

# What Is Economics?



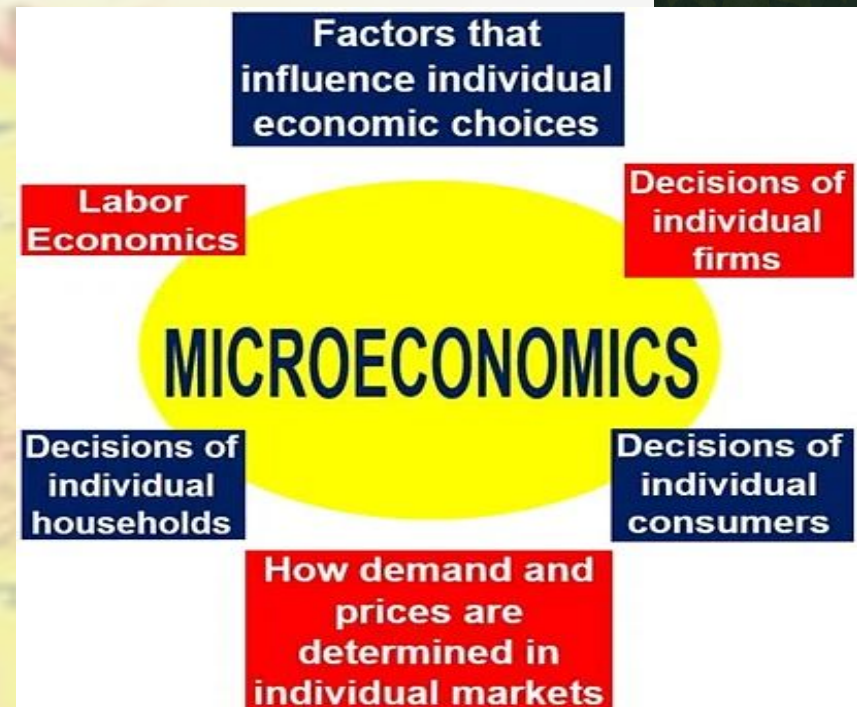
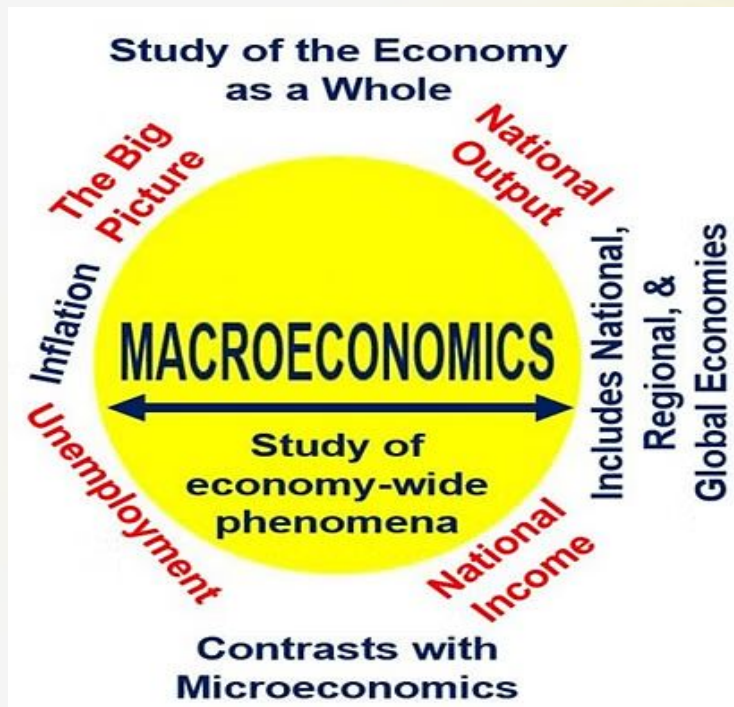
## **Economics**

*[e-kə-'nä-miks]*

A social science concerned chiefly with description and analysis of the production, distribution, and consumption of goods and services.

Branches of economics viz., Macroeconomics and Microeconomics.





