NATIONAL INCOME AND RELATED AGGREGATES

Q1. Who are normal residents of a country?

Ans. A normal residents is said to be one and who ordinarily resides in the country concerned and whose centre of economic interest lies in that country. A person residing in a country for a period of one year is taken as ordinarily residing in that country. A person is said to have his economic interest in a country when he conducts his economic transactions (relating to production, consumption or investment) in that country.

The following person are not treated as:-

- **<u>NORMAL RESIDENTS OF THE COUNTRY</u>:-**

1. Foreign visitors in the country for holidaying, medical treatment, studies, conferences and sports etc.
2. Crew members of foreign vessels, commercial travellers and seasonal workers of the country.
3. Foreigners who are employees of non resident enterprises and who have come to the country for purpose of installing machinery in these enterprises.
4. Border workers or persons who cross the border between two countries daily or regularly in order to work in one country are the residents of the country in which they live, not of the country in which they are working.
5. Officials, diplomats and members of the armed forces of a foreign country are treated as the normal residents of the country to which they belong and not of the country in which they are employed.

- **<u>THUS NORMAL RESIDENTS OF OUR COUNTRY INCLUDE</u>:-**

1. Citizens of our country who normally reside in the country and whose centre of economic interest lies in the country.
2. Citizens of other nations who continue to live in our country beyond a period of one year and whose centre of economic interest lies in our country.
3. Citizens of our country working in international organisations (like world bank and IMF) or foreign embassies located in other country, and
4. Citizens of our country and whose centre of economic interest lies in their home country.

❖ **<u>SOME EXAMPLE SOF NORMAL RESIDENTS AND NON RESIDENTS</u>:-**

NORMAL RESIDENTS	NON RESIDENTS
1. Indian working in foreign embassies in India.	Foreigners working in Indian embassies in Canada and Japan.
2. Indians employed in world health organisation located in India.	Foreigners working in world health organisation located in India.
3. Local people working in the office of international monetary fund in India.	The German working as director of the office of international monetary fund located in India.
4. Ambassador for India in rest of the world.	Ambassador for India in rest of the world.
5. The foreign citizens living in India for a period of more than one year.	The foreign technical experts working in India for a period of less than one year.

❖ **<u>DOMESTIC AND NATIONAL CONCEPTS OF INCOME</u>;-**

- **<u>DOMESTIC TERRITORY OF A COUNTRY</u>:-** The domestic territory of a country is understand to mean political territory of a nation. It refers to economic territory which is much wider concept than political territory.
- **<u>ECONOMIC TERRITORY</u>:-** Economic territory is the geographical territory administrated by a government within which persons, goods and capital circulate freely.

❖ **<u>DOMESTIC TERRITORY (ECONOMIC TERRITORY) OF A NATION INCLUDES THE FOLLOWING</u>:-**

1. Territory lying within the political frontiers including territorial waters of a country.

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2. Ships and aircrafts operated by residents of the country across different parts of the world.
   Example:- Indian ships moving between Japan and Korea regularly or passenger planes operated by Air India between England and Canada are a part of the domestic territory of India
3. Fishing vessels, oil and natural gas rigs and floating platforms operated by the residents of the country in the international waters.
   Example:- The fishing boats operated by Indian fishermen in the international waters of the Indian ocean are a part of the domestic territory of India.
4. Embassies, consulates and military establishments of the country located abroad.
   Example:- The Indian embassy in united states of America is a part of the domestic territory of India and the embassy of USA in India is a part of the domestic territory of united states of America.

❖ **FACTORS INCOME AND TRANSFER INCOME:-**

1. **FACTOR INCOME:-** It refers to income received by factors of production/ lands / labour / capital and entrepreneur) for rendering factor services in the production process.

- It is received for providing factor services of land, labour, capital and enterprise.
- Factor income of normal residents of a country is included in the national income.
- **Examples:-** Rent, wages, interest and profit.

2. **TRANSFER INCOME:-** It refers to income received without rendering any productive service in return.

- It is a unilateral concept.
- It is not included in national income as it does not reflect any production of goods and services.
- It can be received either within the domestic territory of a country or from abroad.
- **Examples:-** Old age pensions, scholarship, unemployment allowance, pocket money etc.

Taxes received by the government are the transfer incomes, of the government as they are received without providing service in return. Similarly, subsidies paid by the governments are transfers payments of the governments.

❖ **DIF FERENCE BETWEEN FACTOR INCOME AND TRANSFER INCOME:-**

Basis	Factor income	Transfer income
Meaning	It refers to income received by factors of production for rendering factor services in the production process.	It refers to income received without rendering any productive service in return.
Nature	It is included in both national income and domestic income.	It is neither included in national income nor in domestic income.
Concept	It is an earning concept.	It is a receipt concept.
Recipient	It is received by factors of production, land, labour, capital and enterprise).	It is generally received by households and governments.
Examples	Rent, wages, interest and profit.	Scholarship, old age pension, unemployment allowance.

