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95%(66)95% found this document useful (66 votes)38K viewsThe document discusses the meaning and definitions of economics. It covers traditional and modern approaches to economics including microeconomics and macroeconomics. Microeconomics focuses SaveSave Agricultural Economics Notes For Later95%95% found this document useful,
undefined580 California St., Suite 400San Francisco, CA, 94104 The series concentrates on theprinciples, techniques and applications of policy analysis, planning and implementation ofagriculturaland rural development. Language:English Pages:87 Author:Dr. N Sunanda Price:Free Lecture 1: Economics Meaning, Definitions, Subject matter of
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elastic demand-types of elasticity of demand-price elasticity of demand- income elasticity-cross elasticity of demand-factors affecting elasticity of demand- practical importance of elasticity of demand. Lecture 15: Supply meaning, definition, law of supply, supply schedule, supply curve. Lecture 16: Increase and decrease in supply, contraction and
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cost, personal income, disposable income. Lecture 22: Methods of measurement of NI product method, income method and expenditure method Lecture 23 Public Finance meaning, Role and importance of Public finance functions of the government Differences between public finance and private finance Lecture 24 Public revenue meaning, major and
minor sources of public revenue Lecture 25: Tax meaning, classification direct and indirect taxes, methods of taxation proportional, progressive, regressive and degressive taxation, Agril taxation other types of taxation, VAT. Lecture 26: Canons of Taxation Adam Smiths canons of taxation equality, economy, certainity and convenience other canons of
taxation Lecture 27 & 28: Public expenditure meaning, need for public expenditure. principles of public expenditure Lecture 29 & 30: Inflation meaning, definition, types of inflation demand pull and cost push inflation- comprehensive and sporadic inflation suppressed and repressed inflation creeping, walking, running and galloping inflation mark up
inflation Related concepts of inflation, Rate of inflation Lecture 31 & 32: Causes of inflation Remedial measures monetary fiscal measures. Reference Books All Agriculture Books Free Download All Dairy Technology Books Free Download All Agricultural Engineering Books Free download All Horticulture Books Free Download For Daily Update follow
us at: Facebook Telegram Whatsapp Instagram YouTube Feedback:After Reading these ICAR eCourse, please give your feedback for improve of the e-Course contents on this website.Click Here Disclaimer:The information on this website does not warrant or assume any legal liability or responsibility for the accuracy, completeness or usefulness of the
courseware contents. The contents are provided free for noncommercial purpose such as teaching, training, research, extension and self learning. If you are facing any Problem than fill formContact Us If you want share any article related Agriculture with us than send atinfo@agrimoon.comwith your contact detail.Economic theory applied to food
production and land use for the agriculturePart of the behavioral sciencesEconomicsOutlineIndexGlossaryEconomists Principles of EconomicsTools and methodologyEconomic theoryMathematical modelingGame theoryRational choiceCognitive science (Behavioral)Economic equilibriumEmpirical methodsExperimentalNational
accountsEconometricsTime seriesSpatialPrescriptive and policyWelfare analysisSocial choice theoryRational choice theoryCostbenefit analysisBranches and subfieldsAppliedEconometricsInternationalHeterodoxMicroMacroMainstreamMathematicalMech. designMethodologyPoliticalIndustrial org.Market
designApplicationsAgricultureBusinessCulturalDemographicDevelopmentEcologicalEducationEngineeringEnvironmentalEvolutionaryFinancialGeographicHappinessHealthHistoryInformationInfrastructureInstitutionsLabourLawManagementOrganizationParticipationPersonnelPlanningPolicyPublic sectorPublic choiceSocial
choiceRegionalRegulatoryResourcesRuralServiceTransportUrbanWelfare Economics portal Society portalvteAgricultural economics is an applied field of economics concerned with the application of economic theory in optimizing the production and distribution of food and fiber products. Agricultural economics began as a branch of economics that
specifically dealt with land usage. It focused on maximizing the crop yield while maintaining a good soil ecosystem. Throughout the 20th century the discipline expanded and the current scope of the discipline is much broader. Agricultural economics today includes a variety of applied areas, having considerable overlap with conventional economics.
[1][2][3][4] Agricultural economists have made substantial contributions to research in economics, econometrics, development economics, and environmental economics. Agricultural economics influences food policy, agricultural policy, and environmental policy.Cartoon showing U.S. President Calvin Coolidge carrying the McNaryHaugen Farm Relief
Bill in a dustpan out to a trash can labeled "VETO"Part of a series onEconomic systemsMajor typesCapitalismSocialismBy ideologyAssociativeCapitalistCorporateDemocraticLaissez-faireMercantilistNeo-NeoliberalSocial
marketStateWelfareDemocraticDevelopmentalismDistributistFascistFeministFreiwirtschaftGeorgistGreenNationalistProtectionistReligiousBuddhist economicsChristianSabbath economicsIslamicSocialistCommunistMarket socialistMutualistParticipatorySocialist marketSocialist-oriented marketStateSyndicalistSocial
creditTraditionalistCorporatistFeudalismBy coordinationClosed (autarky)DecentralizedDigitalDirigistDualGiftInformalMarketMixedNaturalOpenPlannedRobinson CrusoeSharingSubsistenceUndergroundVertical archipelagoVirtualBy regional modelAsianEast AsianChineseSingaporeanKeralanEuropeanAnglo-
SaxonGermanNordicDutchRhenishSovietLatin AmericaSocialism of the 21st centurySectorsCommon ownershipPrivatePublicVoluntaryProperty typesCollective ownershipCommons (Common ownership)Private propertyState ownershipSocial
ownershipTransitionCollectivizationCommunizationCorporatizationDemutualizationDeregulationExpropriationFinancializationLiberalizationMarketizationMunicipalizationMutualizationNationalizationPrivatizationSocializationMarxistCoordinationBarterMarketFreeOpenRegulatedPlanningIn kindCyberneticsIndicativeMaterial balancingPriceSelf-
managedPeer-to-peerSharingOpen accessOther typesAttentionCommons-based peer productionExpeditionaryHunter-gathererInclusive DemocracyInformationManorialismNewly industrializedPalacePlantationPlutonomyPost-capitalistPost-industrialPost-scarcityResource-basedTokenTraditionalTransitionWorld Business portal Economics
portalvteEconomics has been defined as the study of resource allocation under scarcity. Agricultural economics, or the application of economic methods to optimize the decisions made by agricultural producers, grew to prominence around the turn of the 20th century. The field of agricultural economics can be traced back to works on land economics.
Henry Charles Taylor was the greatest contributor in this period, with the establishment of the Department of Agricultural Economics at the University of Wisconsin in 1909.[5]Another contributor, 1979 Nobel Economics Prize winner Theodore Schultz, was among the first to examine development economics as a problem related directly to
agriculture.[6] Schultz was also instrumental in establishing econometrics as a tool for use in analyzing agricultural economics empirically; he noted in his landmark 1956 article that agricultural supply analysis is rooted in "shifting sand", implying that it was and is simply not being done correctly.[7]One scholar in the field, Ford Runge, summarizes
the development of agricultural economics as follows:Agricultural economics arose in the late 19th century, combined the theory of the firm with marketing and organization theory, and developed throughout the 20th century largely as an empirical branch of general economics. The discipline was closely linked to empirical applications of
mathematical statistics and made early and significant contributions to econometric methods. In the 1960s and afterwards, as agricultural sectors in the OECD countries contracted, agricultural economists were drawn to the development problems of poor countries, to the trade and macroeconomic policy implications of agriculture in rich countries,
and to a variety of production, consumption, and environmental and resource problems.[8]Agricultural economists have made many well-known contributions to the economics field with such models as the cobweb model,[9] hedonic regression pricing models,[10] new technology and diffusion models (Zvi Griliches),[11] multifactor productivity and
efficiency theory and measurement,[12][13] and the random coefficients regression.[14] The farm sector is frequently cited as a prime example of the perfect competition economic paradigm.In Asia, the Faculty of Agricultural Economics was established in September 1919 in Hokkaido Imperial University, Japan, as Tokyo Imperial University's School
of Agriculture started a faculty on agricultural economics in its second department of agricultural science. In the Philippines, agricultural economics was offered first by the University of the Philippines Los Baos Department of Agricultural Economics in 1919. Today, the field of agricultural economics has transformed into a more integrative discipline
which covers farm management and production economics, rural finance and institutions, agricultural marketing and prices, agricultural policy and development, food and nutrition economics, and environmental and natural resource economics.Since the 1970s, agricultural economics has primarily focused on seven main topics, according to Ford
Runge: agricultural environment and resources; risk and uncertainty; food and consumer economics; prices and incomes; market structures; trade and development; and technical change and human capital.[15]In the field of environmental economics, agricultural economists have contributed in three main areas: designing incentives to control
environmental externalities (such as water pollution due to agricultural production), estimating the value of non-market benefits from natural resources and environmental amenities (such as an appealing rural landscape), and the complex interrelationship between economic activities and environmental consequences.[16] With regard to natural
resources, agricultural economists have developed quantitative tools for improving land management, preventing erosion, managing pests, protecting biodiversity, and preventing livestock diseases.[17]While at one time, the field of agricultural economics was focused primarily on farm-level issues, in recent years agricultural economists have studied
diverse topics related to the economics of food consumption. In addition to economists' long-standing emphasis on the effects of prices and incomes, researchers in this field have studied how information and quality attributes influence consumer behavior. Agricultural economists have contributed to understanding how households make choices
between purchasing food or preparing it at home, how food prices are determined, definitions of poverty thresholds, how consumers respond to price and income changes in a consistent way, and survey and experimental tools for understanding consumer preferences.[18]Agricultural economics research has addressed diminishing returns in
agricultural production, as well as farmers' costs and supply responses. Much research has applied economic theory to farm-level decisions. Studies of risk and decision-making under uncertainty have real-world applications to crop insurance policies and to understanding how farmers in developing countries make choices about technology adoption.
These topics are important for understanding prospects for producing sufficient food for a growing world population, subject to new resource and environmental challenges such as water scarcity and global climate change.[19]Development economics is broadly concerned with the improvement of living conditions in low-income countries, and the
improvement of economic performance in low-income settings. Because agriculture is a large part of most developing economies, both in terms of employment and share of GDP, agricultural economists have been at the forefront of empirical research on development economics, contributing to our understanding of agriculture's role in economic
development, economic growth and structural transformation. Many agricultural economists are interested in the food systems of developing economies, the linkages between agriculture and nutrition, and the ways in which agriculture interact with other domains, such as the natural environment.[20][21]The International Association of Agricultural
Economists (IAAE) is a worldwide professional association, which holds its major conference every three years. The association publishes the journal Agricultural Economics.[22] There also is a European Association of Agricultural Economists (EAAE), an African Association of Agricultural Economists (AAAE) and an Australian Agricultural and
Resource Economics Society. Substantial work in agricultural economics internationally is conducted by the International Food Policy Research Institute.In the United States, the primary professional association is the Agricultural & Applied Economics Association (AAEA), which holds its own annual conference and also co-sponsors the annual
meetings of the Allied Social Sciences Association (ASSA). The AAEA publishes the American Journal of Agricultural Economics and Applied Economic Perspectives and Policy.Graduates from agricultural and applied economics departments find jobs in many sectors of the economy: agricultural management, agribusiness, agricultural marketing,
education, the financial sector, government, natural resource and environmental management, real estate, and public relations. Careers in agricultural economics require at least a bachelor's degree, and research careers in the field require graduate-level training;[23] see Masters in Agricultural Economics.A 2011 study by the Georgetown Center on
Education and the Workforce rated agricultural economics tied for 8th out of 171 fields in terms of employability.[24][25]Evenson, Robert E. and Prabhu Pingali (eds.) (2007). Handbook of Agricultural Economics. Amsterdam, NL: Elsevier.Agriculture portalBusiness and economics portalAgrarian lawAgrarian reformAgribusinessAgricultural
recessionAgricultural value chainDevelopment economicsDIRTI 5Electrical energy efficiency on United States farmsFood gradingFood securityLand economicsSubsidizingTransport economicsVertical archipelagoNourse, E. G. (1916). "What is Agricultural Economics?". Journal of Political Economy. 24 (4): 363381.^ Karl A. Fox (1987). "agricultural
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Policy Research Institute (IFPRI)Academic and professional associationsAfrican Association of Agricultural Economists (AAAE)Australian Agricultural and Resource Economics AssociationAgricultural & Applied Economics Association (AAEA)Canadian Agricultural Economics Society (CAES) Archived 2015-05-15 at the Wayback MachineEuropean
Association of Agricultural Economists Archived 2021-03-10 at the Wayback MachineInternational Association of Agricultural Economists (IAAE) Archived 2020-10-31 at the Wayback MachineGovernment agenciesU.S. Agency for International Development, Bureau for Economic Growth, Agriculture, and TradeU.S. Department of Agriculture,
Economic Research ServiceEuropean Commission on FarmingAcademic journalsAgricultural Economics (AgEcon)American Journal of Agricultural Economics (AJAE)Applied Economic Perspectives and Policy (AEPP)Department of Agricultural and Resource Economics records at the University of Maryland librarieseurasian journal of agricultural
economicsRetrieved from " . 1LECTURE NOTESCourse No. AECO 141Principles of Agricultural EconomicsCompiled byDr.N SunandaAssistant ProfessorDepartment of Agricultural EconomicsAcharya N G Ranga Agricultural UniversityAgricultural College, NAIRA 2. 2Lecture no.1Economics Meaning, Definitions, Subject matter of Economics
Traditionalapproach consumption, production, exchange and distributionECONOMICSEconomics is popularly known as the Queen of Social Sciences. Itstudies economic activities of a man living in a society. Economic activities are thoseactivities, which are concerned with the efficient use of scarce means that can satisfy thewants of man. After the
basic needs viz., food, shelter and clothing have been satisfied,the priorities shift towards other wants. Human wants are unlimited, in the sense, that assoon as one want is satisfied another crops up. Most of the means of satisfying thesewants are limited, because their supply is less than demand. These means have alternativeuses; there emerge a
problem of choice. Resources being scarce in nature ought to beutilized productively within the available means to derive maximum satisfaction. Theknowledge of economics guides us in making effective decisions. The subject matter ofeconomics is concerned with wants, efforts and satisfaction. In other words, it deals withdecisions regarding the
commodities and services to be produced in the economy, how toproduce them most economically and how to provide for the growth of the economy.Subject matter of economicsEconomics has subject mater of its own . Economics tells how a man utilises hislimited resources for the satisfaction of unlimited wants. Man has limited amount of timeand
money. He should spend time and money in such away that he derives maximumsatisfaction. A man wants food, clothing and shelter. To get these things he must havemoney. For getting money he must make an effort. Effort leads to satisfaction. Thus,wants- efforts- satisfaction sums up the subject mater of economics initially in a primitivesociety
where the connection between wants efforts and satisfaction is direct .Divisions of EconomicsThe subject matter of economics can be explained under two approaches viz.,Traditional approach and Modern approach.Traditional ApproachIt considered economics as a science of wealth and divided it into four divisionsviz., consumption, production,
exchange and distribution1. Consumption: It means the use of wealth to satisfy human wants. It also meansthe destruction of utility or use of commodities and services to satisfy humanwants.2. Production: It is defined as the creation of utility. It involves the processes andmethods employed in transformation of tangible inputs (raw materials, semi- 3.
3finished goods, or subassemblies) and intangible inputs (ideas, information, know-how) into goods or services.3. Exchange: It implies the transfer of goods from one person to the other. It mayoccur among individuals or countries. The exchange of goods leads to an increasein the welfare of the individuals through creation of higher utilities for goods
andservices.4. Distribution: Distribution refers to sharing of wealth that is produced among thedifferent factors of production .It refers to personal distribution and functionaldistribution of income. Personal distribution relates to the forces governing thedistribution of income and wealth among the various individuals of a country.Functional
distribution or factor share distribution explains the share of totalincome received by each factor of production viz., land, labour, capital andorganisation.Lecture No.2Modern Approach Microeconomics and macroeconomics - Methods of economicinvestigation Deduction & , InductionModern Approach :This approach divides subject matter of
economics into two divisions i.e., microeconomics and macro economics. The terms micro- and macro- economics were firstcoined and used by Ragnar Frisch in 1933.1. Micro-Economics or Price Theory:The term micro-economics is derived from the Greek word micro, which means smallor a millionth part. It is also known as price theory. It is an
analysis of the behaviour ofsmall decision-making unit, such as a firm, or an industry, or a consumer, etc. It studiesonly the employment in a firm or in an industry. It also studies the flow of economicresources or factors of production from the resource owners to business firms and theflow of goods and services from the business firms to households.