# Branches of economics

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graph TD; A[Branches of economics] --> B[Microeconomics]; A --> C[Macroeconomics]; B --> B1[Neo-classical (free markets)]; B --> B2[Development economics]; B --> B3[Environmental]; B --> B4[Behavioural (psychology)]; B --> B5[Econometrics (maths)]; B --> B6[Labour economics]; C --> C1[Classical/free market]; C --> C2[Keynesian (gov't intervention)]; C --> C3[Marxist (state control)]; C --> C4[Austrian (free-market)]; C --> C5[Mercantilism (protectionism)]; C --> C6[Monetarist (free-market/control money)];
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## Microeconomics

Neo-classical (free markets)

Development economics

Environmental

Behavioural (psychology)

Econometrics (maths)

Labour economics

## Macroeconomics

Classical/free market

Keynesian (gov't intervention)

Marxist (state control)

Austrian (free-market)

Mercantilism (protectionism)

Monetarist (free-market/control money)

|                                |                     |  |  |
|--------------------------------|---------------------|--|--|
| CENTRAL PROBLEMS of an Economy | What to Produce     | Relates to Selection of goods to be produced                         |  |
|                                |                     | According to Market Analysis   |  |
|                                |                     | As Per Consumer's demand   |  |
|                                | How to Produce      | Relates to Selection of the technique of Production                  | Labour Intensive Technique <ul style="list-style-type: none"> <li>• Use of more Labour than Capital</li> <li>• Labour&gt;Capital</li> </ul>  |
|                                |                     |  | Capital Intensive Technique <ul style="list-style-type: none"> <li>• Use of more Capital than Labour</li> <li>• Capital&gt;Labour</li> </ul> |
|                                | For Whom to Produce | Relates to the part of the society for whom goods are to be produced | According to the distribution of Income  |
|                                |                     |  | According to the availability of resources   |







Meaning, salient features of Economic systems viz.,

- Market Economy,
- Socialist Economy,
- Communist Economy and
- Mixed Economy.