- **GROSS DOMESTIC PRODUCT AT MARKET PRICE(GDPmp):-** It refers to gross market value of all final goods and services produced within the domestic territory of a country during a period of one year. By making adjustments in GDPmp we can derive other aggregates.

- **GROSS DOMESTIC PRODUCT AT FACTOR PRICE(GDPfc):-** It refers to gross money value of all the final goods and services produced within the domestic territory of a country during a period of one year. GDPfc = GDPmp – net indirect taxes

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- **NET DOMESTIC PRODUCT AT MARKET PRICE (NDPmp):-** It refers to net market value of all the final goods and services produced within the domestic territory of a country during a period of one year. NDPmp = GDPmp – depreciation

- **NET DOMESTIC PRODUCT AT FACTOR COST (NDPfc):-** It refers to net money value of all the final goods and services produced within the domestic territory of a country during a period of one year. NDPfc = GDPmp – net indirect taxes – depreciation. NDPfc is also known as domestic income and domestic factor income.

- **GROSS NATIONAL PRODUCT AT MARKET PRICE (GNPmp):-** It refers to gross market value of all the final goods and services produced by the normal residents of a country during a period of one year. GNPmp = GDPmp + net factor income from abroad.

- **GROSS NATIONAL PRODUCT AT FACTOR COST (GNPfc):-** It refers to gross money value of all the final goods and services produced by the normal residents of a country during a period of one year. GNPfc = GNPmp – net indirect taxes.

- **NET NATIONAL PRODUCT AT MARKET PRICE (NNPmp):-** It refers to net market value of all the final goods and services produced by the normal residents of a country during a period of one year. NNPmp = GNPmp – depreciation.

- **NET NATIONAL PRODUCT AT FACTOR COST (NNPfc):-** It refers to net money value of all the final goods and services produced by the normal residents of a country during a period of one year. NNPfc = GNPmp – net indirect taxes – depreciation. It must be noted that NNPfc is also known as national income.

❖ **DIFFERENCE BETWEEN DOMESTIC INCOME AND NATIONAL INCOME:-**

BASIS	DOMESTIC INCOME	NATIONAL INCOME
Nature of concept	It is a territorial concept as it includes the value of final goods and services produced with domestic territory of a country.	
Category of producers	It considers all producers within the domestic territory of the country.	It considers all producers who are normal residents of the country.
NFIA	It does not include NFIA.	It include NFIA.

❖ **GROSS DOMESTIC PRODUCT AT MARKET Vs NATIONAL INCOME:-**

Basis	Gross domestic product at market price	National income
Nature of concept	It is territorial concept as it includes value of final goods and services produced within domestic territory of a country.	It is national concept as it includes the value of final goods and services produced in the entire world.
Category of producers	It considers all the producers within the domestic territory of the country.	It considers the producers who are normal residents of the country.
Net indirect taxes	It is at market price, i.e. it includes net indirect taxes.	It is at factor cost, i.e. it excludes net indirect taxes.
Depreciation	It is inclusive of depreciation.	It does not include depreciation.

❖ **NOMINAL GDP:-** It refers to GDP at current prices. It is the market value of the firm goods and services produced within the domestic territory of a country during an accounting year as estimated using the current year prices. Current years prices are the prices prevailing during the year of

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estimation. Thus, normal GDP = Q × P (where Q = quantity of final goods and services produced during an accounting year, P = prices prevailing during the accounting year).
Nominal GDP can increase when there is increase in other Q or P. If it increase owing to increase in Q / P remaining constant, it shows increase in nominal GDP owing to increase in output.

- **REAL GDP:-** It refers to GDP at constant price. It is the market value of the final goods and services produced within the territory of a country during an accounting year as estimated using the base year prices. Base year is the year of comparison. Real GDP = Q × P* (Here Q = quantity of final goods and services produced an accounting year, P* = prices prevailing during the base year).
  Real GDP increases only when Q increases. Simply because P* is constant. So, that when real GDP increases, there is an increase in the flow of goods and services in the economy. Other things remaining constant, higher the level of real GDP, greater should be the availability of good and services to the residents of a country.

For example Table 1. Estimation of nominal GDP

ASSUMPTIONS:- (I) The economy produces wheat, cloth and sugar only, and (ii) output remains constant.

Table 1 shows how nominal GDP can rise even when output is constant.

Year	Commodity	Quantity	Price	GDPmp (nominal)
2011-12	Wheat Cloth Sugar	20 tonnes 100 metres 5 tonnes	100 per tonne 5 per metre 500 per tonne	2000 500 2500
			Total market value	5,000
2016-17	Wheat Cloth Sugar	20 tonnes 100 metres 5 tonnes	1000 per tonne 20 per metre 1600 per tonne	20,000 2,000 8,000
			Total market value	30,000

Table 2 shows that real GDP rises only when output rises.

Table 2: estimation of real GDP

Assumption:- (i) The economy produces wheat, cloth and sugar only, and (ii) Prices remain constant.

