circular flow of Income

12/03/19

Economics

Q. What do you mean by macroeconomics ?

Ans The term macro is derived from macro which means large. It is basically a study of aggregates or average of the entire economy eg. National income, National output, aggregate demand, aggregate supply etc.

Q. What do you mean by stock and flow ?

Ans Stock variable is that variable which is measured at a particular point of time eg. Stock of goods in the godown on a particular day, National wealth, National capital etc.

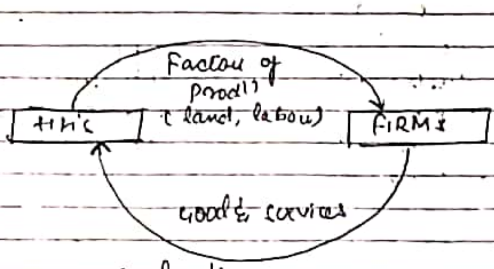
Flow variable refers to that variable which is measured during a period of time eg. production of goods during the month of January or during the year of 2018 etc.

Basis	stock	flow
Mean	It refers to that variable which is measured at a particular point of time	It refer to that variable which is measured over a period of time.
time dimension	It does not have any time dimension	It has a time dimension since it can be measured only during a period of time.

Nature	It is static in nature	It is dynamic in nature
Example	National wealth, Money supply, population of India ...	National income, expenditure on money, No. of births during 2018

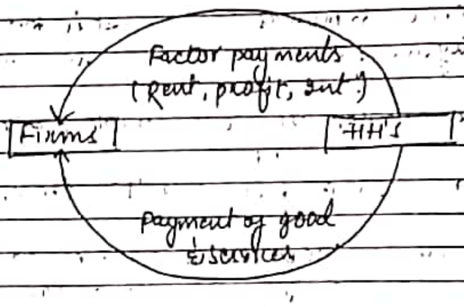
Q. what do you mean by circular flow of income?
→ It refers to a cycle of generation of income, distribution among factor of prodⁿ and finally its circulation from household to firms in the form of consumption expenditure on goods and services produced by them.

Q. what is real flow?
→ Real flow refers to the flow of factor services from household to firms and the corresponding flow of goods & service from firms to HH. It is also known as physical flow.



Real flow

Q. What do you mean by money flow?
→ It refers to the flow of factor payments from firms to household for their factor services & services and corresponding flow of consumption expenditure from HH to firms from purchase of goods & services produced by the firms as shown the diagram.



money flow

as we can see in the diagram households give price for goods & services to the firms and firms pay price for factor services like rent, int, profit, wages etc. This flow is also known as nominal flow.

Q. Difference between Real & money flow?

Basis	Real flow	Money flow
Meaning	Real flow is a flow of goods & services & factor services.	Money flow is the flow of money in form of factor payments & price of goods.

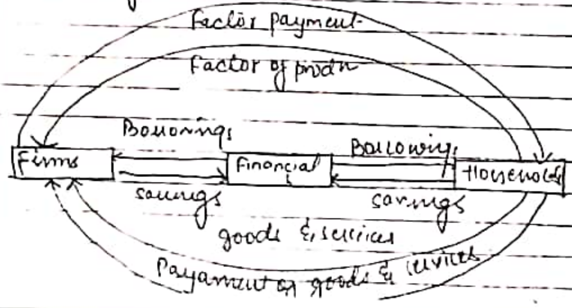
Exchange	It involves Exchange of goods & services.	It involves Exchange of money.
Difficulty in Exchange	There can be difficulty of Barter system in Exchange of goods & services.	There are no such difficulties in money flow.
Alternative name	It is also known as physical flow	It is known as nominal flow.

Q. Explain circular flow in a simple economy?

OR

Explain circular flow in a two sector economy?

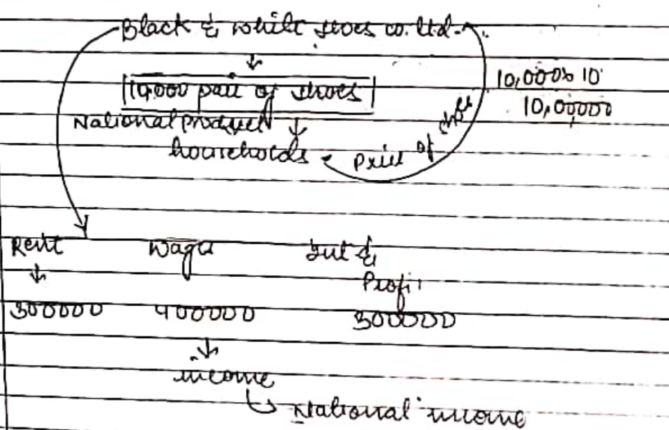
Ans. A simple economy assumes the existance of only two sectors that is household sector & firm sector where households are the owner of factor services & consumer of goods & services where as firms are the producers of goods & services. It is the simplest form of closed economy where there is no govt. or foreign sector. The circular flow is shown in the diagram below:



As shown in the diagram the household provide factor services to the firms & firms provide factor payment. Similarly, firms provide goods & services to the household & households pay price for goods & services in return.

Q. In a two sector economy national product is equal to national income, comment?

Ans. In a two sector model the national product is distributed among factor of prodn in the terms of money value of goods & services. It means total money value of output is given to factor prodn in the form of rent, interest, profit & wages so, national product in two sector economy is just equal to national income.