It studies thecomposition of such flows and how the prices of goods and services in the flow aredetermined.A noteworthy feature of micro-approach is that, while conducting economicanalysis on a micro basis, generally an assumption of full employment in the economyas a whole is made. On that assumption, the economic problem is mainly that of
resourceallocation or of theory of price.Importance of Micro-Economics: Micro-economics occupies a very important place inthe study of economic theory. Functioning of free enterprise economy: It explains the functioning of a freeenterprise economy. It tells us how millions of consumers and producers in aneconomy take decisions about the
allocation of productive resources among millionsof goods and services. 4. 4 Distribution of goods and services: It also explains how through market mechanismgoods and services produced in the economy are distributed. Determination of prices: It also explains the determination of the relative prices ofvarious products and productive services.
Efficiency in consumption and production: It explains the conditions of efficiencyboth in consumption and production. Formulation of economic policies: It helps inthe formulation of economic policies calculated to promote efficiency in productionand the welfare of the masses.Limitations of Micro-Economics: Micro-economic analysis suffers from
certainlimitations: It does not give an idea of the functioning of the economy as a whole. It fails toanalyse the aggregate employment level of the economy, aggregate demand, inflation,gross domestic product, etc. It assumes the existence of full employment in the whole economy, which ispractically impossible.2. Macro-Economics or Theory of Income
and Employment:The term macro-economics is derived from the Greek word macro, which meanslarge. Macro-economics is an analysis of aggregates and averages pertaing to theentire economy, such as national income, gross domestic product, total employment, totaloutput, total consumption, aggregate demand, aggregate supply, etc. Macro-
economicslooks to the nation's total economic activity to determine economic policy and promoteeconomic progress.Importance of Macro-Economics: It is helpful in understanding the functioning of a complicated economic system. Italso studies the functioning of global economy. With growth of globalisation andWTO regime, the study of macro-
economics has become more important. It is very important in the formulation of useful economic policies for the nation toremove the problems of unemployment, inflation, rising prices and poverty. Through macro-economics, the national income can be estimated and regulated. Theper capita income and the peoples living standard are also estimated
through macro-economic study.Limitations of Macro-Economics: Individual is ignored altogether. For example, in macro-economics national saving isincreased through increasing tax on consumption, which directly affects the consumerwelfare. The macro-economic analysis overlooks individual differences. For instance, thegeneral price level may be
stable, but the prices of food grains may have gone upwhich ruin the poor. A steep rise in manufactured articles may conceal a calamitous 5. 5fall in agricultural prices, while the average prices were steady. The agriculturistsmay be ruined.DEFINITIONS OF ECONOMICSThe word economics has been derived from the Greek Word OIKONOMICAS
with OIKOS meaning a household and NOMOS meaning management. Kautilya, thegreat Indian statesman, named his book on state crafts as Arthashastra.WEALTH DEFINITION OF ECONOMICS : Adam smith defined Economics as An enquiry into the nature and causes of wealth of nations in his book, entitled Wealthof Nations. He is regarded as the
Father of Economics.Criticisms of Adam smith definition:WELFARE DEFINITION OF ECONOMICS : Alfred Marshall in his bookPrinciples of Economics defined Political Economy or Economics as a study ofmankind in the ordinary business of life, it examines that part of individual and socialaction which is most closely connected with the attainment
and with the use of thematerial requisites of well- being . Thus it is on the one side a study of wealth, and onthe other, and more important side, a part of the study of man.Criticisms of Alfred Marshall definition:SCARCITY DEFINITION OF ECONOMICS: In his publication Nature andSignificance of Economic Science Lionel Robbins formulated his
conception ofEconomics based on the scarcity concept. Economics is the science which studieshuman behaviour as a relationship between ends and scarce means which have alternativeuses.GROWTH DEFINITION OF ECONOMICS: John Maynard Keynes is known as theFather of Modern Economics. He defined economics as the study of the
administrationof scarce resources and of the determinants of employment and income.In the words of Nobel prize winner Prof. Samuelson, Economics is the study of howpeople and society end up choosing with or without the use of money, to employ scarceproductive resources that could have alternative uses, it produces various commoditiesover
time and distributes them for consumption, now or in the future, among variouspersons and groups in society. It analyses costs and benefits of improving patterns ofresources allocation.ImportanceEconomics analyses the economic problems of the society. It plays a major role in theeconomic development of the country by proposing the optimum
allocation of resources. 6. 6Knowledge of economics is useful in understanding various national and internationalevents and trends.Amarthya Sen, Bharat Ratna recipient was awarded Nobel Prize for Economics.Methods of Economics Investigation :There are two methods of economic investigation that are used in economictheory i.e., 1) Deductive
method and 2) Inductive Method1. Deductive Method: This method involves reasoning or inference fromthe general to the particular or from the universal to the individuals. It isalso known as the abstract, analytical, hypothetical or apriori method.Deduction involves four steps:(1) Selecting the problems(2) Formulating the assumptions(3) Formulating
the hypothesis through the process of logical reasoning wherebyinferences are drawn and(4) Verifying the hypothesis.2. Inductive Method: This method is also known as Concrete method,historical method or realistic method. It involves reasoning from particulars to the generalor from the individual to the universal. This method derives economic
generalisations onthe basis of experiments and observations. In this method detailed data are collected oncertain economic phenomenon and effort is then made to arrive at certain generalizationswhich follow from the observations collected.Is Economics a Science or an ArtScience is a systematized body of knowledge in which the facts are so
arrangedthat they speak for themselves. Judged by this standard, economics is certainly ascience.Economics is also an art because it lays down precepts or formulas to guidepeople to reach their goals.Economics therefore is a science as well as an art.Economics A Social Science 7. 7Economics deal with the activities of people living in an organized
communityor society, in such activities which relate to the earning and use of wealth or with theproblems of scarcity, choice and exchange. Hence it called a social science.Positive Economics and Normative Economics:1. Positive economics is concerned with what is whereas Normative economics isconcerned with what ought to be.2. Positive
economics describe economic behaviours without any value judgment whilenormative economics evaluate them with moral judgment.3. Positive economics is objective while normative economics is subjective.4. The statement, Price rise as demand increase is related to positive economics,whereas the statement, Rising prices is a social evil is related
to normative economics.Lecture No.3Agricultural Economics Definitions, Meaning, Importance of AgriculturalEconomics Branches of agricultural economicsAGRICULTURAL ECONOMICSIntroductionA study of economic principles, with emphasis on their application to the solution offarm, agribusiness, and agricultural industry problems in
relationship to other sectors isknown as Agricultural Economics. In other words, it applies principles of economics toissues of agricultural production, natural resources, and rural development. It mainlyfocuses on principles of microeconomics.Agricultural economics began in the 19th century as a way to apply economicprinciples and research
methods to crop production and livestock management. The rootsof the discipline, however, can be found in the writings of the classical economists likeAdam Smith.The word, agriculture comes from the Latin word ager, referring to the soil andcultura, to its cultivation. Agriculture, in its widest sense can be defined as the cultivationand /or
production of crop plants or livestock products. It is synonymous with farming:the field or field dependent production of food, fodder and industrial organic materials.Having known the meaning of agriculture, let us know what economics is.Economics is the science that studies as to how people choose to use scarce productive 8. 8resources to
produce various goods and to distribute these goods to various members ofsociety for their consumption. Now having defined agriculture and economics, we lookinto the field of agricultural economics.DefinitionAgricultural economics is an applied field of economics in which the principles ofchoice are applied in the use of scarce resources such as
land, labour, capital andmanagement in farming and allied activities. It deals with the principles that help thefarmer in the efficient use of land, labour and capital. Its role is evident in offeringpracticable solutions in using scarce resources of the farmers for maximization ofincome.Prof. Gray has defined agricultural economics as The science in which
theprinciples and methods of economics are applied to the special conditions of agriculturalindustryAccording to Prof.Hibbard, Agricultural economics is the study of relationshipsarising from the wealth-getting and wealth-using activity of man in agricultureSnodgras and Wallace defined agricultural economics as an applied phase ofsocial science of
economics in which attention is given to all aspects of problems relatedto agriculture.Importance of agricultural economicsAkin to economics, the field of agricultural economics finds to seek relevance betweencause and effect using the most advanced methods viz, production functions andprogramming models. It uses theoretical concepts of
economics to provide answers to theproblems of agriculture and agribusiness. Initially earnest efforts were made by theeconomists to use the economic theory to agricultural problems. Now the subject mattersof agricultural economics is enriched in many directions and fields taking the relevanttools of sciences particularly mathematics and statistics.
Agricultural depression whichoccurred in last quarter of 19thcentury and middle of 20thcentury brought aboutincreased attention and concern to find out plausible cause and solutions for worldagricultural depression. Here in this context the contribution made by agronomists,economists, horticulturists, etc., is noteworthy. Agriculture is the integral
part of theworld food system, having the foundation links between crops and animal productionsystem. Agricultural economists here have to play a major role in understanding theintricacies involved in the foundation systems. Knowledge regarding problems inproduction, finance, marketing and government policies and their impact on productionand
distribution is very essential to find out suitable solutions for the farm problems.Students of agricultural economics are taught the subject disciplines viz., 9. 9microeconomics, macroeconomics, agricultural production economics, farmmanagement, agricultural marketing etc., to fulfill the requirements.Lecture No.4.Agricultural production economics-
Meaning- Definitions- Subject matter Objectives - Farm Management Meaning scope Definitions- ObjectivesAgricultural production economicsAgricultural production economics is a field of specialization within the subject ofAgricultural Economics. It is concern with the selection of production pattern andresource use efficiency in order to optimize
the objective function of farming communityor the nation within a frame work of limited resources. The goals of agriculturalproduction economics are:(1) To provide guidance to individual farmers in using their resources mostefficiently and(2) To facilitate the most efficient use of resources from the stand point of economy.DefinitionAgricultural
production economics is an applied field of science wherein theprinciples of choice are applied to the use of capital, labour, land and managementresources in the farming industry.Subject matterAgricultural production economics involves analysis of production relationships andprinciples of rational decisions in order to optimize the use of farm
resources onindividual farms and to rationalize the use of inputs from nations point of view. Theprimary interest is applying economic logic to problems that occur in agriculture.Agricultural production economics is concerned with the productivity of inputs.As a study of resource productivity, it deals with resource use efficiency, resourcecombination,
resource allocation, resource management and resource administration.The subject matter of production economics involves topics like factor-productrelationship, factor-factor relationship and product- product relationship, size of farm,returns to scale, credit and risk and uncertainty, etc.Objectives: 10. 101. To determine and outline the conditions
which give the optimum use of capital,labour, land and management resources in the production of crops and livestock.2. To determine the extent to which the existing use of resources deviates from theoptimum use.3. To analyse the forces which condition existing production pattern and resourceuse.4. To explain means and methods in getting from
the existing use to optimum use ofresources.Farm managementIn the context of increased accent on commercialization there is a greater need toimprove the managerial abilities of the farmers. So far the managers in general haveresponded admirably to technological changes that occurred in Indian agriculture. Butresponse of some of the farmers is
not in line with needed direction. We can alwaysdifferentiate those farmers performing against those not performing. Hence, it is ofparamount importance for the farm managers to identify the changes that take place andrespond suitably, for any lapse on his part does not help him to survive in the changingeconomy. This speaks of the need for the
managers to sharpen the skills to tackle varyingproblems that crop up from time to time in the organization of farm business.The role of farm management, therefore, is to supply the information from thefarmers for sound planning. All farm management tools are helpful to the farmers insolving their managerial problems for successful operation of
the farm business.ScopeFarm management is considered to fall in the field of microeconomics. It treats everyfarm as separate unit because of differences in the ability of resources, problems andpotentiality. The main concern of farm management is the farm as a unit. Farmmanagement deals with the allocation of inputs at the level of individual
farms. Theobjective of farm management is to maximize returns from the farm as a whole. It isinterested in the profitability along with practicability. What crops, livestock enterprisesand their combination to grow, what amount of resources to be applied, how the variousfarm activity to be performed, etc., all these fall within the scope of farm
management.DefinitionsFarm management is defined as the science that deals with organization and operation ofthe farm in the context of efficiency and continuous profits (J. N.Efferson)Farm management is defined as the art of managing a farm successfully as measured bythe test of profitableness (Gray)Farm management is a branch of
agricultural economics, which deals with wealth earningand wealth spending activities of farmer in relation to the organization and operation of 11. 11the individual farm unit for securing maximum possible net income (Bradford andJhonson)Objectives1. To examine production pattern and resource use on the farm.2. To identify the factors
responsible for the present production pattern and resourceuse on the farm.3. To determine the conditions of optimality in the resource use and the productionpattern on the farm.4. To analyse the extent of sub optimality in the resource use on the farm, and5. To suggest ways and means in getting the present use of resources to optimalityon the
farm.Lecture No.5Agricultural finance Meaning Definitions micro vs macro finance need foragricultural finance-Agricultural marketing meaning, definition , importance ofagricultural marketingAgricultural financeAgricultural finance generally means studying, examining and analyzing thefinancial aspects pertaining to farm business, which is the
core sector of the country. Thefinancial aspects include money matters relating to production of agricultural productsand their disposal.According to Murray (1953), It is an economic study of borrowing finds by farmers; ofthe organization and operation of farm lending agencies, and of societys interest in creditfor agriculture.According to Tandon and
Dhandyal (1962), as a branch of agricultural economics,which deals with the provision, and management of bank services and financial resourcesrelated to individual farm unitsMicro Vs Macro financeAgricultural finance is viewed both at macro level and micro level. Macro financedeals with the different sources of raising funds for agriculture as a
whole in the economyand it is also concern with the lending procedures, rules, regulations, monitoring and 12. 12controlling procedures of different agricultural institutions. Thus, macro finance pertainsto financial agriculture at the aggregate.Micro finance deals with financing the individual farm business units and it isconcern with the study as to
how the individual farmer considers various sources of creditto be borrowed from each source and how he allocates the same among the alternativeuses within the farm.Need for agricultural financeGiven the requirement of finance in agricultural sector, very few farmers will havecapital of their own to invest in agriculture. Therefore, a need arises to
provide credit toall those farmers who require it. Even if we look into the expenditure pattern of the farmfamilies, they have hardly any savings to fall back on. Therefore, credit enables thefarmers to advantageously use seeds, fertilizers, irrigation, machinery, etc. Farmer has toinvariably search for a source which supplies adequate farm credit. Above
all, small andmarginal farmers constitute majority of the farming community.Agricultural MarketingThe term, agricultural marketing implies selling of goods and services by the farmers andranchers. It includes various functions viz., assembling, transportation, storing, buying,selling, standardization, grading, processing, sales promotion,
etc.According to Thomsen, agricultural marketing comprises all the operations, andthe agencies conducting them involved in the movement of farm produced foods, rawmaterials and their derivatives, such as textiles, from the farms to the final consumer andeffects of such operations on farmers, middlemen and consumers.Importance of agricultural
marketingMarketing gives signals to increase production and thereby ensures the availability ofgoods, and services. If the marketing activity is developed, demand for goods increases asa result, production of goods also increases. Due to increased production, the demand forinputs increases i.e., demand for input is derived from the increase in
demand for theoutput. To distribute the required input to the farm sector, the input marketing has to bestrengthened.Lecture No.6Basic terms and concepts in economics Goods & Services free and economicgoods, Utility Cardinal and Ordinal approaches. Characteristics of utility - Formsof utility.BASIC TERMS AND CONCEPTS IN ECONOMICS 13.