Year	Commodity	Quantity	Price	GDPmp (real)
2011-12	Wheat Cloth Sugar	20 tonnes 100 metres 5 tonnes	100 per tonne 5 per tonne 500 per tonne	2000 500 2500
			Total market value	5000
2016-17	Wheat Cloth Sugar	30 tonnes 200 metres 10 tonnes	100 per tonne 5 per metre 500 per tonne	3000 1000 5000
			Total market value	9000

- **GDP AT CURRENT PRICES:-** GDP at current prices also called monetary or nominal GDP refers to market value of the final goods and services produced within the domestic territory of a country during an accounting year, as estimated using the current year prices. It may increase without any increase in the quantum of output in the economy.

- **GDP AT CONSTANT PRICES:-** It refers to market value of the final goods and services produced within the domestic territory of a country during an accounting year as estimated using the base year prices. It increases only when there is increase in the quantum of output in the economy.

- **DIFFERENCE BETWEEN GDP AT CURRENT PRICES AND GDP AT CONSTANT PRICES.**

GDP at current prices	GDP at constant prices
1. It is the market value of the final goods and services produced within the domestic territory of a country during an accounting year as estimated at current year prices.	It is the market value of the final goods and services produced within the domestic territory of a country during an accounting year as estimated at base year prices.
2. It can increase if price level rises even there is no increase in the flow of goods and services in the economy.	It can increase only when the flow of goods and services increases in the economy.
3. It is known as nominal GDP.	It is known as Real GDP.
4. It is not a good measure of welfare of people.	It is a good measure of welfare of people.

- **CONVERSION OF NOMINAL GDP INTO REAL GDP:-** Nominal GDP or GDP at current prices can be converted into real GDP at constant prices by using the price index. GDP at constant prices of a country estimated at base year prices. We assume the price index or the level of price of base year to be 100. If GDP at current prices is divided by the price index of the current year and multiplied by the price index of base year (which is always equal to 100), we obtain GDP at constant prices or real GDP.

- **REAL GDP OR GDP AT CONSTANT PRICES:-**

$$= \frac{\text{GDP at current prices}}{\text{Price index}} \times 100$$

- **EXAMPLE;-** If in 2011, GDP is Rs. 100 crore, and in 2017 it is Rs. 200 crore at the current prices. And, if price index rises from 100 to 400 within the same period, then GDP at current prices is converted into real GDP (or GDP at constant prices).

Table 3 conversion of nominal GDP into real GDP

Year	GDP at current prices (Rs. In crore)	Index number of current prices index	GDP at constant prices (or base year prices (Rs. In crores).
2017	200	400	200 × 110/400 = 50

- **GDP AND WELFARE:-** Real GDP is considered as an index of welfare of the people. Welfare of the people is measured in terms of the availability of goods and services per person. Increase in real GDP means increase in the level of output in the economy. This means greater availability of goods per person. This leads to higher level of welfare. It is because of this reason that the planners and politicians in a country always lay emphasis on the growth rate of GDP. Higher the growth of GDP greater is the flow of goods and services. Also, higher level of output, with higher will be the level of employment. It is also associated with higher level of efficiency and productivity on the economy. Purchasing power of the people tends to rise. Aggregate demand rises. This leads to higher investment. Higher investment leads to yet another cycle of GDP growth. And, another cycle of increase in welfare of the people. Thus, there is a strong relationship between GDP growth and increase in the level of welfare of the people.

- **GDP AND VIRTUOUS CIRCLE OF GROWTH:-**

- Rise in real GDP   Rise in the level of employment as well as efficiency (or productivity)   Rise in incomes of the people   Rise in aggregate demand   Rise in inducement to invest   Higher level of investment   Rise in real GDP once again. And the cycle continuous.

- **<u>LIMITATIONS</u>:**- But there are limitations related to the positive relationship between GDP and welfare.

1. **<u>DISTRIBUTION OF INCOME</u>:-** If distribution of income turns unequal GDP growth fails to reflect a rise in social welfare. India is facing this situation at present.
2. **<u>COMPETITION OF GDP</u>:-** Composition of GDP may not be welfare oriented. **Example:-** Increase in the production of defence goods does not lead to any direct increase in welfare of the people.
3. **<u>NON MONETARY EXCHANGES</u>:-** In rural economic barter system of exchange still prevails to some extent. Payment for farm labour are after made in kind rather than in cash. All such transactions remain unrecorded. This causes indertimation of GDP. So, it remains an inappropriate index of welfare.
4. **<u>EXTERNALITIES</u>:-** Externalities refer to goods and bad impact of an economy activity without paying the price or penalty for that. There are both example, Mr. X maintains a beautiful garden and Mr. Y (neighbour of Mr. X) enjoys it. It adds to welfare of Mr. Y but he does not pay for it. Negative externalities occur when, for example, stubble burning by the farmers lead to air pollution. It causes a loss of social welfare. But, most farmers do not pay the penalty. GDP fails to account for the impact of positive and negative externalities on social welfare. Hence, it is an inappropriate index of welfare.

Thus, there are serious limitations of GDP as an index of welfare. These limitations reduce the significances of GDP as an index of welfare.