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MACRO ECONOMICS

Ch 1- Circular Flow of Income.

Ques1 What do you mean by macroeconomics?

Macro is a word derived from the term 'makros' which means large, so macro-economics is that branch of economics that deals with economy as a whole. It deals with aggregates like aggregate demand national income, total consumption, total savings etc.

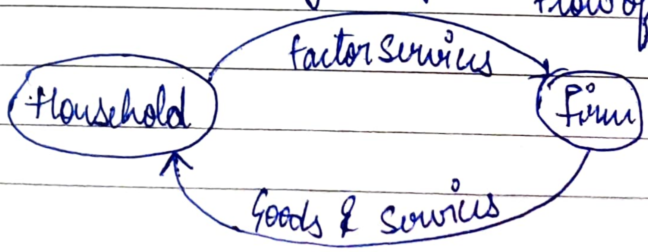
Ques2 What do you mean by circular flow of income?

It refers to the cycle of generation of income in the production process, its distribution among factors of production and finally its circulation from household to firms in the form of consumption to expenditures on goods and services produced by them.

(i) **Real flow**

It refers to the flow of factor services from household to firms and corresponding flow of goods and services from firm to household. It is also known as physical flow where there is only exchange of goods and services between two sectors without involvement of money as shown in following diagrams.

Flow of goods & Services



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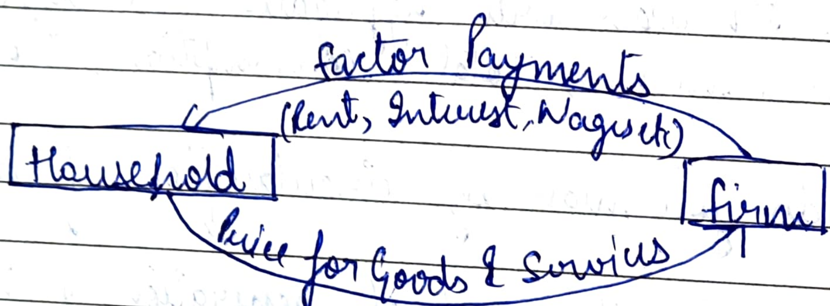
(i) **Money flow**

It refers to flow of factor payments from firm to households for their factor services and corresponding flow of consumption expenditure from household to firms for purchase of goods and services produced by firms as shown in following diagram.



Ques 3 What do you mean by stock and how it is different from flow?

* Stock refers to that variable which is measured at a particular pt. of time. for eg: stock of goods in godown, water in a tank, national wealth, national capital etc.

* Flow refers to that variable which is measured over a period of time. for eg: production of goods during the month of January, Water in a river, national income etc.

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Ques4 Difference b/w Stock and flow?

Basis	Stock	Flow
Meaning	It refers to the variable which is measured at a particular pt. of time.	It refers to a variable which is measured during a period of time.
Time dimension	It does not have a time dimension.	It has a time dimension as it can be measured only over a period of time.
Nature of Concept	It is a static concept	It is a dynamic concept
Example	National wealth, quantity of wheat stored, money supply	National Income, quantity of wheat produced during 2020, expenditure during 2020

Ch-2 Basic Concepts of Macro-Economics

Ques 1 What do you mean by domestic / economic territory?

Ans Domestic territory of an economy is related to but not confide to political frontiers and it means to include following for the purpose of calculation of national income.

(1) Ships and aircrafts operated by normal residents between two or more countries

eg: Airplanes operated by Air India between America, Japan etc.
Similarly, Airplanes operated by Qatar Airways in whole world

(2) Fishing vessels, oil and natural gas rigs and floating platforms operated by residents of a country in international waters

eg: fishing boats operated by Indian fishermen in international waters.

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(3) Embassies, consolates and military establishments of a country located abroad.

eg: indian embassy in America is a part of Indian Domestic territory.

Note: International organisations like UNO, WHO etc located within geographical boundaries of a country are not part of domestic territory of that country.

Ques2: which of the following are covered under domestic territory of India?

1. Branch of State Bank of India in China No
2. Russian embassy in India Not
3. Microsoft Office in India Yes
4. Company in India owned by Japanese Yes
5. Tata lented it's building to Google in America. ~~Yes~~ Not

Ques3. Who are normal residents of a country?

It refers to an individual or an institution who ordinarilly resides in a country and whose centre of economic interest lies in that country.
Here, centre for economic interest implies two things:-
(i) resident lives within domestic territory
(ii) resident carries out basic economic activities like earning spending and accumulation from that location.