13GOODS and SERVICESEconomics is concerned with the production and distribution of goods and services.Goods: It is defined as anything that satisfies human wants or needs.Characteristic features of goods:1. They are tangible in nature2. They are the material outcome of productionExample: Foodgrains, Machinery, Seeds, Fertilizers
etc.,Services would be the performance of any duties or work for another or professionalactivity. .Characteristic Features of Services:1. They are intangible2. Non- Materialistic3. Inseparable4. Variable5. PerishableExample: Services rendered by agricultural labourers, doctors, teachers etc.,Classification of GoodsThe goods are classified based on
supply, durability, consumption and transferability.1) Based on Supply: The goods are categorized as economic goods and free goods basedon the supply criteriaFree goods are those goods that exist in lenty that can be used as much as we like. Theyare gifts of nature and used without payment Example: Air, sunshine etc.The economic goods, on the
other hand, are scarce and can be had only on payment.They are limited and generally man- made and hence those can be available only onpayment. In Economics, we are concerned with economic goods only. Economic goodsmean wealth.Thus there would have been no science of economics if all goods had been free goods.The distinction between
free goods and economic goods, of course is not permanent, forinstance air is a free good but when we receive it under fan it is an economic good.2) Based on Consumption: The Goods are categorized as Consumer goods and ProducerGoods. 14. 14Consumer goods are those which yield, satisfaction directly. They are used by consumerdirectly to
satisfy the wants Example: food, clothing, etc. These goods are known as theGoods of First order.Producer goods are these goods which help us to produce other goods. They givesatisfaction indirectly by producing other goods which will yield final satisfaction.Example: machinery, tools etc. They are also termed goods of the second order..3) Based on
Durability: This classification emphasized on the nature of the goods andtheir usage.Mono Period Goods are those goods which can be used only once in the production andconsumption process. Example: Seeds, Fertilizers,food etc.,Poly Period Goods are those which can be used repeatedly during the production andconsumption process over several
periods. Example:refrigerator machinery, implementsetc.,4) Based on Transferability:External Material Transferable good. Example: Land, Buildings etc.,External material non-Transferable good. Example: Degree Certificate, PAN Card etc.,External non material transferable good. Example: Goodwill of a businessExternal non material Non-
transferable good. Example: Friendship,lightInternal non material Non-Transferable good. Example: Intelligence Quotient ,ability,cruelty etc., 15. 15CLASSIFICATION OF GOODSGOODSSUPPLY CONSUMPTION DURABILITY TRANSFERABILITYFree Economic Consumer Producer Mono Poly External InternalGoods Goods Goods Goods Period goods
Period goodsMaterial non materialTransferable Non- Transferable Non - transferable transferable goodsgoods goods goods 16. 16UTILITYThe basis of consumer behaviour is that people tend to choose those goodsand services they value high. Based on this premise economists developed the notion ofutility to describe the consumption patterns
adopted by the consumers.Definition : Utility means the power to satisfy a human want. Any commodity orservice which can satisfy a human want is said to have utilityCharacteristics of Utility :1. Utility is subjective: Utility varies from person to person, for Eg:- A high yieldingvariety seed gives more utility to the farmer. The same seed provided to a
clothmerchant gives zero utility.2. Utility varies with purpose : For Eg:- Coconut oil is used as coking oil or hair oil oras lubricant.3. Utility varies with time : The Intensity of a persons desire for a commodity isdifferent at various time periods, for Eg:- Labour requirement for paddy is peakduring transplantation harvesting and threshing period than
other operations takenup in paddy cultivation.4. Utility varies with ownership : Ownership of a good creates greater utility from agood than when it is hired Eg:- owning a tractors gives more utility than hiring it.5. Utility need not be synonymous with pleasure: For Eg:- A sick man has to consumemedicines for getting cured. He does not get pleasure
during the process.6. Utility does not mean satisfaction: utility is distinct from satisfaction. It impliespotentiality of satisfaction in a given commodity. But the satisfaction is the end resultof consumption. Satisfaction is what we get and the utility is the quality in agoodwhich gives satisfaction.KINDS OR TYPES OF UTILITYThe kinds or types of utilities
are 1) Form utility 2) Place utility 3) Time utility and4) Possession utility.1. Form Utility : The Change in the form offers greater utility to the good than in itsoriginal form. For example: Processing of paddy into rice. Rice, fetches superior pricethan paddy because of processing.2. Place Utility : The utility obtained by spatial movement of the goods is
termed asplace utility. Transportation aids in place utility i.e., through the transfer of goods fromsurplus production area to deficit or slack areas. Example: Shimla apples are transportedto all parts of the country thereby increasing the utility of apples. 17. 173. Time utility: Storing the commodity at the times of surplus production and makethem
available during scarcity creates time utility. Storage aids in creation of time utilityby the supply of seasonal products during off season as per the consumers requirements.4. Possession Utility: The Utility obtained due to possession or transfer of ownershipof the commodity is called possession utility. Buying and selling creates possessionutility. For
Eg:- Agriculture land sold to real estate for plots would increase the utility forthe same piece of land.Cardinal and Ordinal UtilityCardinal utility : This is based on the premise that utiIity could be measured and can beaggregated across individuals. It quantitatively measures the preference of an individualtowards a certain commodity. Numbers
assigned to different goods or services can becompared. A utility of 100 units towards a cup of coffee is twice as desirable as a cup oftea with a utility level of 50 units. The only limitation is its subjectivity.Ordinal utility: this is the ordinal measurement of utility. According to this utility can notbe quantified.For Example: If the utility is 100 units
towards a cup of coffee and 50 unitsfor a cup of tea, the conclusion drawn is that Coffee is preferred over tea. The ordering isimportant rather than the magnitude of the numerical values like 100 and 50 in the giveninstance. This approach faces the limitation of utilities not being compared. 18. 18Lecture No.7Value Definition Characteristics; Price
Meaning, Wealth Meaning Attributesof wealth, Types of wealth, Distinction between wealth and welfare.Value and wealthValueThe word Value in economics conveys value-in-exchange. It does not include freegoods which have only value-in-use. In other words, value of a commodity refers to thosegoods that can be obtained in exchange for itself or
purchasing power of a commodity interms of other commodities and services. Value can be referred to as the capacity of agood to command other things in exchange.Characteristics of Value.1. It must possess utility2. It must be scarce and3. It must be transferable and marketable.PriceIn Pre historic times, people did not know money and they had a
barter system in whichgoods are exchanged with goods. Therefore, in those days value and price were usedsynonymously. But now days, goods are exchanged for money. Therefore, Valueexpressed in monetary terms is PriceWealthIn ordinary language, Wealth conveys an idea of prosperity and abundance. A man ofwealth understood as a rich person.
But in Economics Wealth is synonymous witheconomic goods. In short, Wealth means anything which has value.Definition: It consists of all potentially exchangeable means of satisfying human wants(J.M.Keynes)Characteristics of wealth :1. It should possess utility2. It must be scarce3. It must be transferable4. It must be external to personRelation
between Money and Wealth : Money is a form of wealth .All money is wealthbut all wealth is not money 19. 19Relation between Income and Wealth : Income is different from wealth. Wealth yieldsincome. Therefore, Wealth is a fund whereas income is a flTypes of Wealth :1. Individual Wealth : It consists of all tangible and intangible possessions of
theindividuals besides loans due to them. Example: Land, bonds, deposits are tangiblepossessions while, intangible possessions are copyrights, patents etc.,2. Social Wealth : It is the wealth, which is collectively used by all the people in anation. Example: Railways, Public Parks, Government colleges etc.,3. Representative Wealth : It is that form of
wealth in the form of title deeds4. National Wealth : It is an aggregate of all individuals wealth and social wealth of thecountry inclusive of loans due to people and to the nation debts have to be deducted.Example: Rivers, mountains.5. Cosmopolitan Wealth: It is wealth of the whole word. It is a sum total wealth of allnationals.6. Negative Wealth : It
refers to the exclusive debts owed by the individuals and thenation.Wealth and Welfare comparedWealth WelfareIt is the means to an end It is the end itselfIt is objective It is subjectiveIt includes harmful goods It does not include harmful goodsIt does not include free goodsFree and economic goods lead to welfare 20. 20Lecture No.8Law of
Diminishing Marginal Utility statement, assumptions of law, explanation,limitations of the law, Importance.LAW OF DIMINISHING MARGINAL UTILITY (LDMU)The law of diminishing marginal utility is a generalization drawn from the characteristicsof human wants, H.H Gossen was the first to formulate this law in 1854.Marshall has stated the law of
diminishing marginal utility as follows The additionalbenefit which a person derives from a given increase of his stock of a thing diminisheswith every increase in the stock that he already has. In other words, the law simply statesthat other things being equal, the marginal utility derived from successive units of a givencommodity goes on decreasing.
Hence the more we have of a thing; the less we want ofit, because every successive unit gives less and less satisfaction.Marginal Utility: The addition to the total utility by the consumption of the last unitconsidered just worthwhile.Total utility : The sum total of utilities obtained by the consumer from consumption ofdifferent units of a
commodityASSUMPTIONS :1. There should be a single commodity with homogeneous units wanted by an individualconsumer2. There should not be any change in the taste, habit, custom, fashion and income ofthe consumer3. There should be continuity in the consumption of the commodity4. Units of the commodity should be of a suitable size5. Pries
of the different units of the commodity and of the substitutes of the commodityshould remain the same6. The commodity should be divisible7. The consumer should be an economic man who acts rationally8. Goods should be normal goods. 21. 21Schedule showing marginal utility and total utilityUnits of apples consumed Total utility in utils Marginal
utility in utils1 7 72 11 4 (11 - 7)3 13 2 (13 - 11)4 14 1 (14 - 13)5 14 0 (14 - 14)6 13 -1 (13 - 14)The above table shows that when a person consumes no apples, he gets no satisfaction.His total utility is zero. In case he consumes one apple, he gains seven units ofsatisfaction. His total utility is 7 and his marginal utility is also 7. In case he
consumessecond apple, he gains extra 4 utils (MU). Thus given him a total utility of 11 utils fromtwo apples. His marginal utility has gone down from 7 utils to 4 utils because he has aless craving for the second apple. Same is the case with the consumption of third apple.The marginal utility has now fallen to 2 utils while the total utility of three apples
hasincreased to 13 utils (7 + 4 + 2). In case the consumer takes fifth apple, his marginalutility falls to zero utils and if he consumes sixth apple also, the total utility startsdeclining and marginal utility becomes negative. Total utility and marginal utility fromthe successive utits of the commodity are plotted in the figure below:i. The total utility curves
starts at the origin as zero consumption of apples yieldzero utility.ii. The TU curve reaches at its maximum or a peak at M when MU is zero. 22. 22iii. The MU curve falls throughout the graph. A special point occurs when theconsumer consumes fifth apple. He gains no marginal utility from it. After thispoint, marginal utility becomes negative.MUa =
TUa TU(a-1)Importance of the Law:1. The law of diminishing marginal utility is the basic law of consumption. The law ofdemand, the law of equimarginal utility and the concept of consumers surplus arebased on it.2. The law helps in bringing variety in consumption and production.3. The law helps to explain the phenomenon in the value theory that
the price of acommodity falls when its supply increases. It is because with the increase in thestock of a commodity its marginal utility diminishes.4. The famous diamond water paradox of Smith can be explained with the help of thislaw. Diamonds are scarce and hence possess high marginal utility and hence higherprice. On the otherhand, water is
relatively abundant because of which it possess lowmarginal utility and low price even though its total utility is high5. The principle of progressive taxation is based on this law. As a person s incomeincreases, the rate of tax rises because the marginal utility of money to him falls withthe rise in his income. The law underlines the socialist plea for an
equitabledistribution of wealth.Exceptions to LDMU are as follows:1. Hobbies: In case of certain hobbies like stamp collection or old coins, everyadditional unit gives more pleasure. MU goes on increasing with the acquisition ofevery unit.2. Drunkards: It is believed that every dose of liquor Increases the utility of a drunkard.3. Miser: In the case of
miser, greed increases with the acquisition of every additionalunit of money.4. Reading: The habit of reading of more books gives more knowledge and in turngreater satisfactions. 23. 23Lecture No.9Law of Equi-marginal Utility Meaning, Assumptions, Explanation of the Law,Practical Importance, Limitations.LAW OF EQUI MARGINAL UTILITYThe
principle of equal marginal utility occupies an important place in the cardinal utilityanalysis. According to this, a consumer is in equilibrium when he distributes his givenmoney income among various goods in such a way that marginal utility derived from thelast rupee spent on each good is the same. The Marshallian approach to
consumersequilibrium is based on the following assumptions.AssumptionsThe main assumptions of the law of equi-marginal utility are as under:(1) Independent utilities. The marginal utilities of different commodities are independentof each other and diminishes with more and more purchases.(2) Constant marginal utility of money. The marginal
utility of money remains constantto the consumer as he spends more and more of it on the purchases of goods.(3) Utility is cardinally measurable.(4) Every consumer is rational in the purchase of goods.(5) Limited money income. A consumer has limited amount of money income to spend.Definition and explanation of the law:The law of equi-marginal
utility is simply an extension of the law of diminishingmarginal utility to two or more than two commodities. The law of equi-marginal, isknown, by various names. It is named as the Law of Substitution, the Law of MaximumSatisfaction, the Law of Indifference, the Proportionate Rule and the Gossens SecondLaw. In cardinal utility analysis, this law is
stated by Lipsey in the following words. Thehousehold maximizing the utility will so allocate the expenditure between commoditiesthat the utiliIity of the last penny spent on each item is equal. As we know, everyconsumer has unlimited wants. However, the income at his disposal at any time islimited. The consumer is therefore, faced with a choice
among many commodities that hecan and would like to pay. He therefore, consciously or unconsciously compares thesatisfaction which he obtains from the purchase of the commodity and the price which hepays for it. If he thinks the utility of the commodity is greater than the utility of money,he buys that commodity. As he buys more and more of
that commodity, the utility of thesuccessive units begins to diminish. He stops further purchase of the commodity at apoint where the marginal utility of the commodity and its price are just equal. If he 24. 24pushes the purchase further from his point of equilibrium, then the marginal utility of thecommodity will be less than that of price and the
household will be a loser. A consumerwill be in equilibrium with a single commodity symbolically when:Consumers equilibrium with two or more than two goods purchased. A prudentconsumer in order to get the maximum satisfaction from his limited means compares notonly the utility of a particular commodity and the price but also the utility of the
othercommodities which he can buy with his scarce resources. If he finds that a particularexpenditure in one use is yielding less utility than that of other, he will try to transfer aunit of expenditure from the commodity yielding less marginal utility to commodityyielding higher marginal utility. The consumer will reach his equilibrium position when
itwill not be possible for him to increase the total utility by transferring expenditure fromless advantageous uses to more advantageous uses.The consumer will maximize total utility from his given income when the utility fromthe last rupee spent on each good is the same. Algebrically, this iswhen; Here (a), (b), (c), n are large numbergoods

consumed.It may here be noted that when a consumer is in equilibrium there is no way to increaseutility by reallocating his given money income.The doctrine of equi-marginal utility can be explained by taking an example. Suppose aperson has Rs.5 with him which he wishes to spend on two commodities, Pencil andErasers. The marginal utility
derived from both these commodities is as under:Units of Money MU of Pencils MU of Erasers1 10 122 8 103 6 84 4 65 2 3Rs.5 Total Utility = 30 Total Utility = 39A rational consumer would like to get maximum satisfaction from Rs. 5.00. He canspend this money in three ways. 25. 25(1) Rs. 5.00 may be spent on Pencils only(2) Rs. 5.00 may be
utilized for the purchase of Erasers only.(3) Some rupees may be spent on the purchase of Pencils and some on the purchase ofErasers.If the prudent consumer spends Rs. 5.00 on the purchase of Pencils, he gets 30 utility. Ifhe spends Rs. 5.00 on the purchase of Erasers, the total utility derived is 39 which ishigher than Pencils. In order to make the
best of the limited resources, he adjusts hisexpenditure.(1) By spending Rs. 4.00 on Pencils and Rs. 1.00 on Erasers, he gets 40 utility(10+8+6+4+12=40).(2) By spending Rs. 3.00 on Pencils and Rs. 2.00 on Erasers, he derives 46 Utility(10+8+6+12+10=46).(3) By spending Rs. 2.00 on Pencils and RPs. 3.00 on Erasers, he gets 48
utility(10+8+12+10+8=48).(4) By spending Rs. 1.00 on Pencils and Rs. 4.00 on Erasers, he gets 46 utility(10+12+10+8+6=46).The sensible consumer will spend Rs. 2.00 on Pencils and Rs. 3.00 on Erasers and willget the maximum satisfaction. When he spends Rs. 2.00 on Pencils and Rs. 3.00 onErasers, the marginal utility derived from both these
commodities is equal to 8. When themarginal utilities of the two commodities are equalized, the total utility is then maximumi.e., 48 as is clear from the schedule given above.The law of equi-marginal utility can be explained with the help the diagrams.In the diagram, MU is the marginal utility curve for Pencils and KL of Erasers. When aconsumer
spends OP amount (Rs.2) on Pencils and OC (Rs.3) on Erasers, the marginalutility derived from the consumption of both the items (Pencils and Erasers) is equal to 8PENCILS ERASERS 26. 26units (EP=NC). The consumer gets the maximum utility when he spends Rs. 2.00 onPencils and Rs. 3.00 on Erasers and by no other alteration in the
expenditure.We now assume that the consumer spends Rs. 1.00 on Pencils (OC amount) and Rs.4.00 (OQ) on erasers. If CQ more amount is spent on erasers, the added utility is equalto the area CQ NN. On the other hand, the expenditure on Pencils falls from OP amount(Rs.2) to OC amount (Rs. 1.00). There is a loss of utility equal to the area CPEE.