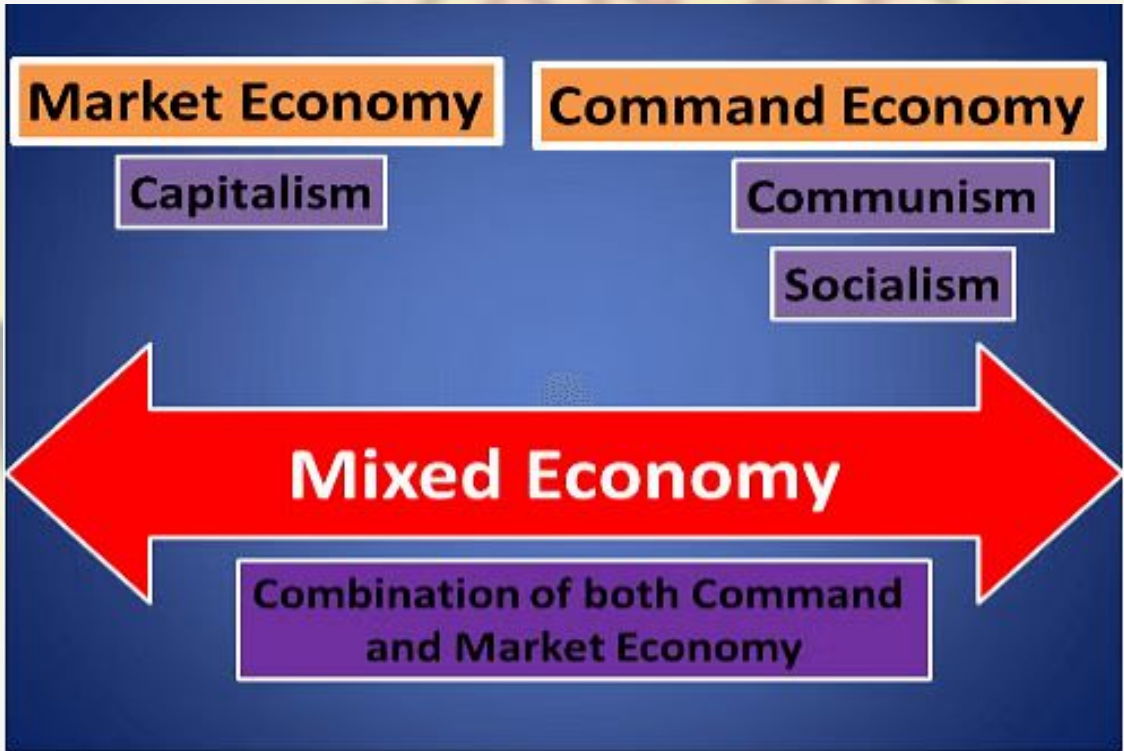


Five economic systems illustrate historical practices used to allocate resources

1. **Primitivism-** In primitive agrarian societies, individuals produced necessities from building dwellings, growing crops, and hunting game at the household or tribal level.
2. **Feudalism-** This was defined by the lords who held land and leased it to peasants for production, who received a promise of safety and security from the lord.
3. **Capitalism-** With the advent of the industrial revolution, capitalism emerged and is defined as a system of production where business owners organize resources including tools, workers, and raw materials to produce goods for market consumption and earn profits.
  - Supply and demand set prices in markets in a way that can serve the best interests of society.
4. **Socialism** is a form of a cooperative production economy.
  - Economic socialism is a system of production where there is limited or hybrid private ownership of the means of production.
  - In this system, prices, profits, and losses are not the determining factors used to establish who engages in the production, what to produce and how to produce it.
5. **Communism** holds that all economic activity is centralized through the coordination of state sponsored central planners with common ownership of production and distribution.



| PARAMETER              | CAPITALIST   | SOCIALIST                                     | MIXED   |
|------------------------|--|---|---|
| Ownership of Property  | Private  | public  | Both public and private   |
| Price Determination    | determined by the market forces of demand and supply | determined by the central planning authority. | determined by central planning authority and demand & supply.                   |
| Motive of Production   | Profit motive  | Social welfare                                | The profit motive in the private sector and welfare motive in the public sector |
| Role of Government     | No role  | Complete role                                 | Full role in the public sector and limited role in the private sector           |
| Competition            | Exists   | No competition                                | Exist only in the private sector  |
| Distribution of income | Very Unequal   | Quite Equal                                   | Considerable inequalities exist.  |







