

After understanding the circular flow of income, it's time to understand some of the important terms and definition of national income which will helps in solving the numerical questions,

- **Domestic territory (economic territory)**

It is an important concept of national income analysis.

**“Domestic territory means the political frontiers/borders of a country”.**

According to united nations, Domestic territory is the geographical territory administrated by a government within which persons, goods and capital circulates freely.

**It also includes :-**

- Ships and aircrafts owned and operated by home country between any other countries.  
Example:-Planes of Air India comes under the domestic territory of our country even though they were flying between china and Japan.
- Embassies, consulates and military establishments of a country located abroad.
- Fishing vessel, oil and natural gas rigs operated by the residence of a country in the international water.



- ❖ **Domestic territory does not include :-**

- Embassies, consulates and military establishments of foreign country located in domestic country.
- International organizations like UNO, WHO etc. located within the geographical boundaries of a country.



- ❖ **Normal residents :-**

A normal resident of a country refers to an individual or an institution who ordinarily resides in a country for a period more than one year and whose center of economic interest lies in that country (i.e. he carries all the economic activities of earning, spending and saving from that country)

- ❖ **Not included in normal resident :-**

- Foreign tourists and visitors
- International organization.
- Foreign staff of embassies located in the given country.
- Employees of international organization are considered as residents of the country to which they belong.
- Border workers.

- ❖ **Citizen :-**

Citizenship is basically a legal concept based upon 2 things

- 1) On the place of birth
- 2) By some legal provisions.  
i.e. one can be the citizen of a particular country either by taking birth in that country or by some legal provisions.

- ❖ **Factor income :-**

It refers to the income received by the factors of production for rendering their factor services in the process of production.

Factor income earned by the normal residence is included in national income.

### ❖ **Transfer income :-**

It refers to the income received without rendering any productive service in return.  
For example-Old age pension, scholarship etc.

**Transfer income is not included in national Income**

### ❖ **Final and intermediate Goods :-**

#### **Final Goods :-**

It refers to those goods which are used either for consumption or for investment. That is they are those goods which are used for final consumption. Final goods are neither resold nor used for any further transformation in the process of production.

#### **Intermediate Goods :-**

It refers to those goods which are used either for resale or for further production in the same year.

These goods are generally purchased by one production unit from another production unit.

#### **Intermediate Goods (example)**



**For example:-** furniture purchased by a furniture mart is an intermediate good for the mart, whereas if the same furniture is purchased by a household then it is termed to be as final good. So, a commodity can't be completely classified as intermediate or final goods it depends upon the nature of use.

It should be remembered that intermediate goods must be used up in the same year. If they remain more than one year then they are treated as final goods

**Example:-** Ram limited purchased 10 units for further production, he used only 7 units in this year. The remaining 3 are also treated as final goods(at the end of the year)

### ❖ **Consumption and Capital goods :-**

#### **Consumption goods :-**

They are those goods which directly satisfy the wants of a consumer.

**Example:-** Bread, shirt, Furniture etc.



#### **Types of Consumption goods:-**

- 1) Durable goods (Life span many years. Such as T.V, Computer, Furniture etc)
- 2) Semi durable goods (Life span around 1 year. Such as, clothes, shoes etc)
- 3) Non Durable goods (used up in single act of consumption. like bread, milk etc)
- 4) Services

**Capital goods:-** They are those final goods which help in production of other goods and services

**Example:-** Machinery, fixtures etc



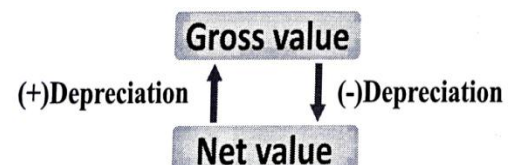
Till the above definition we had learnt some general concepts which are mandatory for the study of national income. Now, we will derive different formulas which help us in calculating national income of our economy.

### ● **Gross value:-**

The value of the commodity at the time of its purchase is known as its gross value.

**Example:-** 2 years back, Ramesh purchased REDMI note 5 pro at rupees 15000.

So the gross value of that phone is rupees 15000



- **Net Value:-**

The present and actual value of the commodity is known as its net value.

Example:-After 2 years, if Ramesh wants to sell his phone it would be approx 8000.

So the net value of my phone is rupees 8000

- **Depreciation:-**

The difference between the gross and net value of the commodity is known as depreciation.

In other words, the reduction in the value of a commodity due to passage of time is termed to be the depreciation.

(15000 – 8000 = 7000 depreciation)

- **Depreciation is also known as :-**

- |   |                               |                                   |
|---|-------------------------------|-----------------------------------|
| ✓ | Current replacement cost      | Replacement cost of fixed capital |
| ✓ | Capital consumption allowance | Consumption of fixed capital.     |

### Net indirect tax (NIT) :-

**NIT = Indirect tax – Subsidies**

- ❖ **Indirect tax:-**

It refers to those taxes which are imposed by the government on the production and sale of goods and services.