Theloss in utility (Pencils) is greater than that of its gain in erasers. The consumer is notderiving maximum satisfaction except the combination of expenditure of Rs. 2.00 onPencils and Rs. 3.00 on erasers.This law is known as the Law of Maximum Satisfaction because a consumer tries to getthe maximum satisfaction from his limited resources by so
planning his expenditure thatthe marginal utility of a rupee spent in one use is the same as the marginal utility of arupee spent on another use. It is known as the Law of Substitution because consumercontinues substituting one good for another till he gets the maximum satisfaction. It iscalled the Law of Indifference because the maximum satisfaction
has been achieved byequating the marginal utility in all the uses. The consumer then becomes indifferent toread just his expenditure unless some change fakes place in his income or the prices ofthe commodities, etc.Limitations of the Law(i) Effect of fashions and customs. The law of equi-marginal utility may becomeinoperative if people forced by
fashions and customs spend money on the purchase ofthose commodities which they clearly know yield less utility but they cannot transfer theunit of money from the less advantageous uses to the more advantageous uses becausethey are forced by the customs of the country.(ii) Ignorance or Carelessness. Sometimes people due to their ignorance of
price orcarelessness to weigh the utility of the purchased commodity do not obtain the maximumadvantage by equating the marginal utility in all the uses.(iii) Indivisible Units. If the unit of expenditure is not divisible, then again the law maybecome inoperative.(iv) Freedom to Choose. If there is no perfect freedom between various alternatives,
theoperation of law may be impeded;Practical Importance of Law of LEMU:1. Consumption: A wise consumer acts on this law while arranging his expenditure andobtains maximum satisfaction.2. Production: To obtain maximum net profit, he must substitute one factor of producingto another so as to have most economical combination. 27. 273.
Exchange: Exchange implies substitution of one thing to another and hence this law isimportant.4. Distribution: It is on the principle of the marginal productivity that the share of eachfactor of production is determined.5. Public finance: The Government is also guided by this law in public expenditure byallocation of revenue (money) in such a way that
it will secure maximum welfare ofthe people.Lecture No.10Consumers Surplus Meaning, Assumptions, Explanation, Difficulties inmeasuring Consumers Surplus, Importance.CONSUMERS SURPLUSImportance:The concept of consumers surplus is based on the theory of demand. It wasintroduced by marshal in 1895 in his publication principles of
economics.According to marshal consumers surplus is the excess of the price which hewould be willing to pay rather than go without the thing, over that which he actually doespay, is the economic measure of this surplus satisfaction. In brief, consumers surplus isthe difference between what the consumer is willing to pay and what he actually
pays.Assumptions:1. Marginal utility of money for the consumer is assumed to be the same through out theprocess of exchange.2. Commodity does not have substitutes3. In the market at the given point of time, there are no differences of income, tastes,preferences and fashions among the consumers and4. Each commodity is considered independent
of others.Explanation:To illustrate let us suppose that a consumer is willing to buy jamun if it price wereRs.1/-, 2 jamun if the price were 75 paise. 3 jamun at 50 paise and 4 at 25 paise. Supposethe market price is 25 paise per jamun. At this price the consumer will buy 4 jamun andenjoy a surplus of Rs.1.50 (0.75 +0. 50 + 0.25). This is shown in
table.Units of Marginal Utility Actual Price ConsumerJamun (Price willing to pay) Surplus1 1.00 0.25 0.752. 0.75 0.25 0.503. 0.50 0.25 0.254. 0.25 0.25 -- 28. 28Our hypothetical consumer is prepared to pay Rs.2.50/-(Rs.1.00 + 0.75 + 0.50 + 0.25) forfour jamuns but actually pays Rs.1/- and therefore derives a surplus of Rs.1.50/-(Rs.2.50/- - Rs.1.00/-).
It can also be expressed asCS = Total utility Marginal UtilityCS = TU (Price x NO. Of units of the commodity)Consumers surplus is represented diagrammaticallyPrice per units is OQ. At this price, the consumer will demand OQ quantity ofcommodity, he will get total satisfaction equal to the area OQRA, and thus gets a surplussatisfaction equal to PRA
(OQRA OQRP). Thus surplus satisfaction has been definedas consumers surplus.Difficulties in measuring Consumers Surplus:1. The cardinal measurement of utility is difficult because it is close to impossible for aconsumer to say that the first unit of commodity gave him 10 units of satisfaction and thesecond unit of commodity gave him 5 units of
satisfaction.2. Marginal utility for the same commodity id different to different consumers. Marginalutility for a particular commodity varies from person to person depending upon theirincome, tastes and preferences.3. Existences of substitutes: In the real world a number of substitutes for a commodityexist, thus making the work of measuring
consumers surplus a complicated task.4. Marginal utility of money is not constant: Marshall based his concept of consumerssurplus on the simplifying assumption that the marginal utility of money is constant. Asthe consumer buys more and more units of a commodity x, the amount of money withhim diminished, in this case, the marginal utility of
money is bound to increases ratherthan remain constant.5. Lack of awareness of different price: It is not possible for a consumer to be aware ofthe entire demand schedule.Importance of Consumers SurplusAJamun (Rs)RPO 29. 291. Conjunctural Importance : When the people enjoy larger consumers surplus, it doesnot indicate that they are better off.
Thus it serves as an index of economic betterment.2. Useful to the Monopolist : The monopolist can freely raise the process of the goods ifthey bring in higher consumers surplus, without any fear of foregoing the sales.3. Helps in Public Finance and Taxation : More taxes can be impose by the governmentto get more revenue, on those goods for which
consumers surplus is high4. Helps to measure benefits from International Trade: International trade impliestransaction of commodities across the frontiers. Generally, those commodities whichhappen to be cheaper in the foreign markets are imported thereby resulting in higherconsumers surplus of satisfaction for the commodity. 30. 30Lecture
No.11&12Demand Meaning, Definition, Types of demand - income demand, price demand,cross demand- Demand Schedule, demand curve, Law of demand contraction andextension, increase and decrease in demandDEMANDMeaning of DemandDemand in economics means a desire to possess a good supported by willingness andability to pay for it.
If you have a desire to buy a certain commodity, say, a tractor, but donot have the adequate means to pay for it, it will simply be a wish, a desire or a want andnot demand. Demand is an effective desire, i.e., a desire which is backed by willingnessand ability to pay for a commodity in order to obtain it. In the words, "Demand means thevarious
quantities of a good that would be purchased per unit of time at different prices ina given market. There are thus three main characteristics of demand in economics.i. Willingness and ability to pay. Demand is the amount of a commodity for which aconsumer has the willingness and also the ability to buy.ii. Demand is always at a price. If we talk of
demand without reference to price, it will bemeaningless. The consumer must know both the price and the commodity. He will thenbe able to tell the quantity demanded by him.iii. Demand is always per unit of time. The time may be a day, a week, a month, or a year.Individual's Demand for a commodity:The individuals demand for a commodity is the
amount of a commodity which theconsumer is willing to purchase at any given price over a specified period of time. Theindividual's demand for a commodity varies inversely with price ceteris paribus. As theprice of a good rises, other things remaining the same, the quantity demanded decreasesand as the price falls, the quantity demanded increases.
Price (p) is here an independentvariable ad quantity (q) dependent variable.The Market Demand for a Commodity:The market demand for a commodity is obtained by adding up the total quantitydemanded at various prices by all the individuals over a specified period of time in themarket. It is described as the horizontal summation of the individuals
demand for acommodity at various possible prices in market.In a market, there are a number of buyers for a commodity at each price. In orderto avoid a lengthy addition process, we assume here that there are only four buyers for acommodity who purchase different amounts of the commodity at each price. The 31. 31horizontal summation of
individuals demand for a commodity will be the marketdemand for a commodity as is illustrated in the following schedule:Demand ScheduleDemand schedule is a tabular representation of the quantity demanded of a commodity atvarious prices. For instance, there are four buyers of apples in the market, namely A, B, Cand D.Demand schedule for
applesPRICE (Rs.per dozen)Buyer A(demand indozen)Buyer B(demand indozen)Buyer C(demand indozen)Buyer D(demand indozen)MarketDemand(dozens)10 1 0 3 0 49 3 1 6 4 148 7 2 9 7 257 11 4 12 10 376 13 6 14 12 45The demand by buyers A, B, C and D are individual demands. Total demand by the fourbuyers is market demand. Therefore, the
total market demand is derived by summing upthe quantity demanded of a commodity by all buyers at each price.Demand CurveDemand curve is a diagrammatic representation of demand schedule. It is a graphicalrepresentation of price- quantity relationship. Individual demand curve shows the highestprice which an individual is willing to pay for
different quantities of the commodity.While, each point on the market demand curve depicts the maximum quantity of thecommodity which all consumers taken together would be willing to buy at each level ofprice, under given demand conditions.1) Derived demand.Derived demand refers to demand for goods which are needed for further
production. It isthe demand for producers goods like industrial raw material, machine tools andequipments.2) Autonomous demandAutonomous demand is independent of the other product or main product. Its not linkedor tie-up with the other goods or commodity.eg: food articles,clothes. 32. 32Price Demand:It refers to various quantities of a good or
service that a consumer wouldbe willing to purchase at all possible prices in a given market at a given point in time,ceteris paribus.Income Demand:It refers to various quantities of a good or service that a consumer wouldbe willing to purchase at different levels of income, ceteris paribus.Cross Demand : It refers to various quantities of a good or
service that a consumer wouldbe willing to purchase not due to changes in the price of the commodity underconsideration but due to changes in the price of related commodity. For example:Demand for tea is more not because price of tea has fallen but because price of coffee hasrisen. Thus demand for substitutes take the form of cross demand.Law
of Demand1. The law of demand states that as price increases (decreases) consumers will purchaseless (more) of the specific commodity. Demand varies inversely with price.As price falls from P1 to P2 the quantity demanded increases from Q1 to Q2. This is anegative relation between price and quantity, hence the negative slope of the
demandschedule; as predicted by the law of demand.Demand curve has a negative slope, i.e, it slopes downwards from left to right depictingthat with increase in price, quantity demanded falls and vice versa. The reasons for adownward sloping demand curve can be explained as follows-1. Income effect- With the fall in price of a commodity, the
purchasing power ofconsumer increases. Thus, he can buy same quantity of commodity with less money or hecan purchase greater quantities of same commodity with same money. Similarly, if theprice of a commodity rises, it is equivalent to decrease in income of the consumer as nowhe has to spend more for buying the same quantity as before. This
change in purchasingpower due to price change is known as income effect. 33. 332. Substitution effect- When price of a commodity falls, it becomes relatively cheapercompared to other commodities whose prices have not changed. Thus, the consumer tendto consume more of the commodity whose price has fallen ,i.e, they tend to substitute
thatcommodity for other commodities which have now become relatively dear.3. Law of diminishing marginal utility It is the basic cause of the law of demand. Thelaw of diminishing marginal utility states that as an individual consumes more and moreunits of a commodity, the utility derived from it goes on decreasing. So as to getmaximum
satisfaction, an individual purchases in such a manner that the marginal utilityof the commodity is equal to the price of the commodity. When the price of commodityfalls, a rational consumer purchases more so as to equate the marginal utility and theprice level. Thus, if a consumer wants to purchase larger quantities, then the price mustbe lowered.
This is what the law of demand also states.Changes in demand for a commodity can be shown through the demand curve in twoways: (1) Movement along the demand curve(Extension and contraction) and (2) Shiftsof the demand curve(Increase and decrease).(1) Movement along the Demand Curve:Demand is a multivariable function. If income and
other determinants of demand such astastes of the consumers, changes in prices of related goods, income distribution etcremain constant and there is a change only in price of the commodity, then we movealong the same demand curve, In this case, the demand curve remains unchanged. When,as a result of change in price, the quantity demanded
increases or decreases, it istechnically called extension and contraction in demand.A movement along a demand curve is defined as a change in the quantity demanded dueto changes in the price of a good will result in a movement along the demand curve. Forinstance, a fall in the price of apples from P1 to P2 causes an increase in the
quantitydemanded from Q1 to Q2Shifts in the demand curveA shift of the demand curve is referred to as a change in demand due any factor otherthan price. A demand curve will shift if any of these occurs:1. Change in the price of other goods (complements and substitutes); leading to increase/ decrease of real income 34. 342. Change in the income
level3. Change in consumers tastes and preferencesEach of these factors tends the demand curve to shift downwards to the left or upwards tothe right. While downward shift signifies decrease in demand, an upward shift of thedemand curve shows an increase in the demand.As shown in the figure the demand curve will shift to D2 from D1 and
accordingly theprice and quantity demanded will change.Movements along a demand curve is the result of increase or decrease of the price of the good,while the demand curve shifts when any demand determinant other than price changesDeterminants of demandVarious factors affect the quantity demanded by a consumer of a good orservice. The
key determinants of demand are as follows1. Price of the good: This is the most important determinant of demand. The relationshipbetween price of the good and quantity demanded is generally inverse as we will see laterwhile studying law of demand2. Price of related goods: Substitutes: If the price of a substitute goes down than the quantity
demanded of thegood also goes down and vice versa. Complementary goods: If the price of gasoline goes up the quantity demanded ofautomobiles will go down. Thus the price of complements have an inverserelationship with the demand of a good3. Income: Higher the income of the consumer the more will be quantity demanded ofthe good. The only
exception to this will be inferior goods whose demand decreaseswith an increase in income level 35. 354. Individual tastes and preferences: a preference for a particular good may affect theconsumers choice and he / she may continue to demand the same even in risingprices scenario5. Expectations about future prices & income: If the consumer
expects prices to rise infuture he / she may continue to demand higher quantities even in a rising pricescenario and vice versaExceptions to the law of demandUnlike other laws, law of demand also has few exceptions i.e. there is no inverserelationship between price and quantity demanded for these goods. Few of them are asfollows:1. Giffen goods:
These are those inferior goods whose quantity demanded decreaseswith decrease in price of the good. This can be explained using the concept of incomeeffect and substitution effect2. Commodities which are regarded as status symbols: Expensive commodities likejewellery, AC cars, etc., are used to define status and to display ones wealth.
Thesegoods doesnt follow the law of demand and quantity demanded increases with pricerise as more expensive these goods become, more will be their worth as a statussymbol.3. Expectation of change in the price of the goods in future: if a consumer expects theprice of a good to increase in future, it may start accumulating greater amount of
thegoods for future consumption even at the presently increased price. The same holdstrue vice versa 36. 36Lecture No.13&14Elasticity of demand Meaning, elastic and inelastic demand, kinds of elasticity ofdemand, perfectly elastic, perfectly inelastic, relatively elastic, relatively inelastic,unitary elastic demand-types of elasticity of demand-price
elasticity of demand-income elasticity-cross elasticity of demand-factors affecting elasticity of demand-practical importance of elasticity of demandEEllaassttiicciittyy ooff DDeemmaanndd::TThhee eellaassttiicciittyy ooff ddeemmaanndd mmeeaassuurreess tthhee rreessppoonnssiivveenneessss ooff qquuaannttiittyy ddeemmaannddeedd ttoo aa
cchhaannggeeiinn aannyy oonnee ooff tthhee aabboovvee ffaaccttoorrss bbyy kkeeeeppiinngg ootthheerr ffaaccttoorrss ccoonnssttaanntt.. WWhheenn tthhee rreellaattiivveerreessppoonnssiivveenneessss oorr sseennssiittiivveenneessss ooff tthhee qquuaannttiittyy ddeemmaannddeedd iiss mmeeaassuurreedd ttoo cchhaannggeess iinn
iittsspprriiccee,, tthhee eellaassttiicciittyy iiss ssaaiidd bbee pprriiccee eellaassttiicciittyy ooff ddeemmaanndd..Types of Elasticity of DemandThe quantity of a commodity demanded per unit of time depends upon various factorssuch as the price of a commodity, the money income of the consumer and prices ofrelated goods, the tastes of the people,
etc. Whenever there is a change in any of thevariables stated above, it brings about a change in the quantity of the commoditypurchased over a specified period of time. The three main types of elasticity are nowdiscussed in brief.(1) Price Elasticity of Demand:The concept of price elasticity of demand is commonly used in economic literature.