**Co-existence of  
Public and Private  
sector**



**Reduction of Economic  
Inequalities**



**Private property**



**Limited government**



**Government Protection  
of Labour**



**Freedom of choice**



**System of markets  
and prices**



**Consumers Sovereignty  
Protected**



**Motive of self interest**



**Competition**

## **CHARACTERISTICS OF MIXED ECONOMY**



**Government regulation  
and control over  
Private sector**



**Role of Price system  
and Government  
Directives**



**Existence of Economic  
Planning**





# Production Possibility Curve?



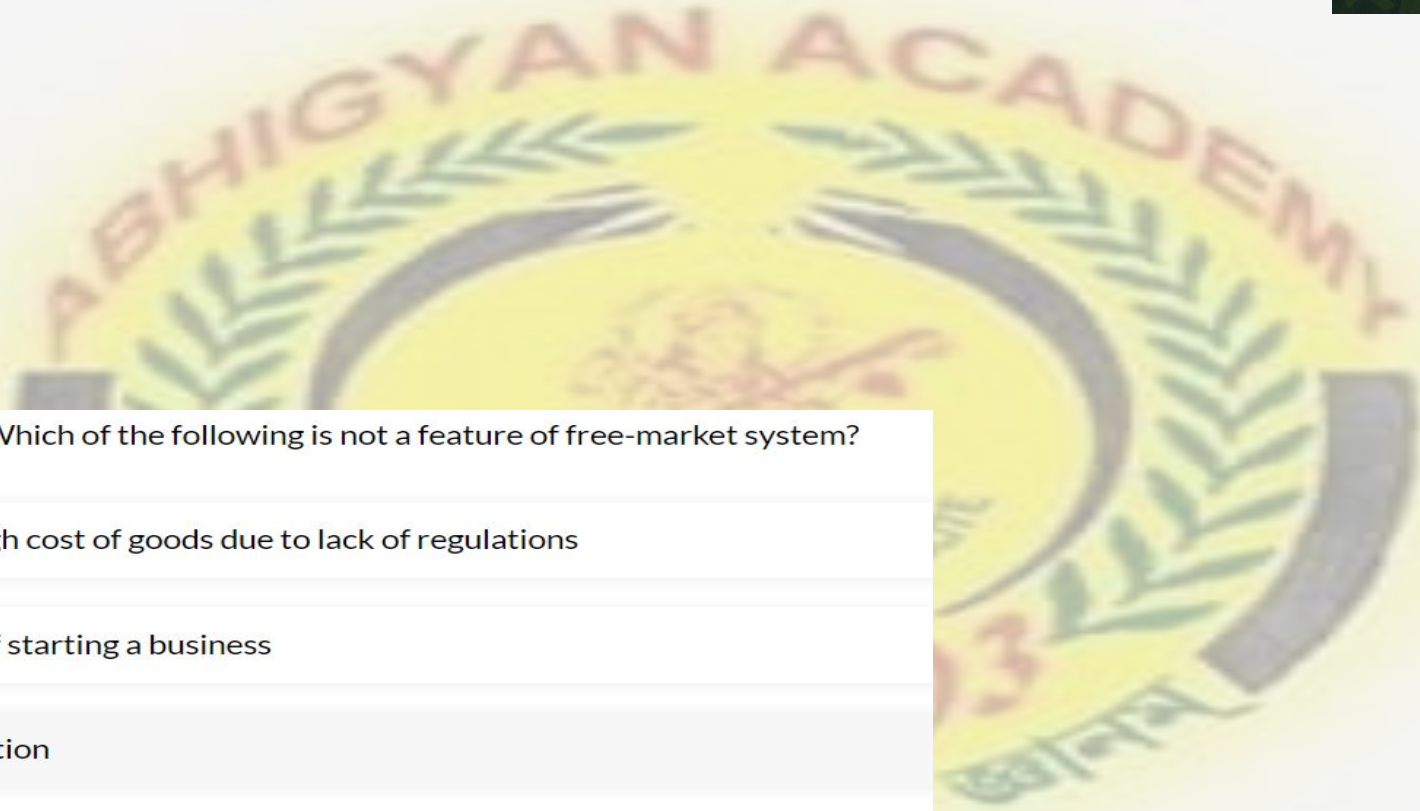
Economy Problem  
Resources limited  
Wants unlimited



Concave from origin- Opportunity

What to produce?  
How much to  
produce?





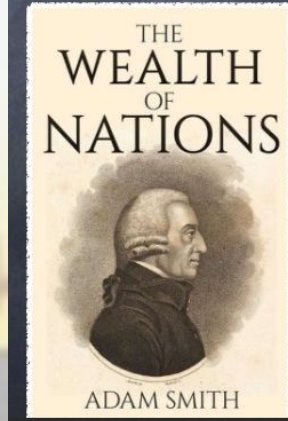
**Try yourself:** Which of the following is not a feature of free-market system?

- a.** The high cost of goods due to lack of regulations
- b.** Ease of starting a business
- c.** Innovation
- d.** Open Competition

## Other Classification

### 1. **Classical economics**

- Classical economics is often considered the foundation of modern economics. It was developed by Adam Smith, David Ricardo, Jean-Baptiste Say.
- It is based on:
  - Operation of free markets. How the *invisible hand* and *market mechanism* can enable an *efficient allocation of resources*.
  - Classical economics suggests that generally, economies work most efficiently when government intervention is minimal and concerned with the protection of private property, promotion of free trade and limited government spending.

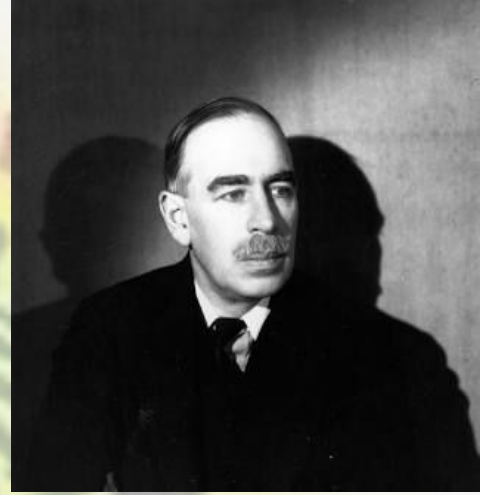






2. **Keynesian economics** was developed in the 1930s against a backdrop of the Great Depression.