Example:- GST, Excise duty

Indirect tax increases the price of the commodity in the market

- ❖ **Subsidies:-**

It refers to the financial assistance given by the government to an enterprise on the production of certain goods and services.

Example:- in India, LPG cylinder is sold at subsidised rates

Subsidy reduces the market price of the commodity.

- ❖ **Factor Cost and Market price:**

- ❖ **Factor Cost:-**

It refers to the amount paid to the factors of production for their contribution in the production process (Cost of production).

- ❖ **Market Price:-**

It refers to the price at which the product is actually sold in the market.

- ❖ **Net Factor Income From Abroad (NFIA):-**

FIA = Factor Income received from abroad- factor income paid to abroad

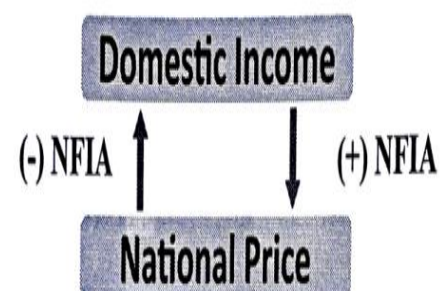
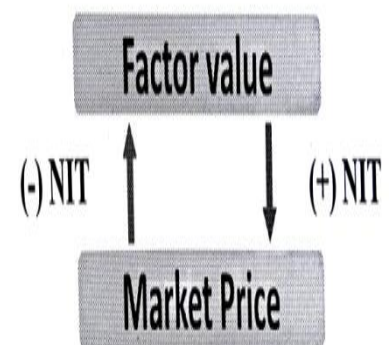
It refers to the difference between factor income received from rest of the world (ROW) and factor income paid to the rest of the world.

NFIA can be:-

- Positive (Received > Paid)\
- Negative (Received < Paid)
- Zero (Received = Paid)

### Components of NFIA:-

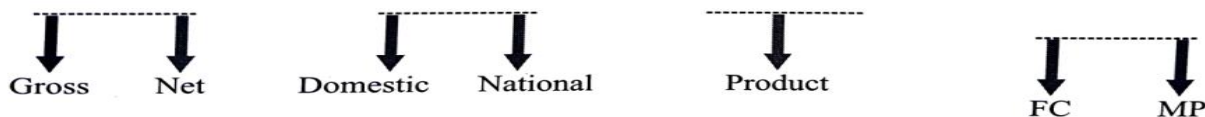
- Net compensation to employees
- Net income from property and entrepreneurship
- Net retained earnings (Savings)



$$\text{NFIA} = \text{FIFA}(\text{EXPORT}) - \text{FITA}(\text{IMPORT})$$

❖ **Basic Aggregates of National Income:-**

The different aggregates of national income are written in specified format which is as follows



- **The first place can be filled by 2 alternatives that is Gross and Net**

And we have the formula to reach Net value from the Gross value

That is,  $\text{Gross Depreciation} = \text{Net}$

- **At second place, we have Domestic and National**

Also, we can alter from domestic to national by the given formula

$\text{Domestic} + \text{NFIA} = \text{National}$

- **The third place is fixed for term 'Product'**

- **At the last place, we have 2 more alternatives which are**

Factor Cost and Market Price

Also,  $\text{Factor Cost} + \text{NIT} = \text{Market Price}$

So now we can read the aggregates of national income easily, such as

**GDPmp = Gross Domestic Product at Market Price**

**NDPmp = Net Domestic product at Market price**

**GNPfc = Gross National Product at Factor Cost, and so on...Also,**

**NNPfc = Net National Product at Factor Cost (National Income)**

**NDPfc = Net Domestic Product at Factor Cost (Domestic Income)**

**NDPmp = Net Domestic Product at Market Price.**

The 3 basic formulas which we had learnt in this chapter would help us to shuffle the different aggregates, such as

**$\text{GNPmp} = \text{NNPmp} + \text{Dep}$**

**$\text{GDPmp} = \text{GNPfc} - \text{NFIA} + \text{NIT}$**

**$\text{NNPfc} = \text{GDPmp} - \text{Dep} + \text{NFIA} - \text{NIT}$**

And so on .....

So if we know the value of any aggregate of national income then we can easily shuffle it to other by using these 3 formulas.

**$\text{Gross Value} - \text{Dep} = \text{Net Value}$**

**$\text{Factor cost} + \text{NIT} = \text{Market Price}$**

**$\text{Domestic} + \text{NFIA} = \text{National Income}$**

- **Categorization of Domestic Income { NDP<sub>fc</sub> }**