Priceelasticity of demand is the degree of responsiveness of quantity demanded of a good to achange in its price. Precisely, it is defined as the ratio of proportionate change in thequantity demanded of a good caused by a given proportionate change in price. Theformula for measuring price elasticity of demand is:Price Elasticity = Percentage change
in quantity demandedPercentage change change in price= q / q P / PExample. Let us suppose that price of a good falls from Rs.10 per unit to Rs.9 per unit ina day. The decline in price causes the quantity of the good demanded to increase from125 units to 150 units per day, The price elasticity using the simplified formula will be:Ep = q / P x P / qq =
150 - 125 = 25 P = 10 - 9 = 1Original quantity = 125 Original price = 10Ep = 25 / 1 x 10 / 125 = 2. The elasticity coefficient is greater than one.Therefore the demand for the good is elastic. 37. 37(2) Income Elasticity of Demand:Income is an important variable affecting the demand for a good. When there is a changein the level of income of a
consumer, there is a change in the quantity demanded of agood, other factors remaining the same. The degree of change or responsiveness ofquantity demanded of a good to a change in the income of a consumer is called incomeelasticity of demand. Income elasticity of demand can be defined as the ratio ofpercentage change in the quantity of a good
purchased, per unit of time to a percentagechange in the income of a consumer.Ey = Percentage change in demandPercentage change in incomeEy = q / y x y / qLet us assume that the income of a person is Rs.4000 per month and he purchases sixCDs per month. Let us assume that the monthly income of the consumer increases toRs.6000 and the
quantity demanded of CD's per month rises to eight .The elasticity ofdemand for CDs will be calculated as under:q = 8 - 6 = 2 y = 6000 - 4000 = 2000Original quantity demanded = 6 Original income 4000Ey = q / y x y / q = 2 / 200 x 4000 / 6 = 0.66The income elasticity is 0.66 which is less than one.(3) Cross Elasticity of Demand:The concept of cross
elasticity of demand is used for measuring the responsiveness ofquantity demanded of a good to changes in the price of related goods. Cross elasticity ofdemand is defined as the percentage change in the demand of one good as a result of thepercentage change in the price of another good.. The formula for measuring crosselasticity of demand is:Exy
= % change quantity demanded of good X% change in price of good YThe numerical value of cross elasticity depends on whether the two goods in question aresubstitutes, complements or unrelated.For example: Coke and Pepsi 38. 38DDeeggrreeeess ooff PPrriiccee EEllaassttiicciittyy ooff DDeemmaanndd::The economists grouped various degrees of
elasticity of demand into five categories. (1)Infinitely elastic, (2) Perfectly inelastic, (3) Unit elasticity, (4) Relatively elastic, and (5)Relatively inelastic demand.(1) Perfectly inelastic demand: When the quantity demanded of a good does not changeat all to whatever change in price, the demand is said to be perfectly inelastic or theelasticity of demand
is zero.(2) Perfectly elastic demand: A perfectly elastic demand curve DD/is a horizontal linewhich indicates that the quantity demanded is extremely (infinitely) responsive to price.Even a slight rise in price drops the quantity demanded of a good to zero. The curve DD/is infinitely elastic. This elasticity of demand as such is equal to infinity.(3) Unitary
elastic demand: When the quantity demanded of a good changes by exactlythe same percentage as price, the demand is said to be unitary elastic.(4) Relatively elastic demand: If a given proportionate change in price causes relativelya greater proportionate change in quantity demanded of a good, the demand is said to berelatively elastic.
Alternatively, we can say that the elasticity of demand is greater than I. 39. 39(5) Relatively Inelastic demand: When a given proportionate change in price causes arelatively less proportionate change in quantity demand, demand is said to be inelastic.The elasticity of a good here is less than I or less than unity.Factors Determining Price Elasticity of
Demand:(i) Degree of necessity: If the consumption of the commodity or commodities is essentialand necessary, the demand for those commodities is said to be relatively inelastic. Indeveloping countries of the world, the per capital income of the people is generally low.They spend a greater amount of their income on the purchase of necessaries of
life suchas wheat, milk, course cloth etc. They have to purchase these commodities whatever betheir price. The demand for goods of necessities is, therefore, less elastic or inelastic. Thedemand for luxury goods, on the other hand is greatly elastic whose consumption can bepostponed. For example, refrigerators, televisions etc(ii) Availability of
substitutes. If a good has greater number of close substitutes availablein the market, the demand for the good will be greatly elastic. For examples, if the price 40. 40of Coca Cola rises in the market, people will switch over to the consumption of PepsiCola. which is its close cheaper substitute. So the demand for Coca Cola is elastic.(iii) Proportion of
the income spent on the good: If the proportion of income spent onthe purchase of a good is very small, the demand for such a good will be inelastic. Forexample, if the price of a box of matches or salt rises by 50%, it will not affect theconsumers demand for these goods. The demand for salt, match box therefore will beinelastic. On the other hand, if
the price of a car rises from Rs.6 lakh to Rs.9 lakh and ittakes a greater portion of the income of the consumers, its demand would fall. Thedemand for car is, therefore, elastic.(iv) Time. The period of time plays an important role in shaping the demand curve. In theshort run, when the consumption of a good cannot be postponed, its demand will be
lesselastic. In the long run if the rise price persists, people will find out methods to reduce theconsumption of goods. For example: if the price of electricity goes up, it is very difficultto cut back its consumption in the short run than in the long run by adoption of availablealternatives.(v) Number of uses of a good. If a good can be put to a number of
uses, its demand ismore elastic (Ep > 1). For example, if the price of coal falls, its quantity demanded willrise considerably because demand will be coming from households, industries, railwaysetc.Practical Importance of Elasticity of Demand:1. Importance in taxation policy: The concept has immense importance in the sphere ofgovernment finance.
When a finance minister levies a tax on a certain commodity, he hasto see whether the demand for that commodity is elastic or inelastic. If the demand isinelastic, he can increase the tax and thus can collect larger revenue.2. Price discrimination by monopolist: If the monopolist finds that the demand for hiscommodities is inelastic, he will at once fix
the price at a higher level in order tomaximize his net profit. In case of elastic demand, he will lower the price in order toincrease, his sales and derive the maximum net profit.3. Importance to businessmen: When the demand of a good is elastic, they increases saleby lowering its price. In case the demand is inelastic, they charge higher price for
acommodity.4. Help to trade unions. The trade unions can raise the wages of the labor in an industrywhere the demand of the product is relatively inelastic. On the other hand, if the demand,for product is relatively elastic, the trade unions cannot press for higher wages.5. Use in international trade: The terms of trade between two countries are based
on theelasticity of demand of the traded goods.6. Determination of rate of foreign exchange: The rate of foreign exchange is alsoconsidered on the elasticity of imports and exports of a country.7. Guideline to the producers: The concept of elasticity provides a guideline to theproducers for the amount to be spent on advertisement. If the demand for a
commodity is 41. 41elastic, the producers shall have to spend large sums of money on advertisements forincreasing the sales.8. Use in factor pricing: The factors of production which have inelastic demand canobtain a higher price in the market then those which have elastic demand. This conceptexplains the reason of variation in factor pricing. 42.
42Lecture No.15Supply meaning, definition, law of supply, supply schedule, supply curveSUPPLYMeaning of supplyIt is the amount of a commodity that sellers are able and willing to offer for sale atdifferent prices per unit of time. In the words of Meyer Supply is a schedule of theamount of a good that would be offered for sale at all possible prices at
any period oftime; e.g., a day, a week, and so on.Difference/Distinction between Supply and Stock:Supply refers to that quantity of the commodity which is actually brought into the marketfor sale at a given price per unit of time. While Stock is meant the total quantity of acommodity this exists in a market and can be offered for sale at a short notice.
The supplyand stock of a commodity in the market may or may not be equal if the commodity isperishable, like vegetables, fruits, fish, etc; then the supply and stock are generally thesame. But in case if a producer finds that the price of his product is low as compared toits cost of production, he tries to withhold the entire or a part of a stock. In case
of afavorable price, the producer may dispose off large quantities or the entire stock of hiscommodity; it will all depend upon his own valuation of the commodity at that particulartime.Market supplyConsider the supply schedule below:Price Quantity supplied by Market SupplyRs A B C A+B+C10 40 60 80 1808 30 45 60 1356 22 33 44 994 15 23 30
682 10 15 20 45We can see in the above table, the supply schedule of three producers A, B and C forvarious price levels. As seen in the table above the supply of goods decreases as the priceof the goods fall. Now consider that the market consists of only these three suppliers, sothe market supply will be the sum of the goods supplied at various price
levels all otherthings remaining same. The same is depicted using the charts below. The first three charts 43. 43show the individual supply curve of A, B and C as per the supply schedule above, whilethe chart below that depicts the market supply curve i.e. the aggregate supply of A, B andCLaw of SupplyThe law of supply states that the quantity of a
good offered or willing to offer by theproducer/owners for sale increase with the increase in the market price of the good andfalls if the market price decreases, all other things remaining unchangedAn increase in price will increase the incentive to supply which means that supply curveswill slope upwards from left to right. Supply curves can be
curves or straight lines.Consider the supply of labour as in the figure below: 44. 44The above supply curve shows the hours per week at job by the labour on the X axis andhourly wages on the Y axis. As we can see that as the hourly wages increase the hoursspent on job also increases. Thus the supply curve is a left to right upward sloping
curveDeterminants of supplyQuantity supplied of a good/ service is affected by various factors. Several key factorsaffecting supply are discussed as below: Price of the product: Since the producer always aims for maximising hisreturns/profit, so the quantity supplied changes with increase or decrease in the price ofthe good. Technological changes:
Advanced technology can yield more quantity and at lessercosts. This may result in the producer to be willing to supply more quantity of the goods Resource supplies and production costs: Changes in production costs like wage costs,raw material cost and energy costs might impact the producers production andeventually the supply. An increase in
such cost might result in lesser quantities producedand thus lesser quantities supplied and vice versa Tax or subsidy: Since the producer aims to minimise costs and expand profit, anincrease in tax will increase the total cost, thereby decreasing the supply. Similarly asubsidy might incentivize the producer to supply more of that goods in order to
maximisehis profits. Tax and subsidy are two important tools used by central government tocontrol supplies of certain goods. For example an increase in tax can be used to reducethe supply of cigarettes, while increase in subsidy can be used to increase the supply offertilizers Expectations of prices in future: An expectation that the prices of goods
will fall infuture might lead to lessen the production by the producer and thereby decrease thesupply and vice-versa. 45. 45 Price of other goods: A producer might have several options to produce. Since themoney to invest is limited with the producer he would decide to produce the good whichoffers him the maximum profit. Thus if the producer is
currently producing good A andthe price of good B increases than he might switch to producing good B as this wouldresult in better returns for him. Number of producers in the market: This is a very important factor or determinant ofsupply. If there are large number of producers or sellers in the market willing to sellgoods then the supply of good
will increase and vice versaSupply functionSupply function expresses the relationship between supply and the factors (thedeterminants of supply, as discussed above) affecting the producer/supplier to offer goodsfor sale.For instance take the supply function as belowQs = f(P, Prg, S)where;P = price;Prg = price of related goods; andS = number of
producers.The supply curve is the graphical representation of the supply function and itshows the quantity of a good that the seller is offering or willing to offer at various prices 46. 46Lecture No.16Increase and decrease in supply, contraction and extension of supply, factorsaffecting supply.Movement along the Supply curve (Extension and
contraction)Movement along the supply curve happens due to change in the price of the good andresulting change in the quantity supplied at that price.For instance, an increase in the price of the good from P1 to P2 in the figure below resultsin an increase of quantity supplied of the good from Q1 to Q2. This movement from pointA to point B on the
supply curve S due to change in price of the good all other factors ofsupply remaining unchanged is called movement along the supplycurve.Shifts in the Supply curveShift in the supply curve is also sometimes referred as a change in supply. This happensdue to changes in factors of supply other than that of price of the goodFor example, if the price of
a factor or of a related good increases the supply curve shifts.Similarly changes in technology and government tools like tax and subsidy tends to shiftsupply curve. 47. 47The supply curve can shift to the right or left as shown in the figure. A shift towards theright i.e. from S1 to S2 curve denotes an increase in supply of the good. Similarly a shiftin the
supply curve from S1 to S3 denotes a decrease in supply of the good.As seen in the figure above a rightward shift in the supply curve from S1 to S2 increasessupply from Q1 to Q2 while the price of the good remains same at P1. Similarly aleftward shift from S1 to S3 decreases supply from Q1 to Q3 whilst the price remaininguunchanged at P1Factors
affecting changes in supply:The factors causing Shifts in supply curve arei.Changes in Factor Prices: If the prices of the various factors of production fall down, itwill result in lowering the cost of production and so an increase in the supply on varyingprices.i. Changes in Technique: If an improvement in technique takes place in a particularindustry, it
will help in reducing its cost of production. This will result in greaterproduction and so an increase in the supply of the commodity. The supply curve willshifts to the right of the original supply curve.ii. Improvement in the Means of Transport: The supply of the commodity may alsoincrease due to improvement in the means of communication and
transport. If the meansof transport are cheap and fast, then supply of the commodity can be increased at a shortnotice at lower price.iii. Climatic Changes in case of Agricultural Products: The supply of agriculturalproducts is directly affected by the weather conditions and the use of the better methodsof production. If rain is timely, plentiful, well-
distributed and improved methods ofcultivation are employed then other things remaining the same, there will be bumpercrop. It would then be possible to increase the supply of the agricultural products.iv. Political Changes: The increase or decrease in supply may also take place due topolitical disturbances in a country. If country wages wars
against another country or somekind of political disturbances take place just as we had at the time of partition, then thechannels of production are disorganized. It results in the decrease of certain goods thesupply curve shifts to the left of originals curve.v. Taxation Policy: If a government levies heavy taxes on the import of particularcommodities,
then the supply of these commodities is reduced at each price. The supplycurve shifts to the left, conversely, if the taxes on output in the country are low andgovernment encourages the import of foreign commodities, then the supply can beincreased easily. The supply curve shifts to the right of original supply curve.vi. Goals of firms. If the firms
expect higher profits in the future, they will take the riskand produce goods on large scale resulting in larger supply of the commodities. Thesupply curve shifts to the right. 48. 48Lecture No.17Elasticity of supply, kinds of elasticity of supply perfectly elastic, perfectlyinelastic, relatively elastic, relatively inelastic and unitary elastic - factors
affectingelasticity of supply.Elasticity of Supply:Elasticity of Supply: it is defined as the responsiveness or sensitiveness of supply to thechanges in the price of the good.The extent to which quantity supplied of a commodity changes with the givenchange in the price refers to elasticity of supply.There are five degrees of elasticity of supply. They are
discussed in brief as under:(i) Perfectly elastic supply. Supply curve in graph 7.1 (a) is perfectly elastic (horizontal).The firm will supply any amount of output at Rs.4 per unit. If the price falls below Rs.4(say Rs.3.5) per unit, then the quantity supplied falls to zero. The price is too low tosustain any producer in the market. Elasticity of supply is infinite.