Following are not included under the category of normal residence -

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• considered

* Foreign tourist who visit a country for recreation, holidays, medical treatment, sports etc.

* Foreign staff of embassies, officials, dimplomats and members of armed forces of a foreign country located in a given country.

* International organisations like UNO, WHO etc are not • normal residents of a country in which they operate ~~are located~~ but ~~and~~ they are normal residents of international area.

* Employees of international organisations are considered as residents of the country ~~in which they are~~ belong ~~located~~ in which they belong and not international area.

eg: An Indian citizen working with office of UNO located in America shall be considered as normal residents of India

* Crew members of foreign vessels, commercial travellers and seasonal workers provided their stay is less than a year.

* Border workers who live near the international border and cross on a regular basis to work in other country, they are considered as normal residents of the country in which they live and not in which they work.

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Ques4 Who are considered as normal residents of India out of following-

✓(1) Indian officials working in Indian Embassy in America.

(2) A Japanese tourist who stays in India for 2 Months.

✓(3) Indians going to Pakistan for watching Cricket Match.

✓(4) Indian working in UNO office located in America for less than 1 year.

✓(5) Indian Employees working in WHO located in India.

Ques5 What do you mean by factor income? and how it is different from transfer income?

Basis	Factor Income	Transfer Income
Meaning	It means the income received by factors of production for giving factor services in production process.	It is the income received without giving any productive services in return
Nature	It is included in domestic as well as national income (Bilateral)	It is neither included in domestic nor in national income. (Unilateral)

Basis	Factor	Transfer
Concept	It is an earning concept	It is a receipt concept
Recipient	It is received by factors of production (land, labour, capital etc)	It is received by households and govt.
Example	Rent, interest, profit etc	Gifts, Scholarships, grants etc.

Ques What do you mean by final goods and how are they different from Intermediate goods?

Final Goods

These refer to those goods which are used either for consumption or for investment. It includes goods purchased by household for consumption and goods purchased by firms for capital formation or investment.

Intermediate Goods

Those goods which are used either for resale or for further production in the same year, they are normally purchased by one production unit from another production unit. Their

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demand is derived demand.

Ques7 Identify whether the following are intermediate goods or final goods.

1. Paper purchased by a publisher I
2. Furniture purchased by a school F
3. Milk purchased by a household F
4. Computer installed in an office F
5. Coal used by manufacturing firms I
6. Purchase of pulses by a consumer F
7. Coal used by consumer households F
8. Mobile sets purchased by Mobile dealer. I

Ques8 What do you mean by consumer goods?

Consumption goods refer to those goods which satisfy the wants of consumers directly.
eg: bread, butter, television, mobile phone etc.
These goods can further be classified into following -

(1) **Durable goods** - It refer to those goods that can be used again and again over a considerable period of time.
eg: television, mobile phone

(2) **Semi Durable goods** - Those goods which can be used for a limited period of time generally one year are known as semi-durable goods.
eg: stationary, crockery, shoes etc.

(3) **Non-Durable goods** - Those goods which can be used for a single consumption and cannot be used again and again are known as non-durable goods.
eg: vegetable, fruits, milk, etc.

(4) **Services** - It refer to non-material goods which directly satisfy the human needs. They cannot be seen or touched and one pt. to be noted is there is no difference of time in production & consumption of services.

Ques9 What do you mean by capital goods?

It refer to those final goods which are used in production of other goods and services.
eg: plant & machinery, equipments etc.
These goods do not lose their identity in the production process. They are used for production purposes and have expected life of several years. These goods have derived demand because their demand depends upon demand of

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other goods which they produce.

Note - A point to be noted is that all goods used by a producer are not capital goods and producer goods include 2 types of goods

1. Single use producer goods
2. Capital Goods

Ques 10 Differentiate b/w Consumer and Capital goods.

Basis	Consumption Goods	Capital Goods
1. Meaning	It refer to those goods which satisfy the wants of consumers directly.	It refer to those goods which help in production of other goods & services
2. Satisfaction of human wants	They satisfy human wants directly	They satisfy human wants indirectly
3. Production capacity	They do not promote/increase production capacity	They promote production capacity
4. Expected life	They generally have a limited life	They generally ~~exp~~ have expected life more than 1 year.

Ques 17 What do you mean by production boundary?

Ans Production boundary is a line around production sector as long as goods remain within the production boundary, they are intermediati goods and when they come out of production boundary they become final goods. It is an imaginary line drawn around the productive sector and this boundary is imp. to be understood to understand the diff. b/w intermediati & final goods.
for eg: wheat produced by a farmer goes to a flour mill, flour produced by the mill goes to a bakery, from the bakery bread is produced and from that bread, a sandwhich is produced. A sandwhich is the final good which moves out of the production boundary.