Q. How does real flow consists of factor flow or product flow?

Ans. Real flow consists of two kinds of flows :-

1. factor flow : the flow of factor services from household to firms

2. product flow : the flow of goods & services from firms to households.

Q. classify the following as stock & flow

1. amount of bank deposit as on 31 march – stock
2. losses – flow
3. product of cement during 2017 – flow
4. profit – flow
5. population as on 31 Mar 2018 – stock
6. No. of literate people as on 1 Jan 2018 – stock
7. savings – flow
8. National income – flow
9. capital – stock
10. No. of people employed during 2018 – flow

10/03/19

Chapter. Basic concepts of Macro economics

Q1 what do you mean by a domestic & economic territory?

Ans. Domestic territory means the political frontiers of the country but for the purpose of national income accounting it is not confined to the same but also includes the following :

1. ships & aircrafts owned and operated by normal residents between two or more countries eg planes operated by air india between other countries is a part of domestic territory of India.

2. fishing vessels oil vessels and natural gas rigs operated by a residents of a country in the international water eg fishing boats operated by indian fisher man in the international waters

3. embassies consulates and military establishment of a country located abroad eg indian embassie located in America is a part of indian domestic territory.

Q2. who are the normal residents of the company

Ans Normal residents of a country are an individual or an institution who ordinarily resides in a country who centre of economic interests also lies in that country that is the residents carries out the basic economic activities of earning spending and accumulation from that location following are not included under this :

1 foreign tourists & visitors.

2. foreign staff of embassies and members of armed forces of a foreign country.
3. international organisations like UNO, WHO, are not considered as normal residents of the country in which they operate instead they are normal residents of international area.
4. crew members of foreign vessels and commercial travel who stay for less than a year.
5. Border workers who live near the international border and cross the border regularly to work in other country. They are treated as normal residents of the country where they live.

Q. What do you mean by factor income?
Ans. factor income refers to the income received by factors of production for rendering services like rent given to land, wages to labour, profit to entrepreneur etc. This is bi-lateral payment given in exchange of services.

Q. What do you mean by Transfer income?
It is a unilateral payment and it refers to that income which is received without rendering any productive services in return eg old age pension, scholarship, pocket money etc.

Q. Differenciate between transfer income and factor income?

Basis	factor income	Transfer income
meaning	It refers to income received by factors of prodn for rendering factor services in the prodn process.	It refers to income received without rendering any productive services in return.
inclusion	It is included in national as well as domestic income	It is neither included in national income nor domestic income
concept	It is earning concept	It is a receipt concept
recipient	It is received by factor of prodn	It is received by general households
Example	Rent, interest, profit, etc	scholarships, gift, grants etc.

Q = What are the final and intermediate goods?
Ans * final - It refers to those goods which are used either for consumption or for investment. they are neither resold nor used in further prodn process eg meat, milk etc purchased by household.

* intermediate - those goods which are either resold or used for further prodn process. they are not directly used for consumption purposes. eg fabric used by govt. manufactures. the cost of such good is merged with the value of final goods.

Q. Difference between final & intermediate goods

Basis	Intermediate	Final
Meaning	Definition	Definition
Inclusion	They are neither included in national nor Domestic income	They are included in national as well as Domestic income.
Value addition	Some value has to be added in these goods to make them usable.	No value has to be added in final goods.
Production boundary	They are still within the production boundary	They have crossed the prodn boundary
Example	fabric used by garment manufacturing	milk & meat purchased by household.

23/3/19.

Q. What is consumption goods & capital goods

Ans. Consumption goods refer to those goods which satisfy the wants of consumer directly eg bread, butter, pens, TV etc.
These goods are further classified into following categories

(1.) Durable goods - those goods which can be used again and again over a period of time eg. TV, mobile etc.

(2) Semi durable good - those goods which can be used for a ltd period of time which is generally one year. In other words goods which can be used again and again but for a ltd. period of time only eg. A tooth brush, clothes.

(3) Non-durable goods - those goods which can be used for a single consumption and can not be used again and again are known as non-durable goods eg. apple, milk, bread etc.

(4) Services - It refers to non-material goods which directly satisfy the human wants these are intangible that is they can't be seen or touched eg. service of a teacher, doctor

• Capital goods : those goods which are final goods and helps in prodn of others goods and services. eg plant and mach., equipments etc.

These goods are used in future for productive purposes and have expected lifetime of several years they do not loose their identity in the process of production there val is derived val. It must be noted here that all goods used by producers are not capital goods there are certain goods which are used by producer goods for one time only are known single use producer goods eg coal & electricity etc. but those goods which are used again and again by the producer are known as capital goods.

Q- Difference between consumer goods & capital goods

Basis	Consumer	Capital
satisfaction of human wants	These goods satisfy human want directly.	These goods satisfy human want indirectly.
val	They have direct val..	They have indirect val.
prodn capacity	They do not help in raising production capacity	These goods help in raising prodn capacity
prodn boundary	These goods cross the prodn boundary	These goods do not cross the prodn boundary
eg.	bread, egg, TV etc	plant & machinery, furniture

Q- Differentiate and identify the following goods as consumer goods, capital and intermediate goods.

(1) car purchased by mrx for his family - consumer good.

(2) car purchased by taxi driver as taxi - capital goods

(3) car purchased by a car dealer for resale - intermediate goods.