(ii) Perfect inelastic supply. A perfectly inelastic supply represents a situation in whichsellers sell a fixed quantity of good for sale. The price increase from Rs.4 to Rs. 8 has notfed to increase in quantity supplied. The quantity supplied is totally unresponsiveness tochanges in price. The supply curve is vertical = Es = 0.(iii) Unit elastic supply. In case
of unit elasticity of supply, the percentage change inprice brings about the same percentage change in quantity supplied of a good. In figure7.1(c) doubling the price of a good from Rs.4 to Rs.8 per unit doubles the quantitysupplied .from 40 to 80 units Es = 1.(iv) Elastic supply. When the percentage increase in the price of a good brings about, alarger
percentage increase in the supply of a good, the supply of a good said to elasticFig. 7.1(d) shows a 25% increase in the price of a good (Rs.4 to Rs.5), causes a 100%increases in the supply of goods (from 40 to 80 units per day) (Es >1). The supply curvehas a flatter slope. 49. 49(v) Inelastic supply. When the percentage change in price of a good causes
a smallerpercentage in quantity supplied, the supply is said to be inelastic (Es < 1). In fig. there isan 100% increase in the price of good (from Rs.4 to Rs.8) but itbrings a 25% increase in-the quantity supplied (40 to 50 units per day). The supply curveis steeply sloped.Note: The category of elasticity of supply at any point on the supply curve can be
judgedby drawing a tangent to the point of the curve under consideration. If the tangent meetsthe vertical axis, then supply is elastic at that point and its value will be between one andinfinity.. In case it touches, the horizontal axis, then the supply of the good is inelastic atthat point and its value will lie between zero and one. Any straight line supply
curvethrough the origin will have unitary elastic.Determinants of Price Elasticity of Supply:The main factors which determine the degree of price elasticity of supply are as under:(i) Time period. Time is the most significant factor which affects the elasticity of supply.If the price of a commodity rises and the producers have enough time to make
adjustmentin the level of output, the elasticity of supply will be more elastic. If the time period isshort and the supply cannot be expanded after a price increase, the supply is relativelyinelastic.(ii) Ability to store output. The goods which can be safety stored have relatively elasticsupply over the goods which are perishable and do not have storage
facilities. 50. 50(iii) Factor mobility. If the factors of production can be easily moved from one use toanother, it will affect elasticity of supply. The higher the mobility of factors, the greater isthe elasticity of supply of the good and vice versa.(iv) Changes in marginal cost of production. If with the expansion of output, marginalcost increases and
marginal return declines, the price elasticity of supply will be lesselastic to that extent.(v) Excess supply. When there is excess capacity and the producer can increase outputeasily to take advantage of the rising prices, the supply is more elastic. In case theproduction is already up to the maximum from the existing resources, the rising priceswill not
affect supply in the short period. The supply will be more inelastic.(vi) Availability of infrastructure facilities. If infrastructure facilities are available forexpanding output of a particular good in response to the rise in prices, the elasticity ofsupply will be relatively more elastic.(vii) Agricultural or industrial products. In agriculture, time is required to
increase outputin response to rise in prices of goods. The supply of agricultural goods is fairly inelastic.As regards the supply of manufactured consumer goods, it is comparatively easy toincrease production in a short period. Therefore, the supply of consumer goods is fairlymore elastic; In case of supply of aero planes or any other heavy machinery,
the supply isrelatively inelastic as it takes time to manufacture heavy machinery. 51. 51Lecture no:18Price determination equilibrium price and quantity determination of marketpricePRICE DETERMINATION UNDER PERFECT COMPETITIONHaving studied the demand and supply, we know that market demand curve isthe horizontal summation of
the individual demand curves , and similarly the horizontalsummation of the individual supply curves become market supply curve.The intersection of market demand curve and the market supply curve indicatesthe equality of quantity demanded by the consumers and that supplied by the producers.This equality of quantity demanded and quantity
supplied is called equilibrium quantityand the price that occurs at this balancing point is called equilibrium price where thequantity demanded is equal to quantity supplied. When such condition prevails in themarket, the market is said to be in equilibrium, because there are neither shortages norsurpluses of commodity.DETERMINATION OF
MARKET PRICEMarket price is determined by the equilibrium between demand and supply inmarket period or very short run. This market period may be an hour, a day or a few daysor even a few weeks depending upon the nature of the product. The period being short,stock is limited and cannot be produced to meet the increase in demand.
Therefore, thesellers have to confine to the produce available with them. Example: Perishablecommodities like fish. The nature of supply curve in a market period under the twosituations of perishable and non-perishable goods are discussedMarket Price of a Perishable CommodityThe graphical representation for the market price of Perishable
Commodity likefish is presented in Figure . The supply is limited by the available quantity on that day,and it cannot be kept back for the next period and therefore, the whole of it must be soldaway on the same day at prevailing prices. 52. 52The supply curve of fish is a vertical straight line MS, when OM is the quantity of fishavailable on that day. DD
is the market demand curve. With perfect competition betweenbuyers and sellers, an equilibrium price OP will be determined at which the quantitydemanded is equal to the available supply. That is, equilibrium price will be establishedat the point where downward slopping demand curve DD intersects the vertical supplycurve MS.Now suppose that
there is a sudden increase in demand from DD to DD with thesupply of fish remaining unchanged, the larger demand will raise the market price sharplyfrom OP to OP. On the contrary, if there is a decrease in demand from DD to D D theprice will fall and the quantity sold will remain the same.Market Price of Non-Perishable and Reproducible GoodsIn
case of non-perishable but reproducible goods, supply curve cannot be avertical straight line and the seller rough out its length, because some of the goods can bepreserved or kept back from the market and carried over to the next market period. Therewill then be two critical price levels. The first, if price is very high the seller will beprepared to sell
the whole stock. The second level is set by a low price at which the sellerwould not sell any amount in the present market period, but will hold back the wholestock of some better time. The price below which the seller will refuse to sell is calledthe Reserve Price.Given the two price levels, one at which the seller is prepared to sell the wholestock and
the other at which he will refuse to sell at all, the amount which he will offerfor sale will vary with price. Given his anticipations of future price and intensity of hisneed for cash, etc., he will be prepared to supply more at a higher price than at a lowerone. The supply curve of a seller will, therefore, slope upward to the right. Beyond aprice at which he
is prepared to sell the whole stock, the supply curve will be a verticalstraight line whatever the price.In Figure SRFS is the supply curve of the durable goods while OQ is the totalamount of the stock of the goods. Up to price OP, the quantitySupplied varies with price so that at a higher price more is supplied that at a lower one.At the price OS,
nothing is sold, the whole stock being held back. Therefore, SF portionof the supply curve slopes upwards from left to right. At price OP the whole of the stockis offered for sale, and beyond the price OP the quantity supplied remains the same what 53. 53ever the price. Therefore, beyond the price OP, the market supply curve will bevertical straight
line (FS). DD is the demand curve which slope downwards from left toright. Market price comes to settle at OP, because at this price the quantity demanded isequal to the quantity supplied. At this equilibrium price OP, OM amount from the stockis sold , while the rest of the stock i.e., MQ (=RC) is held back from the market.Suppose now the demand
increases from DD to D D, the price will rise to OP,and the whole stock OQ will be sold. If now the demand, further increasefrom D D to some higher level, the quantity supplied or sold will remain the some, i.e.,equal to OQ, and only the price will rise so that, at the new equilibrium level, the quantitydemanded is equal to the available supply. If the
demand decreases from DD to D D,the price will be fall to OP, and the amount sold will decrease to OM.Since, in a perfectly competitive market, the product is homogeneous and nobuyer has any preference for a particular seller, therefore, a single uniform market pricewill be established in the market. Once the market price is determined, an
individualseller in the market will take the price as given and constant. Thus, the demand curvewhich is downward slopping for all sellers is for a single seller a horizontal straight line,i.e., perfectly elastic at the level of the ruling market price.One important conclusion that follows from the above analysis of pricedetermination in the market period is
that costs of production do not enter into thecalculation of the seller, and therefore, have little influence on the market price. 54. 54Lecture No.19Markets definition, essentials of market, classification of market structure perfect and imperfect marketsMARKETThe word market has been derived from the Latin word marcatus which
meansmerchandise or trade.Definitions: A market is any place where the sellers of a particular good or service can meet withthe buyers of that goods and service where there is a potential for a transaction to takeplace. The buyers must have something they can offer in exchange for there to be apotential transaction. A market is the sphere within
which price determining forces operate. A market is the area within which the forces of demand and supply converge toestablish a single price. Economists understand by the market not any particular market place in which thingsare bought and sold but the whole of any region in which buyers and sellers are insuch free contact with one another that
the prices of the same goods tend to equalityeasily and quickly.Essentials of a Market :They may also be termed as the components of a market.1. The existence of a good or commodity for transactions.2. The existence of buyers and sellers3. Business relationship or intercourse between buyers and sellers4. Demarcation of area such as place, region,
country or the whole world.Market Structure : It refers to the size and design of the market. It relates to thoseorganizational characteristics of a market which influence the nature of competition andpricing and affect the conduct of business firms.Monopsony is a market structure in which there is only one buyer instead of one seller.Oligopsony is a
market structure in which there are only few buyers.Bilateral monopoly is a market structure in which a single seller faces a single buyers 55. 55Markets are classified based on the degree of competition as perfect and imperfect marketPerfect market : A market is said to be perfect when all the potential sellers and buyersare promptly aware of the
prices at which transaction take place and all the offers madeby other sellers, and buyers, and when any buyer can purchase from any seller andconversely. Under such a condition, the price of a commodity will tend to be the same (after allowing far cost of transport including import duties) all over the market.Imperfect market : A market is said to
be imperfect when some buyers or sellers or bothare not aware of the offers being made by others. Different prices prevail for the samecommodity at the same time.Comparative Characteristics of MarketsPerfect Monopolistic Oligopoly MonopolyCompetition CompetitionNumber & Many (small Many (small to Few (large) OneNature of sellers)
medium) Inter - dependentSellers IndependentPrice No control Some control Considerable Absolutecontrol controlNature of Homogeneous (no SomeSome t i m e sbut No substitutesProduct differentiation) differentiation not alwaysBarriers to None Low Considerable Entry isentry blockedProfit Normal Profits in Some profits in Considerable Large
ProfitsPotential LR SR & LRProfits in SR& i n SR & LRLRProduct None or minim al Considerable Heavy Some but notPromotIon & directed toAdvertising competition,but toincrease sales 56. 1PERFECT COMPETITIVE MARKETPerfect competition market is the world of price-takers. A perfectly competitive firm sellsa homogeneous product [one
identical to the product sold by others in the industry]. It isso small relative to its market that it cannot affect the market price; it simply takes theprice as given.Perfect competition market is a market under which no buyer or seller can affectunilaterallyCharacteristics of Perfect Competition Market:The main characteristics of perfect competition
market are as follows:01. Large Number of Buyers and sellers:One condition of perfect competition is that there should be operating in the market alarge number of buyers and sellers. If that is so, no single seller or purchaser will be ableto influence the market price, because the output of any single firm is only a smallproportion of the total output
and of the total demand.02. Homogeneous Product:The second condition is that the commodity produced by all firms should be standardizedor identical03. Free Entry or Exit:There should be no restrictions, legal or otherwise, on the firms entry into, or exit from,the industry. In this situation, all the firms will be making just normal profit. If the profitis
more than normal, new firms will enter and extra profit will be competed away; and if,on the other hand, profit is less than normal, some firms will quit, raising the profits forthe remaining firms. But if there are restrictions on the entry of new firms, the existingfirms may continue to enjoy supernormal profit. Only when there are no restrictions
onentry or exit, the firms will earn normal profit.04. Perfect Knowledge: Another assumption of perfect competition is that the purchasersand sellers should be fully aware of the prices that are being offered and accepted. In casethere is ignorance among the dealers, the same price cannot rule in the market for thesame commodity. When the
producers and the customers have full knowledge of theprevailing price, nobody will offer more and none will accept less, and the same pricewill rule throughout the market. The producers can sell at that price as much as they likeand the buyers also can buy as much as they like05. Absence of Transport Costs: If the same price is to rule in a market,
it is necessarythat no cost of transport has to be incurred. If the cost of transport is there, the prices mustdiffer to that extent in different sectors of the market. 57. 206. Demand Curve of Perfect Competition Market is Completely Horizontal:Figure-01: Demand curve looks horizontal to a perfect competitor.The industry demand curve has inelastic
demand at the market equilibrium. However, thedemand curve for the perfectly competitive firm is horizontal (i.e. completely elastic).07. No Government Regulation: Government does not intervene in the marketingfunctions.Pure competition differs from perfect competition in the sense that it excludes thefeatures of Perfect mobility of resources and
Perfect knowledge. 58. 3Lecture No.20Characteristics of monopolistic competition, monopoly, oligopolyMonopolistic Competition, Monopoly and OligopolyChamberlin is associated with Monopolistic CompetitionCharacteristic features of Monopolistic Competition:i) Large Number of firms: The number of firms operating under
monopolisticcompetition is sufficiently large. Moreover there is freedom of entry. There are noquantitative restrictions or differences in market conditions. However, each firm differsfrom its rivals in some qualitative respect.ii) Close Substitutes: Under monopolistic competition firms produce very closesubstitutes. Chocolates of one company may
serve a similar purpose as that of some otherfirm. The only difference may be of some variation in the quality of the product.iii) Group: Firms under monopolistic competition together form a group. They cannot becalled an industry. This is because their products are somewhat dissimilar and nothomogenous as under competitive industry.iv) Product
Differentiation: Under monopolistic competition products aredifferentiated. This is the outstanding feature of this form of market. Otherwisemonopolistic competition closely resembles perfect competition. The fundamentaldifference between the two is that products are no more homogenous. Goods producedare deliberately differentiated by trade
name or brand name or salesmanship or qualityetc.(v) Selling (Advertising) Cost: Selling Cost i.e., advertisement expenditure and ProductDifferentiation together enable the producer to maintain some control over marketconditions and influence the shape of the demand curve. Whenever a product isdifferentiated it is necessary to inform buyers; and
advertisement is the only mediumthrough which buyers can be told about superiority of that product.Features of Monopoly: Monopoly is another traditional form of market. It is an extremeform, opposed to a competitive market structure. As against this, a competitive market isone with a large number of firms or producers.1. Monopoly is a case
where there is only a single seller in the market. This, however, is atheoretical concept.2. Absence of substitutes: for the goods produced and sold by the monopolists. Buyershave no other option except to purchase goods from the monopolist at whatever price hecharges. This results in a situation in which the monopolist has complete control
overmarket conditions. He can decide his own price and earn profits without any fear of 59. 4competition from his rivals. The Cross Elasticity of Demand is negligible or very low.Yet a monopolist has certain constraints arising out of demand and technical conditions.3. There is no distinction between the firm and industry in monopoly market
situation.4. There is complete negation of competition.OligopolyThe word OLIGOPOLY is derived from the Greek words oligmeans a few and polywhich means sellers.Oligopolistic Market refers to a market characterized by the presence of a small numberof producers who often act together to control the supply of a particular good and itsmarket
price.It is dominated by a few large suppliers who are interdependent on each other, beforemaking any pricing and investment decisions. It is also explained as a market condition inwhich sellers are so few that an action of any one of them will materially affect price andhave a measurable impact on competitors; in other words; since there are few
participantsin this type of market, each Oligopolist is aware of the actions of the other.OPEC is an example of Oligopoly since few countries control the production of oil, thesteel and the automobile industry in United States of America is another example.The Key characteristics of an Oligopolistic Market are as follows: - It is a market dominated by a
small number of participants who are able tocollectively exert control over supply and market prices. Few firms sell branded products which are close substitutes of each other. Entry barriers for the other firms are high; the barriers can be due to patents,copyrights, government rules / regulations or ownership of scare resources. Firms are
interdependent for decision making. Products can be homogenous (standardized) or heterogeneous (differentiated). The sellers are the price makers and not price takers, since the few sellers mutuallydominate the pricing decisions. The sellers can achieve supernormal profits in the long run. The sellers can achieve economies of scale; since for the
large producers as the levelof production rises, the cost per unit of products decreases; thus ensuring higher profits. There is high degree of market concentration, since the four-firm concentration ratiois often used, where the market shares of four largest firms are measured (as apercentage) since they form the major portion of the market share.An
Oligopolist faces a downward sloping demand curve; however; the price elasticitydepends on the rivals reaction to change its price, investment and output. 60. 5TheKinkedDemandCurveGraph This assumes that firms seek to maximise profits If they increase price, then they will lose a large share of the market because they becomeuncompetitive
compared to other firms, therefore demand is elastic for price increases. If firms cut price then they would gain a big increase in Market share, however it isunlikely that firms will allow this. Therefore other firms follow suit and cut price as well.Therefore demand will only increase by a small amount: Demand is inelastic for a pricecut Therefore this
suggests that prices will be rigid in OligopolyThe below diagram suggests that a change in Marginal Cost still leads to the same price,because of the kinked demand curve (profit maximization occurs where MR = MC 61. 6Lecture No.21National Income concepts of national income - Gross domestic product, grossnational product, net national
product, net domestic product- national income atfactor cost, personal income, disposable income.NATIONAL INCOMEIntroductionFor understanding the concept of national income, it is necessary to know how aneconomy works. In any economy, its people are engaged in on productive activity or theother, whereby they earn income and spend their
income on goods and services to satisfytheir wants. The health and progress of an economy are to be judged from how much theyare able to produce arid spend i.e. Countrys total output, income and expenditure. Thoseaggregates of the economy are but different aspects of its national, income.Circular Flow: The Wheel of the WealthIn every economy
there are households on the one hand and productive enterprises orfirms on the other. The function of house holds is to consume goods and services for thesatisfaction of their wants. Thus the household is the basic consuming unit in theeconomy. The function of productive enterprises (forms) is to produce goods and servicesfor the satisfaction of the
wants of households and thus the firm or productive enterpriseis the basic producing unit in the economy. The household here may be family unit whileproducing unit (firm) may be grocery shop, factory etc. Besides, Government is anothersector which occupies an important Position. It like households, purchases goods andservices arid since it runs
many public enterprises it act as, producing unit. Thushouseholds, firms and government are the main components of the entire economicorganization of a country which is know as an economy. Economy is the sum total of theoperations of the households, firms and government. 62. 7In every economy there is always a circular flow (movement) of
resource services (i.e.services of land, labour capital and enterprise) from the household to firms and thereverse movement of goods and services from the firms to the households. This isdepicted in the diagram given below.The inner circuit shows the real flows would take place only in barter economy wheregoods and services are exchanged for
goods and services. But in the modern economywhere use of money as medium of exchange is widely adoptedHouseholds supply the resource services or factors to firms and receive in returnpayments in terms of money for goods and services they want. The firms sell goods andservices for money and use the money so received to pay the households
for their supplyof resource services. Thus labour gets Wages; capital gets interest land gets rent andenterprise gets profits all in terms of money, this circular flow of money also known asWheel of Wealth. This flow of money is not continuously at steady level. It may contractor expand when depression and prosperity occur, respectively in an economy.
