Shoolini University

Course– Indian Economy Econ(H)221

Lecture 6 : National Income: Concepts and Measurement

National Income - introduction

- **Definitions**:
  - The labor and capital of a country, working on its natural resources produces certain net amount of goods and services, the aggregates of which is known as national income or national product.
  - Is also defined as the total market value of all the final goods and services produced in an economy in a given period of time.
- **National income (NI):**
  - Is an important indicator of a nation's progress
  - GNP (NI) being the monetary measure of all final goods and services produced, is widely used as an index for judging the performance of an economy.
  - The concept of NI is linked to the society as a whole, in contrast to the private income. But NI is not merely the simple aggregation of private incomes.

National Income …

- **Gross National Product at Market Price (GNP_{MP})**

- GNP_{MP} is the total value of all the final goods and services produced during the period of one year plus the net factor incomes earned from abroad during that year,

  i.e. the earnings of all the nationals, whether operating within the country or outside it; and at the same time it excludes the income earned by foreign nationals residing in the country.

National Income …

- **Net National Product at Marker Price (NNP_{MP}):**

NNP_{MP} is equal to GNP minus the charges on account of depreciation and replacements, where depreciation represents the values of fixed capital consumed during the process of production.

$$\mathbf{NNP_{MP}} = \mathbf{GNP_{MP}} - \text{Depreciation}$$

National Income …

- **Net National Product at Factor Cost (NNP_{FC}) or NI**

  - **NNP_{FC}** or National income is equal to the sum total of factor incomes received by the factors of production during the year. It is equal to the sum of rent, wages, interests and profits in a given year.
  - Thus, the national income is equal to the **NNP_{MP}** minus revenue of the government by way of indirect taxes plus subsidies provided by the government.

National Income …

- **National Income at Current Price and Constant Price:**

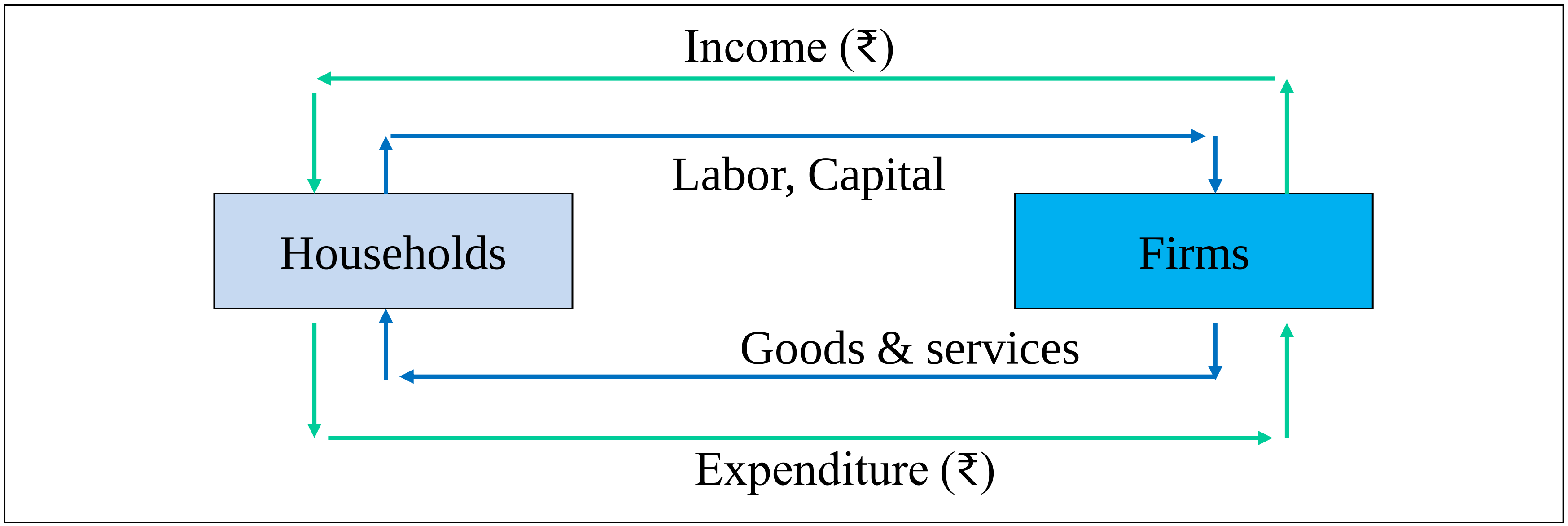
•When the value of goods and services is found out by multiplying the quantity produced during one year by the prices prevailing in that year, it is national income at current prices.

•On the other hand, when the value of goods and services is calculated by multiplying the quantity during one year with prices of the base year, it is called National Income at Constant Prices.

Income, Expenditure and Circular Flow

Two ways of viewing GDP

- Total **income** of everyone in the economy, measured in a specific way
- Total **expenditure** on the economy's output of goods and services



For the economy as a whole, ***income must equal expenditure***.

Methods of Measuring national income

National income of a country can be measured in three alternative ways

- As a flow of income, and
- As a flow of expenditure
- Value added method.

Product Method

- This method is popular in U.S.A. and is called as Total Product method or Goods Flow Method. In India, It is known as inventory or Product method. In this method, the economy is classified in to three transaction sector like industrial, services and foreign transaction sector
- Calculate the money value of all final goods and services produced in an economy during a year at market price (GDP).

Income Method

- Calculate the income earned by various factor services engaged in the process of production. The sum of these incomes provides us the measure of gross national income at factor cost (NNP at Factor Cost)
- GNP = wages and salaries + rent +interest + Dividends + undistributed corporate profits + mixed incomes + direct taxes + indirect taxes + depreciation + net income from abroad

Expenditure method

- Prof. Samuelson calls this as " Flow of Product Approach". In India, it is known as Outlay method.
- GNP is the sum of expenditure incurred on goods and services during one year in a country.
- **GNP = C + I + G + (x – M)**
- We sum up the flow of expenditure in an economy to arrive at national income estimates,
- If we add the value of expenditure on all these items we get the value of gross national expenditure at market prices.

Value Added Method

- In order to avoid double counting value added at each stage of production should be calculated to arrive at GNP.
- Difference between the value of output and input at each stage of production is called the value added.
- By adding such value added for all industries in the economy, GNP can be calculated.

Items excluded from National Income Accounting

- What is not/is counted
  - Intermediate goods X
  - Resale of existing houses X
  - Second hand goods (used cars etc.) X
  - Existing shares X
  - Non marketed goods and services (volunteer work, Housework) X
  - Unreported/illegal transactions X
  - Capital gain is not income X
  - Commission /Brokers' fee √
  - Imputed rents of owner-occupied dwellings √
  - Only the interest earned from the capital gain is considered as income √

Thank you

Dr. (Ms) Kesari Singh
School of Business Management and Liberal Arts
Shoolini University
Village Bajhol, Solan (H.P)
+91 9816603968
kesari@shooliniuniversity.com