Study Materials for BA (Hons.) Economics

Part – 1

Paper- 2

Topic – National Income Concept and Measurement

Introduction

National income is an uncertain term which is used interchangeably with national dividend, national output and national expenditure. On this basis, national income has been defined in a number of ways. In common parlance, national income means the total value of goods and services produced annually in a country.

In other words, the total amount of income accruing to a country from economic activities in a year's time is known as national income. It includes payments made to all resources in the form of wages, interest, rent and profits.

Definition of national income

Simon Kuznets has defined national income as "the net output of commodities and services flowing during the year from the country's productive system in the hands of the ultimate consumers."

Concepts of national income

There are a number of concepts pertaining to national income and methods of measurement relating to them.

1- Gross domestic product (GDP):- GDP is the total value of goods and services produced within the country during a year. This is calculated at market prices and is known as GDP at market prices. Dernberg defines GDP at market price as "the market value of the output of final goods and services produced in the domestic territory of a country during an accounting year."

There are three different ways to measure GDP:

A- The Product Method: - In this method, the value of all goods and services produced in different industries during the year is added up. This is also known as the value added method to GDP or GDP at factor cost by industry of origin. The following items are included in India in this: agriculture and allied services; mining; manufacturing, construction, electricity, gas and water supply; transport, communication and trade; banking and insurance, real estates and ownership of dwellings and business services; and public administration and defence and other services (or government services). In other words, it is the sum of gross value added.

B- The Income Method: - The people of a country who produce GDP during a year receive incomes from their work. Thus GDP by income method is the sum of all factor incomes: Wages and Salaries (compensation of employees) + Rent + Interest + Profit.

C- Expenditure Method: - This method focuses on goods and services produced within the country during one year.

GDP by expenditure method includes:

a- Consumer expenditure on services and durable and non-durable goods (C)

b- Investment in fixed capital such as residential and non-residential building, machinery, and inventories (I)

c- Government expenditure on final goods and services (G)

d- Export of goods and services produced by the people of country (X)

e- Less imports (M). That part of consumption, investment and government expenditure which is spent on imports is subtracted from GDP. Similarly, any imported component, such as raw materials, which is used in the manufacture of export goods, is also excluded.

Thus GDP by expenditure method at market prices = C+ I + G + (X – M), where (X-M) is net export which can be positive or negative.