Thediagram explains circular flow of closed economy where savings and role of Governmentis totally absent.Definition of National Income1) National Income is that part of objective income of the community, including incomederived from abroad, which can be measured in money - Pigou.2) National income may be defined as the money value of the
flow of commodities andservices (excluding imports) reckoned at current prices less the sum of following/items,at current prices.Money value of diminution in stocksMoney value of goods and services used up in the course of productionMoney value of goods and services used to maintain intact existing capital equipments.Receipts from indirect
taxation.Favorable balance of tradeNet increase in the countrys foreign indebtedness.In short, National Income is the aggregate factor income (i.e. earning of labour andproperty) which arises from the current production goods and services by the nationseconomy. Here nations economy refers to the factors of production Labour and property,supplied
by the normal residents of the/ national territory. The national income has threeinterpretations 63. 81) It represents a receipts total.2) It represents expenditure total.3) It represents a total value of production.These three - fold interpretation arises out of fact that, every expenditure is at the sametime a receipt and of goods and services purchased
(bought) are valued at their salesprices. ThusValue Received = Value paid = Value of goods & servicesConcepts of National IncomeThe important concepts of National Income are:1. Gross Domestic Product (GDP)2. Gross National Product (GNP)3. Net National Product (NNP) at Market Prices4. Net National Product (NNP) at Factor Cost or National
Income5. Personal Income6. Disposable Income1. Gross Domestic Product (GDP): Gross Domestic Product (GDP) is the total marketvalue of all final goods and services currently produced within the domestic territory of acountry in a year.It measures the market value of annual output of goods and services currently produced.This implies that GDP is
a monetary measure. All goods and services produced in anygiven year must be counted only once so as to avoid double counting. It ignores thetransactions involving intermediate goods.2. Gross National Product (GNP): Gross National Product is the total market value of allfinal goods and services produced in a year. GNP includes net factor income
from abroadwhereas GDP does not. Therefore,GNP = GDP + Net factor income from abroad.Net factor income from abroad = factor income received by Indian nationals from abroad factor income paid to foreign nationals working in India. 64. 93. Net National Product (NNP) at Market Price: NNP is the market value of all finalgoods and services
after providing for depreciation. That is, when charges fordepreciation are deducted from the GNP we get NNP at market price. Therefore, NNP =GNP DepreciationDepreciation is the consumption of fixed capital or fall in the value of fixed capital due towear and tear.4.Net National Product (NNP) at Factor Cost (National Income): NNP at factor cost
orNational Income is the sum of wages, rent, interest and profits paid to factors for theircontribution to the production of goods and services in a year. It may be noted that:NNP at Factor Cost = NNP at Market Price Indirect Taxes + Subsidies.5. Personal Income: Personal income is the sum of all incomes actually received by allindividuals or
households during a given year. In National Income there are someincome, which is earned but not actually received by households such as Social Securitycontributions, corporate income taxes and undistributed profits. On the other hand thereare income (transfer payment), which is received but not currently earned such as old agepensions,
unemployment allowances, relief payments, etc. Thus, in moving from nationalincome to personal income, the incomes earned but not received should be deducted andadd incomes received but not currently earned. Therefore,Personal Income = National Income Social Security contributions corporate incometaxes undistributed corporate profits +
transfer payments.Disposable Income: It is the amount of money available with the private individuals tospend. From personal income if we deduct personal taxes like income taxes, personalproperty taxes etc. what remains is called disposable income. Thus,Disposable Income = Personal income personal taxes.Disposable Income can either be
consumed or saved. Therefore,Disposable Income = consumption + saving. 65. 10Lecture No.22Methods of measurement of NI product method, income method and expendituremethodMEASUREMENT OF NATIONAL INCOMEProduction generate incomes which are again spent on goods and services produced.Therefore, national income can be
measured by three methods:1. Output or Production method2. Income method, and3. Expenditure method.Let us discuss these methods in detail.1. Output or Production Method: This method is also called the value-addedmethod. This method approaches national income from the output side. Under thismethod, the economy is divided into different
sectors such as agriculture, fishing, mining,construction, manufacturing, trade and commerce, transport, communication and otherservices. Then, the gross product is found out by adding up the net values of all theproduction that has taken place in these sectors during a given year.In order to arrive at the net value of production of a given industry,
intermediate goodspurchased by the producers of this industry are deducted from the gross value ofproduction of that industry. The aggregate or net values of production of all the industryand sectors of the economy plus the net factor income from abroad will give us the GNP.If we deduct depreciation from the GNP we get NNP at market price. NNP
at marketprice indirect taxes + subsidies will give us NNP at factor cost or National Income.The output method can be used where there exists a census of production for the year.The advantage of this method is that it reveals the contributions and relative importanceand of the different sectors of the economy.2. Income Method: This method
approaches national income from the distribution side.According to this method, national income is obtained by summing up of the incomes ofall individuals in the country. Thus, national income is calculated by adding up the rent ofland, wages and salaries of employees, interest on capital, profits of entrepreneurs andincome of self-employed
people.This method of estimating national income has the great advantage of indicating thedistribution of national income among different income groups such as landlords,capitalists, workers, etc.3. Expenditure Method: This method arrives at national income by adding up all theexpenditure made on goods and services during a year. Thus, the
national income is 66. 11found by adding up the following types of expenditure by households, private businessenterprises and the government: -(a) Expenditure on consumer goods and services by individuals and households denotedby C. This is called personal consumption expenditure denoted by C.(b) Expenditure by private business enterprises on
capital goods and on making additionsto inventories or stocks in a year. This is called gross domestic private investmentdenoted by I.(c) Governments expenditure on goods and services i.e. government purchases denotedby G.(d) Expenditure made by foreigners on goods and services of the national economy overand above what this economy spends
on the output of the foreign countries i.e. exports imports denoted by(X M). Thus,GDP = C + I + G + (X M).Difficulties in the Measurement of National Income1. Prevalence of non monetized transactions in agriculture still lot of product doesnot come into the market, It consumed at farm level.2. Illiteracy - Due to illiteracy it is not possible to keep
regular account.3. Occupational specialization is incomplete.4. Lack of adequate statistical data.5. Estimation of value of inventories i.e. raw material is very difficult.6. Estimation of depreciation on capital goods and avoiding double counting is toomuch difficult.Use of National Income data: It is very useful to measure economic welfare,
determinestandard of living of a community, similarly to assess economic development and forcomparison purpose the national income is must. 67. 12Lecture No.23Public Finance meaning, Role and importance of Public finance -functions of the government Differences between public finance and privatefinancePUBLIC FINANCEEvery Government
has to perform different functions and for this purpose it requiresfunds. These funds however are contributed by the every citizen of the country. Thecontribution may be less or more but it is necessary. Thus Public Finance deals withWhy Government takes money how it gets money and where it spends money?Distinction between Public and Private
Finance:Individual and states are similar in that they1. Both require resources2. Both have to maximum results from their resources.3. Both attempts to get the best out of all items of expenditure.There are, however, some important differences between private and public finance:They arePublic Finance Private Finance1States proposed expenditure

determines itsincome.Income determines its expenditure2A public authority can vary the amount ofits income and expenditure within limitsAn individual can not change his incomeand expenses easily.3A state is always repay its funds to peoplein services and does not save the funds.After meeting the needs, individualprefers for saving the income.4 State budgets are generally for one yearFor individual there is no fixed periodof time. The income expenditure iscontinuous.5 The state budget is public It is kept a secret.6State can issue paper Currency to meet itsExpenditure.It is not possible for individualImportance of Public FinanceEvery body realizes necessity of money. The importance of money is too much not onlyfor individual but for state (Government) also. The state has to perform number of 68. 13functions for which money (funds) is required. In developing countries like India,Government is performing many important functions like education, industrial andagricultural developments but lack of funds is one of the constraints. For beginning ofany function funds (finance) is must and in view of this the public finance nowadays hasvital importance. Its importance can be easily understood from the functions of theGovernment. They are1) Allocative Function: It refers to the process by which total resource use is dividedbetween private and social goods by which the mix of social goods is chosen, this is doneby the budgetary policy.2) Distributive function: The budgetary policy also affects the distribution of income inthe community. The tax and expenditure measures are adopted to modify the existingdistribution with a view to reducing economic inequalities.3) Stabilization function: The budgetary policy can also be used to maintain a high levelemployments reasonable degree of price level stability, an appropriate rate of economicgrowth and stability in the balance of payment.Apart from these, public finance is important because it is an effective instrument of statecontrol over the economy. The study of public finance is especially important for theunder developed countries as management of state finances is essential to break thevicious circle of poverty. 69. 14Lecture No.24Public revenue meaning, major and minor sources of public revenuePUBLIC REVENUEThe expenditure of the Government has to be met from the revenue that is accrued by theGovernment from various sources.Sources of revenueThe functions of Government are very important and extensive which require heavyexpenditure. Government has to undertake important functions like defense (internal andexternal), Social welfare, education, health, industry, agriculture. For all of these a hugeamount of funds is required.The major sources of revenue for the Government are in the form of Taxes and Priceswhile the minor sources are Fees, Special assessment, Escheat, Grants, gifts donations,tributes and indemnities.Major Sources:1. Tax: A compulsory contribution imposed on the public. (Details discussed in the nextchapter)2. Price: A price is the payment for a service of business character, for example, chargesfor travelling on railways. The price is different from fee. The fee is for public interest.You can escape a price by not purchasing the said service / commodity.Minor Sources:1. Fee: It is also a compulsory payment but made only by those who obtain a definiteservice in return from the government. The fee covers the part of the cost of serviceprovided to the consumer / client. The licence fee, however, is much more than the costof service and there is not much of a positive service in return.2. Special Assessment: This is a compulsory contribution, levied in proportion to thespecial benefit derived, to defray the cost of a specific improvement to propertyundertaken in the public interest. Suppose the government build a road or bridge orprovide mass transport system or makes suitable sewerage and water supplyarrangements, all the property will appreciate in value. The State has the right to levy aspecial tax on the owners of land or property known as special assessment.3. Rates: They are levied by the local bodies, municipalities and district boards for localpurposes. They are generally levied on immovable property of the residents, but notnecessarily for any special improvements effected or special benefits conferred.4. Escheat: It refers to the property that is claimed by Government of the deceasedwithout successors or will.5. Tributes and indemnities: Tributes are paid by the conquered countries. Indemnitiesare paid for any damage done to the country by way of war of aggression. 70. 156. Grants, gifts and donations: Grants are the funds provided by the apex organizationsto its sub-ordinate organizations. For Example: ICAR grants to SAUs. Gifts are thosefunds granted by the foreign countries during natural calamities etc., Donations are forspecific purposes like educational buidings etc., funded by individuals. 71. 1SOURCES OF PUBLIC REVENUEPUBLIC REVENUEMAJOR SOURCES MINOR SOURCESTax Price Fee Special Rates Escheat Tributes GrantsAssessment Indemnities GiftsDonation 72. 1Lecture No.25Tax meaning, classification direct and indirect taxes, methods of taxation -proportional, progressive, regressive and degressive taxation, Agril taxation othertypes of taxation, VAT.Seligman defines tax as a compulsory contribution from a person to the state todefray the expenses incurred in the common interest of all, without reference to specialbenefit conferred.METHODS OF TAXATION1. Proportional & Progressive Tax: A proportional tax is one in which, whatever thesize of income, same rate or percentage of tax is charged.On the contrary, progressive tax refers to the tax system in which the rate of tax increaseswith the increase in income. It is based on the principle higher the income, higher thetax.2. Regressive & Degressive Tax: A tax is said to be regressive when its burden fallsmore heavily on low-income earners / poor than the high-income earners / rich. It isopposite of progressive tax.A tax is called degressive when the higher income does not make a due sacrifice, or whenthe burden imposed on them is relatively less. This tax may be progressive up to acertain limit beyond which a uniform rate is charged.CLASSIFICATION OF TAXES:Specific Tax, Advolarem Tax & VAT: A specific tax is according to the weight of thecommodity. An advolarem tax is according to the value of a commodity. Value AddedTax(VAT) is levied on businessmen on all the processes carried out by them.Direct & Indirect Tax: Direct tax is one which is paid by the person on whom it isharged. The examples of direct taxes are income tax, wealth tax, etc.On the contrary, the indirect tax is paid by one person and its burden is fallen on other,generally the consumer. The examples of indirect taxes are sales tax, central excise duty,custom duty, recreational tax, etc.Agricultural Income :Agriculture income is exempt under the Indian Income Tax Act.This means that income earned from agricultural operations is not taxed. The reason forexemption of agriculture income from Central Taxation is that the Constitution givesexclusive power to make laws with respect to taxes on agricultural income to the StateLegislature. However while computing tax on non-agricultural income agriculturalincome is also taken into consideration. 73. 2As per Income Tax Act income earned from any of the under given four sources meantAgricultural Income;(i) Any rent received from land which is used for agricultural purpose:(ii) Any income derived from such land by agricultural operations including processingof agricultural produce, raised or received as rent in kind so as to render it fit for themarket, or sale of such produce.(iii)Income attributable to a farm house(iv) Income earned from carrying nursery operations is also considered as agriculturalincome and hence exempt from income tax. 74. 3Lecture No.26Canons of Taxation Adam Smiths canons of taxation equality, economy,certainity and convenience other canons of taxationCANONS OF TAXATIONAdam Smiths was a pioneer in the field of taxation and made notable contributionspopularly known as Canons of taxation.1. Canon of Equality: means the principle of justice, i.e., in accordance to ability topay. It means the equality of sacrifice. The amount of the tax paid is to be in proportionto the respective abilities of the taxpayers. For example: Progressive taxation.2. Canon of Sacrifice: The principle states that tax amount should be in proportion to therespective abilities of the tax payer. The abilities represents the various income levels.3. Canon of Certainty: prescribes that the tax which each individual is bound to payought to be certain, and not arbitrary. The time of payment, the manner of payment, thequantity to be paid, ought to be clear and simple to the taxpayer. Uncertainty in taxationencourages insolence or corruption.4. Canon of Convenience: The tax is to be levied at the time or the manner in which it ismost convenient for the taxpayers to pay their dues. For example, Cess has to becollected from the farmers after the principal crops are harvested and marketed.5. Canon of Economy: It means that the tax will be economical only when the cost ofcollection is small. Huge and unnecessary administrative costs will make the taxcollection an extravagant task.Other Canons of Taxation1. Fiscal Adequacy or Productivity: The State should meet its expenditure from therevenue raised from the people in the form of taxes. However, the government should nothamper the productive capacity by taxing the community heavily.2. Canon of Elasticity: The revenue should increase to cater the needs of the State. Thisis to ensure the government adequate financial resources to meet an emergency situation.3. Canon of Flexibility: It means that there should be no rigidity in the tax system so thatit can be quickly adjusted to new conditions.4. Canon of Simplicity: This aims at tax which is simple, plain and intelligible to thecommon understanding. This canon is essential if corruption or oppression is to beavoided.5. Canon of Diversity: The tax should be a wise admixture of direct and indirect taxes.On the other hand, too great multiplicity will be bad and uneconomical. 75. 46. Social and Economic Objectives: This states that the social and economic objectivesof a standard tax system viz., (i) Reduction of inequalities in the distribution of incomeand wealth, (ii) Accelerating economic growth and (iii) Price stability7. Canon of Neutrality: Taxation system should be used to control threats of economicinstability and stagnation. 76. 