- The existing economic orthodoxy was at a loss to explain the persistent economic depression and mass unemployment. Keynes suggested that markets failed to clear for many reasons (e.g. paradox of thrift, negative multiplier, low confidence). Therefore, Keynes advocated government intervention to kick-start the economy.



3. **Monetarist economics** → Led by Milton Friedman

- Monetarists promoted previous classical ideals, such as belief in the efficiency of markets. They also placed emphasis on the control of the money supply as a way to control inflation.

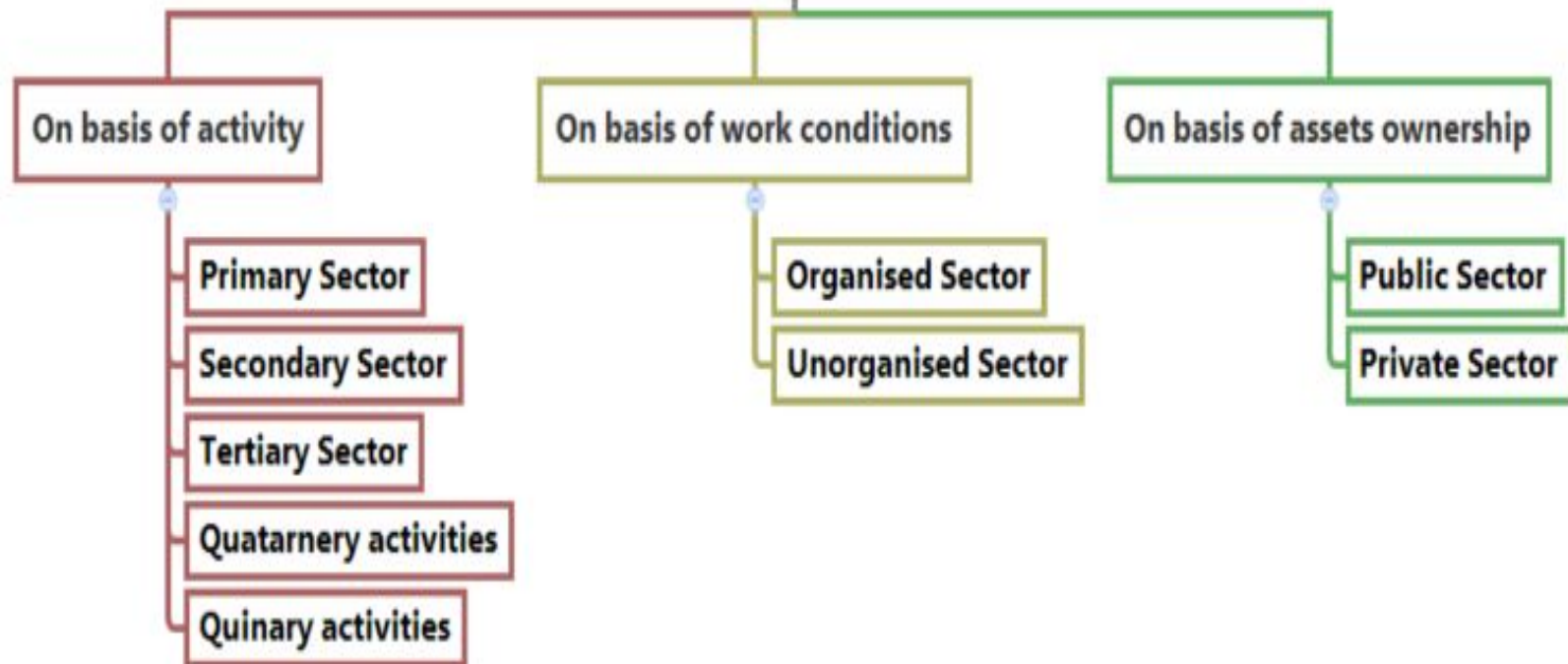


6. **Marxist economics**→ Emphasises unequal and unstable nature of capitalism. Rather than relying on free-market advocate state intervention in ownership, planning and distribution of resources. Radical approach
7. **Neo-liberalism/Neo-classical**→ A modern interpretation of classical economics. Considerable overlap with monetarism. Essentially concerned with the promotion of free-markets, competition, free trade, privatisation, lower government involvement, but some minimal state intervention in public services like health and education.

