GNP is the total measure of the flow of goods and services at market value resulting from current production during a year in a country, including net income from abroad.

GNP INCLUDES FOUR TYPES OF FINAL GOODS AND SERVICES:

(1) Consumers' goods and services to satisfy the immediate wants of the people;

(2) Gross private domestic investment in capital goods consisting of fixed capital formation, residential construction and inventories of finished and unfinished goods;

(3) Goods and services produced by the government; and

(4) Net exports of goods and services, i.e., the difference between value of exports and imports of goods and services, known as net income from abroad.

In this concept of GNP, there are certain factors that have to be taken into consideration:

- **First,** GNP is the measure of money, in which all kinds of goods and services produced in a country during one year are measured in terms of money at current prices and then added together.
- But in this manner, due to an increase or decrease in the prices, the GNP shows a rise or decline, which may not be real. To guard against erring on this account, a particular year (say for instance 1990-91) when prices be normal, is taken as the base year and the GNP is adjusted in accordance with the index number for that year. This will be known as GNP at 1990-91 prices or at constant prices.
- **Second,** in estimating GNP of the economy, the market price of only the final products should be taken into account. Many of the products pass through a number of stages before they are ultimately purchased by consumers.
- If those products were counted at every stage, they would be included many a time in the national product.
- Consequently, the GNP would increase too much. To avoid double counting, therefore, only the final products and not the intermediary goods should be taken into account.
- Third, goods and services rendered free of charge are not included in the GNP, because it is not possible to have a correct estimate of their market price.
- For example, the bringing up of a child by the mother, imparting instructions to his son by a teacher, recitals to his friends by a musician, etc.