5Lecture No.27 &28Public expenditure meaning, need for public expenditure. principles of public expenditurePUBLIC EXPENDITUREPublic Expenditure aids in employment creation through public works programme thusraising the level of income and employment. It helps in toning down the inequalities ofincome and wealth distribution in the country.Need for Public Expenditure1. Social and Economic Overheads: Economic overheads like roads and railways,irrigation and power projects are essential for speeding-up economic development.Social overheads like hospitals, schools, and colleges and technical institutions areessential. Public expenditure has to build up the economic and social overheads.2. Balanced Regional Growth: Special attention has to be paid to the development ofbackward areas and under-developed regions to facilitate balanced regional growth. Thisrequires huge amounts for which reliance has to be placed on public expenditure.3. Development of Agriculture and Industry: Economic development is regardedsynonymous with industrial development but agricultural development provides the baseand has to be given the priority. Government has to incur lot of expenditure in theagricultural sector, For example: Irrigation and power, seed farms, fertilisers factories,warehouses, etc., and in the industrial sector by setting up public enterprises like the steelplants, heavy electrical, heavy engineering, machine-making factories, etc. All theseenterprises are calculated to promote economic development.4. Exploitation and Development of Mineral Resources: Minerals provide a base forfurther economic development. The government has to undertake schemes of explorationand development of essential minerals, For example:, gas, petroleum, coal, etc. Publicexpenditure has to play its pivotal role in the exploration and development of mineralresources.5. Subsidies and Grants to Provinces, Local Governments, and Exporters: The centralgovernment gives grants to State governments which inturn directs to local governmentsto induce them to incur some desirable expenditure. Subsidies have also to be given toencourage the production of certain goods especially for export to earn much neededforeign exchange. 77. 6PRINCIPLES OF PUBLIC EXPENDITUREThe Principles of Public Expenditure are1. Principle of maximum social benefits2. Principle of economy, i.e., wasteful expenditure should be avoided3. Principle of sanction, i.e., authorized expenditure4. Principle of balanced budget5. Canon of elasticity, i.e., fairly flexible6. Avoidance of unhealthy effects on production and distribution1. Principle of Maximum Social Benefits: According to Dalton, the best system of publicexpenditure is that which secures the maximum social advantage from the operationswhich it conducts.2. Principle of Economy: It means that extravagance and waste of all types should beavoided. Public expenditure has great potentiality for public good but it may also proveinjurious and wasteful. If the revenue collected from the taxpayer is heedlessly spent, itwould be obviously uneconomical.To satisfy the principle of economy, it will be necessary to avoid all duplication ofexpenditure and overlapping of authorities. Further, public expenditure should notadversely affect saving. In case government activity damaged the individuals will orpower to save, it would be repugnant to the canon of economy.3. Principle of Sanction: Another important principle of public expenditure is that beforeit is actually incurred, it should be sanctioned by a competent authority. Unauthorisedspending is bound to lead to extravagance and over-spending. It also means that theamount must be spent on the purpose for which it was sanctioned.4. Principle of Balanced Budget: Every government must try to keep its budgets wellbalanced. There should be neither ever-recurring surpluses nor deficits in the budgets.The government, therefore, must try to live within its own means.5. Principle of Elasticity: Another same principle of public expenditure is that it shouldbe fairly elastic. It should be possible for public authorities to vary the expenditureaccording to the needs. A fair degree of elasticity is essential if financial breakdown is tobe avoided.6. Avoidance of Unhealthy Effects on Production or Distribution: It is also necessary tosee that public expenditure exercises a healthy influence both on production and 78. 7distribution of wealth in the community. It should stimulate productive activity so thatthe volume of production in the country increases and it may be possible to raise thestandard of living. The wealth should be fairly distributed. 79. 8Lecture No. 29 & 30Inflation meaning, definition, types of inflation - demand pull and cost pushinflation- comprehensive and sporadic inflation suppressed and repressedinflation creeping, walking, running and galloping inflation mark up inflationRelated concepts of inflation, Rate of inflationINFLATIONInflation indicates the rise in price of a basket of commodities on a point-to-pointbasis. It basically suggests an increase in the cost of living over a period of time, Forexample: 10 essential commodities on 1 st January 2009 for Rs. 100; and the same set of10 commodities costs Rs. 105 on January 1, 2010; the difference in the price is theinflation rate, that is 5 percent. It means that prices are rising at 5 percent per annum.Too much money chasing too few commodities is termed as Inflation.Inflation may be defined as a persistent and appreciable rise in the general price level.Inflation is statistically measured in terms of percentage increase in the price index over aperiod of time usually a year or a month.Related concepts of inflation1. Deflation : A general decline in prices, often caused by a reduction in the supply ofmoney or credit. Deflation can be caused also by a decrease in government, personal orinvestment spending. The opposite of inflation, deflation has the side effect of increasedunemployment since there is a lower level of demand in the economy, which can lead toan economic depression.2. Disinflation: A slowing in the rate of price inflation. Disinflation is used to describeinstances when the inflation rate has reduced marginally over the short term. Although itis used to describe periods of slowing inflation, disinflation should not be confused withdeflation.3. Stagflation : A condition of slow economic growth and relatively highunemployment - a time of stagnation - accompanied by a rise in prices, or inflation.4. Reflation : A fiscal or monetary policy, designed to expand a country's output andcurb the effects of deflation. Reflation policies can include reducing taxes, changing themoney supply and lowering interest rates.Types/ Classification of InflationThere are several types of inflation in the economy which are classified on differentbasis. Some of the important types of inflation are discussed below. 80. 91. Creeping Inflation: When the rise in prices is very slow (less than 3% per annum) likethat of a snail or creeper, it is called creeping inflation. Such an increase in prices isregarded safe and essential for economic growth.2. Walking or Trotting Inflation: When prices rise moderately and the annual inflationrate is a single digit (3% - 10%), it is called walking or trotting inflation. Inflation atthis rate is a warning signal for the government to control it before it turns intorunning inflation.3. Running Inflation: When prices rise rapidly like the running of a horse at a rate ofspeed of 10% - 20% per annum, it is called running inflation. Its control requiresstrong monetary and fiscal measures, otherwise it leads to hyperinflation.4. Galloping or Hyperinflation: When prices rises between 20% to 100% per annum oreven more, it is called galloping or hyperinflation. Such a situation brings a totalcollapse of the monetary system because of the continuous fall in the purchasingpower of money.5. Open inflation: In open inflation, free market mechanism in permitted to fulfill ishistoric function of rationing the short supply of goods and distribute them accordingto consumers ability to pay.6. Repressed inflation : When the government interrupts a price rise, there is repressedor suppressed inflation. Thus, suppressed inflation refers to those conditions in whichprice increase are prevented at the present time though adoption of certain measureslike price control and rationing by the government, but they rise in future on theremoval of such controls and rationing.7. Mark-up Inflation: This type of inflation resulted from the peculiar method of pricingadopted by the big business organizations. According to this method, the big businessorganizations calculate their production costs first and then add to these costs acertain mark-up to yield the targeted rate of profit.8. Comprehensive inflation : When prices of every commodity throughout the economyrise, it is called economy-wide or comprehensive inflation. It is a normal inflationaryphenomenon and refers to the rising prices of the general price level.9. Sporadic inflation : This is a kind of sectional inflation; it consists of cases in whichthe averages of a group of prices rise because of increase in individual prices due toabnormal shortage of specific goods. When the supply of some goods becomesinelastic, at least temporarily, due to the physical or structural constraints, thesporadic inflation has its way.10. Profit induced Inflation: During inflation, the entrepreneur class may tend to expectan upward shifting of the marginal efficiency of capital (MEC); hence, entrepreneursare induced to invest more even by borrowing at higher interest rates. Eventually,investment exceeds savings and economy tends to reach a higher level of moneyincome equilibrium. If economy is operating at full employment level or if there arebottlenecks of market imperfections, real output will not rise proportionately, so theimbalance between money income and real income is corrected through rising prices. 81. 1011. Demand-pull Inflation: At the full-employment output, aggregate demand may begreater than aggregate supply, an inflationary gap exists at full-employment levelwith the price level bid up.12. Cost-push Inflation: It is caused by an autonomous rise in money wages or other inputprices. If producers response by raising prices, it becomes a wage-price spiral.13. Demand-shift Inflation: Aggregate demand often changes faster than the change onresource allocation. Whenever demand changes, the changes in output may not catchup with the change in demand, the excess demand may lead to inflation, at least in theshort run.Measurement of InflationInflation in India is calculated considering various price index tools.A price index is a normalized average (typically a weighted average) of prices for a givenclass of goods or services in a given region, during a given interval of time.Some notable price indices include Consumer price index, wholesale price index Producerprice index and GDP deflator.Rate of inflation: It is defined as the rate of change of the price level as measured by theConsumer price indexRate of inflation in tthperiod = Price level (tthyear) Price level (t - 1thyear) X 100Price level (t - 1thyear)Consumer Price Index (CPI)Consumer Price Index measures the cost of a fixed basket of products and services. It is aweighted average measure of changes in price of products or services within the basket.The consumer price index is also known as cost-of-living index.The consumer price basket includes transportation, food and medical care.Large rises in CPI in a short time typically denotes a period of inflation.C P I (Cost of the bundle in a given period /Cost of the bundle in the base year) X 100Wholesale Price Index (WPI) or Producer Price Index (PPI)Wholesale price is the price of representative basket of wholesale goods.Wholesale price index concentrates on price of goods that are transported within corporatesrather than consumers. The changes in WPI indicate the price changes in industry whichwill in turn represent the changes in supply and demand. 82. 11Lets calculate the WPI for the year 2009 for a particular commodity. Lets assume thatprice of a kilogram of wheat in 1993 is Rs 15.00 and in 2009 it is Rs 18.00. The WPI ofwheat for the year 2006 is(Price of Wheat in 2009 Price of Wheat in 1993)/ Price of Wheat in 1993 x 100i.e. ((18 15)/15) x 100 = 20.Since WPI for the base year is assumed to be 100, WPI for 2009 will be 100+20 = 120.Calculation of Inflation from WPIThe WPI values at two time zones are considered , say, beginning and end of year, theinflation rate of the year can be calculated as(WPI of end of year WPI of beginning of year)/WPI of beginning of year x 100.The GDP or GNP DeflatorIt is an index of the prices of all final goods and services constituted the GDP or GNP.GDP Deflator = (Nominal GDP / Real GDP) X 100Food inflationThe food price inflation in the country can be attributed to low growth in food grainproduction, low competition and poor integration of supply over time and space. Theremedial measures therefore include increase in domestic production and imports, andpromote competition in food markets. 83. 12Lecture No.31 &32Causes of inflation Remedial measures monetary fiscal measures.Causes of Inflation Remedial measuresBroadly speaking inflation arises when the aggregate demand exceeds the aggregatesupply of goods and services. The factors which lead to increase in demand and theshortage of supply are discussed.Factors Causing Increase in Demand:1. Increase in Money Supply: Inflation is caused by an increase in the supply of moneywhich leads to increase in aggregate demand. The higher the growth rate of nominalmoney supply, the higher is the rate of inflation.2. Increase in Disposable Income: When the disposable income of the people increases,it raises their demand for goods and services. Disposable income may increase withthe rise in national income or reduction in taxes or reduction in the saving of thepeople.3. Increase in Public Expenditure: In modern world government activities have beenexpanding which resulted in increase government expenditure. This raised theaggregate demand for goods and services, thereby causing inflation.4. Increase in Consumer Spending: The demand for goods and services also increaseswhen consumer spending increases due to conspicuous consumption or demonstrationeffect.5. Cheap Monetary Policy: Cheap monetary policy or the policy of credit expansion alsoleads to increase in the money supply which raises the demand for goods and servicesin the economy thereby leading to inflation. This is also known as credit-inducedinflation.6. Deficit Financing: In order to meet its mounting expenses, the government resorts todeficit financing by borrowing from the public and even by printing more notes. Thisraises aggregate demand in relation to aggregate supply, thereby leading toinflationary rise in prices.7. Increase in Exports: When the demand for domestically produced goods increases inforeign countries, this raises the earnings of industries producing export commodities.These, in turn, create more demand for goods and services within the economy.Apart from the above factors, expansion of the private sector, existence of blackmoney and the repayment of public debt by the government also increases theaggregate demand for goods and services in the economy.Factors Causing Shortage of Supply: Following are the factors which result in a reductionin the supply of goods and services: 84. 131. Shortage of factors of production: When there is shortage of factors of production likelabour, capital, raw materials, etc. there is bound to be reduction in the production ofgoods and services.2. Industrial Disputes: In countries where trade unions are powerful, they resort tostrikes and lock-outs which resulted in a fall in industrial production thereby reducingthe supply of goods.3. Natural Calamities: Natural calamities like droughts, floods, etc. adversely affects thesupplies of agricultural products. This creates shortage of food products and rawmaterials, thereby helping inflationary pressures.4. Artificial Scarcities: Artificial scarcities are created by hoarders and speculators whoindulge in black marketing. Thus, they are instrumental in reducing supplies of goodsand raising their prices.5. Increase in Exports: When the country produces more goods for exports than fordomestic consumption, this creates shortages of goods in the domestic market. Thisleads to inflation in the economy.6. Lop-sided production: If the stress is on the production of comforts, luxuries, or basicproducts to the neglect of essential consumer goods in the country this createsshortages of consumer goods. This again causes inflation.7. Law of Diminishing Returns: If industries in the country are using old machine andoutmoded methods of production, the law of diminishing returns operates. This raisescost per unit of production, thereby raising the prices of products.8. International Factors: In modern times, inflation is a worldwide phenomenon. Whenprices rise in major industrial countries, their effects spread to almost all countrieswith which they have trade relations. Often the rise in price of a basic raw materiallike petrol in the international market leads to rise in the price of all relatedcommodities in a country.Measures to control InflationInflation is caused by the failure of aggregate supply to equal the increase in aggregatedemand. The various measures to control inflation are:Monetary Measures(a) Credit Control: The central bank could adopt a number of methods to control thequantity and quality of credit to reduce the supply of money. For this purpose, it raisesthe bank rates, sells securities in the open market, raises reserve ratio, and adopts anumber of selective credit control measures, such as raising margin requirements andregulating consumer credit.(b) Demonetisation of Currency: Another monetary measure is to demonetise currency ofhigher denominations. Such a measure is usually adopted when there is abundance ofblack money in the country. 85. 14(c) Issue of New Currency: The most extreme monetary measure is the issue of newcurrency in place of the old currency. Under this system, one new note is exchanged for anumber of the old currency. Such a measure is adopted when there is an excessive issueof notes and there is hyperinflation in the economy.Fiscal Measures(a) Reduction in Unnecessary Expenditure: The government should reduce unnecessaryexpenditure on non-development activities in order to curb inflation.(b) Increase Taxes: To cut personal consumption expenditure, the rates of personal,corporate and commodity taxes should be raised and even new taxes should be levied, butthe rates of taxes should not be too high as to discourage saving, investment andproduction.(c) Increase in Savings: Another measure is to increase savings on the part of the peopleso that their disposable income and purchasing power would be reduced. For this thegovernment should encourage savings by giving various incentives.(d) Surplus Budgets: An important measure is to adopt anti-inflationary budgetary policy.For this purpose, the government should give up deficit financing and instead havesurplus budgets. It means collecting more in revenues and spending less.(e) Public Debt: In addition, the government should stop repayment of public debt andpostpone it to some future date till inflationary pressures are controlled. Instead, thegovernment should borrow more to reduce money supply with the public.Other measures to control inflation generally aims at increasing aggregate supply andreducing aggregate demand directly. These are :-(a) Increase production.(b) Rational Wage Policy:(c) Price Control: Price control and rationing is another measure of direct control to checkinflation. Price control means fixing an upper limit for the prices of essential consumergoods.(d) Rationing:(e). Enhance imports 86. 15Reference Books:1. Dewett, K.K. and Chand, A.1979 Modern Economic Theory S.Chand and Co.,New Delhi2. Dewett, K.K. and Varma, J.D. 1986 Elementary Economics S.Chand and Co.,New Delhi.3. Jhingan, M.L.1990 Advanced Economic Theory Vikas Publishing House, NewDelhi4. Subba Reddy, S, Raghu Ram, P., Sastry, T.V.N. and Bhavani Devi, I. 2009Agricultural Economics Oxford & IBH Publishing Co., Pvt. Ltd., NewDelhi 95%(66)95% found this document useful (66 votes)38K viewsThe document discusses the meaning and definitions of economics. It covers traditional and modern approaches to economics including microeconomics and macroeconomics. Microeconomics focuses SaveSave Agricultural Economics Notes For Later95%95% found this document useful, undefined

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