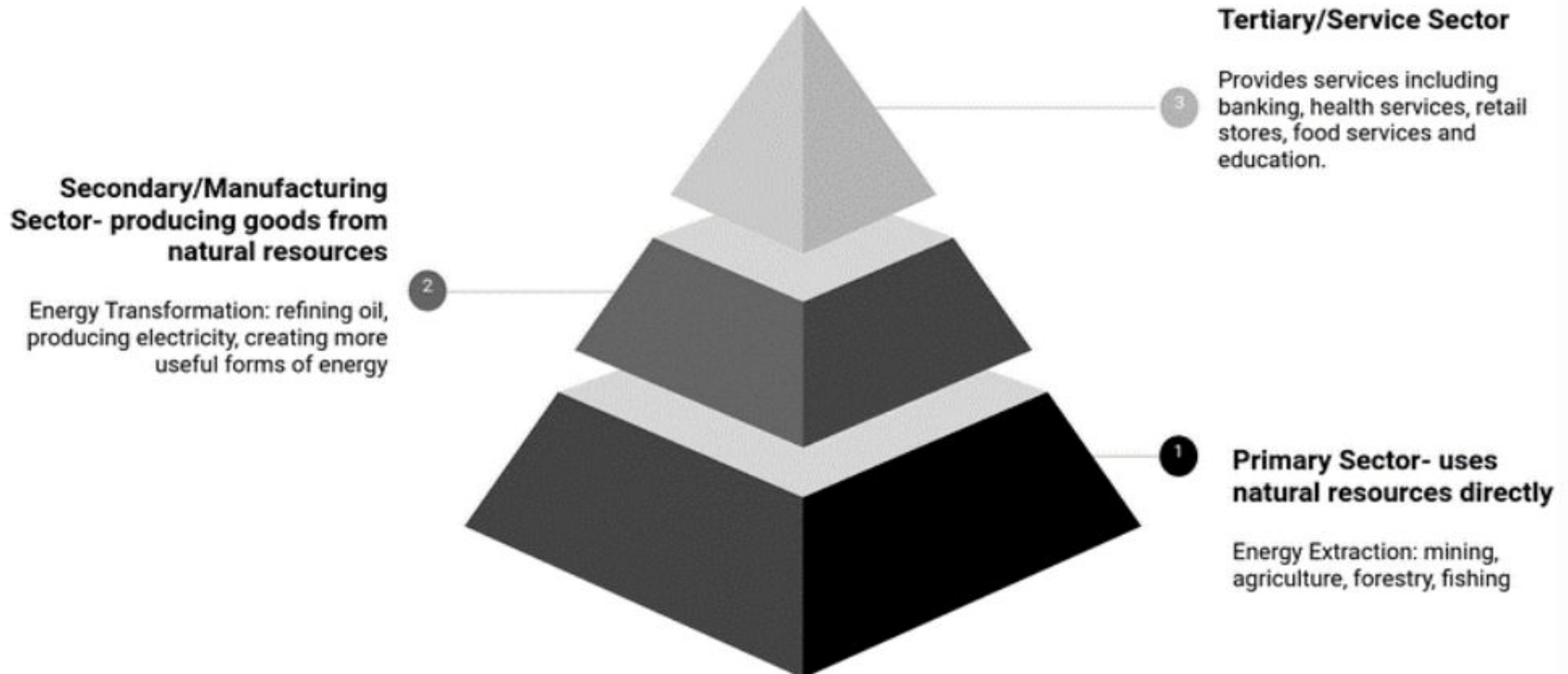
### New Branches of economics

1. **Environmental economics/welfare economics**
  - This places greater emphasis on the environment. This can include:
    - Market failures - tragedy of the commons, Public goods, external costs, external benefits.
    - Environmental economics can take a more radical approach - questioning whether economic growth is actually desirable.
2. **Behavioural economics**→ It examines the psychology behind economic decision making and economic activity.
3. **Development economics**→ Concerned with issues of poverty and under-development in poorer countries of the world. Development economics is concerned with both micro and macro aspects of economic development.
4. **Econometrics** uses statistical methods, regression models and data to predict the outcome of economic policies.
5. **Labour economics**→ Concentration on wages, labour employment and labour markets.