Production Boundary
↓
Wheat produced by a farmer
↓
Flour produced by flour Mill
↓
Bread produced by baker & then sandwhich

sandwhich is a final good goes out of production boundary affects / hamper

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Ques 12 What do you mean by depreciation and how is it different from capital loss?

Basis	Depreciation	Capital loss
Meaning	It refers to the fall in value of fixed asset due to normal wear and tear or pass of time	It refers to loss in the value of asset due to reasons like accidents, natural calamities, thefts etc.
Provision for loss	Provision is made for replacement of asset since it is an expected loss	No such provision is made since it is an unexpected loss
Effect on Production Process	It does not affect the production process	It affects / hampers the production process

Ques 13 What do you mean by indirect taxes?

Those taxes whose burden ~~ind~~ incidence can be shifted on to another are known as indirect taxes. In other words, a tax which is charged ~~by~~ one one, paid by another is known as indirect tax

eg GST, Custom duty, entertainment tax, excise duty.

Net Indirect Tax

It refers to the difference b/w ~~net~~ indirect taxes and subsidies

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Net Indirect Tax = Indirect Tax − Subsidies

Ques 7 What do you mean by net factor income from abroad and what are its components?

It refers to the difference b/w factor income received from rest of the world and the factor income given to the rest of the world.

NFIA = factor income from abroad − factor income to abroad.

NFIA = FIFA − FITA

Here, factor income from abroad means to include the income earned by normal residents of a company from abroad in the form of rent, interest, profit, wages etc. And factor income to abroad means to include the incomes paid to normal residents of other countries for their factor services within the economic territory.

Components of NFIA include following -

(1) Net compensation to employees -
It refers to difference b/w income from work received by resident workers living abroad for less than one year and similar payments made to non-resident workers employed within the domestic territory.

② Net income from property and enterprenuership -
It refers to the difference b/w income received from property and enterpreneurship (rent, interest, dividend) received by residents of a country at similar payments made to non-residents.

③ Net retained earnings -
It refers to the difference b/w retaind earnings of resident companies located abroad and retained earnings of non-resident companies located within the domestic territory

Factor Income = Land + labour + Cap + Ent.

Land ↓ Rent

labour ↓ Wages.

Cap ↓ Int.

Ent. ↓ Profit

Profit → Corp. Tax, Dividend, Retained Earnings

NFIA → Net COE (Wages), Net Income from Prop & Ent (Net Rent, Int. Dividend), Net Retained earnings

Domestic Y + NFIA = National Y

Ques 15 Are the following statements true or false. Give Reasons.

① Intermediate goods have a derived demand while final goods have direct demand.

True

→ Intermediate goods have derived demand. Their demand depends upon demand for final goods. On the other hand final goods have a direct demand, as they satisfy consumer demands directly.

(2) Bread is always a consumer good.

→ False

It depends upon the end use of the bread when purchased by a producer for producing some other goods, it is an intermediate good.

(3) In final goods, no value is to be added.

True

Because final goods final goods have already crossed the production boundary

(4) End use of the goods categorised them into intermediate and final goods.

True

Because it is only the end use that explains whether good has been used as intermediate or as final good

(4) Final goods include only those goods which are consumed by household.

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False, because final goods are those which are purchased by either by household for consumption or by producer for investment

(5) Both expected obsolescence and unexpected obsolescence are considered for determining the amt of depreciation

False, because depreciation is calculated only on the basis of expected obsolescence.

Ques6 Gross investment v/s Net Investment

Gross Investment :- Investment is addition to stock of capital before making any allowance for depreciation. So it is the expenditure on purchase of fixed assets and unsold stock during the year.

Net Investment :- It refers to actual addition made to capital stock of economy in a given period of time. In other words, investment after making allowing for depreciation so,

Net investment = Gross Investment − Depreciation

Ques17 How citizenship is different from residentiship?

Basis	Citizenship	Residentship
~~Basis~~ Meaning	A person who is born in India or person who is ~~lives~~ born outside India and apply for citizenship become citizen of India	A person or an institution who ordinarily resides in a country and whose centre for economic interest lies in that country
Concept	It is a legal concept based on place of birth or some legal provision	It is an economic concept based on economic activity performed by a person
Change from year to year	It does not change on the basis of time period of stay year to year	It may change on the basis of stay from year to year.