# India's Economic Sector

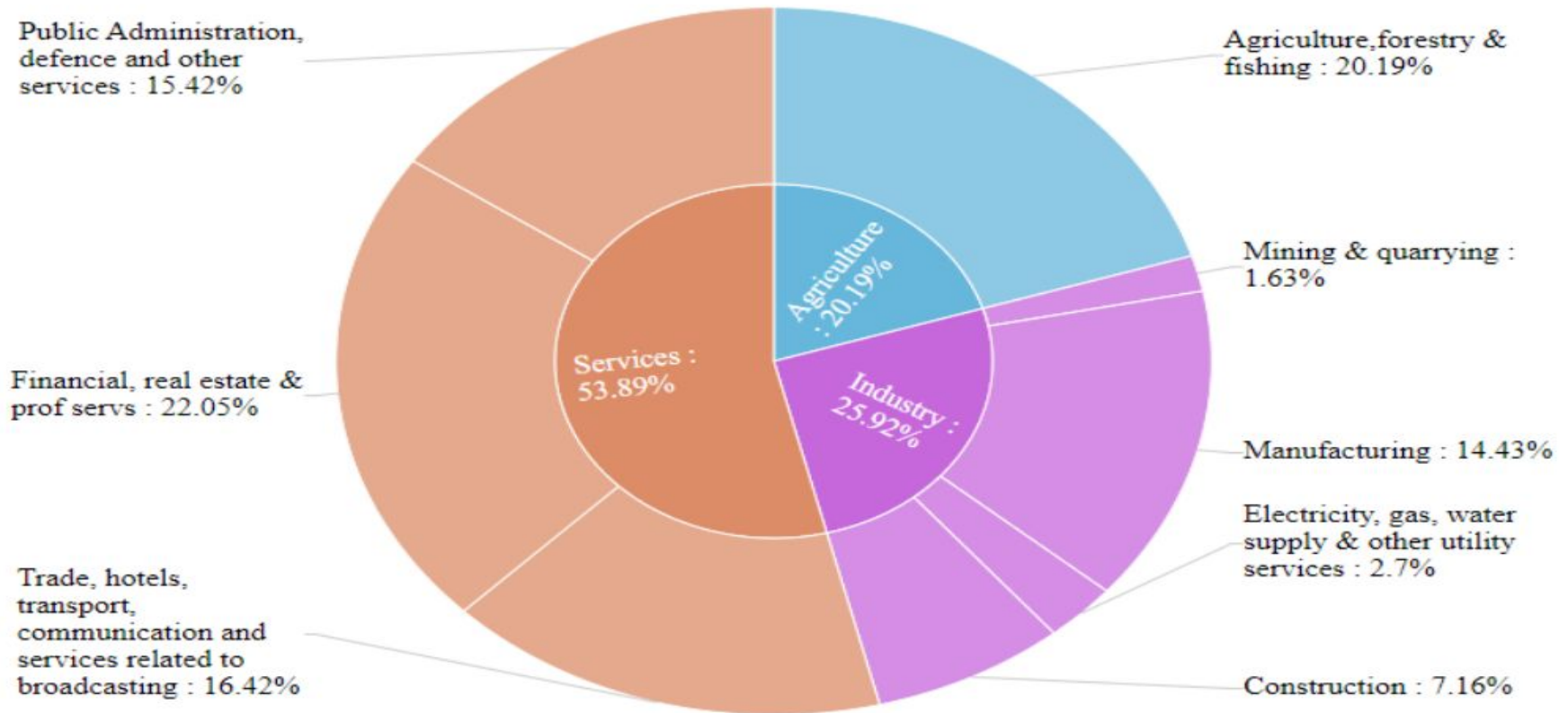


## *Different types of sectors in an economy*





## Sector wise contribution in India

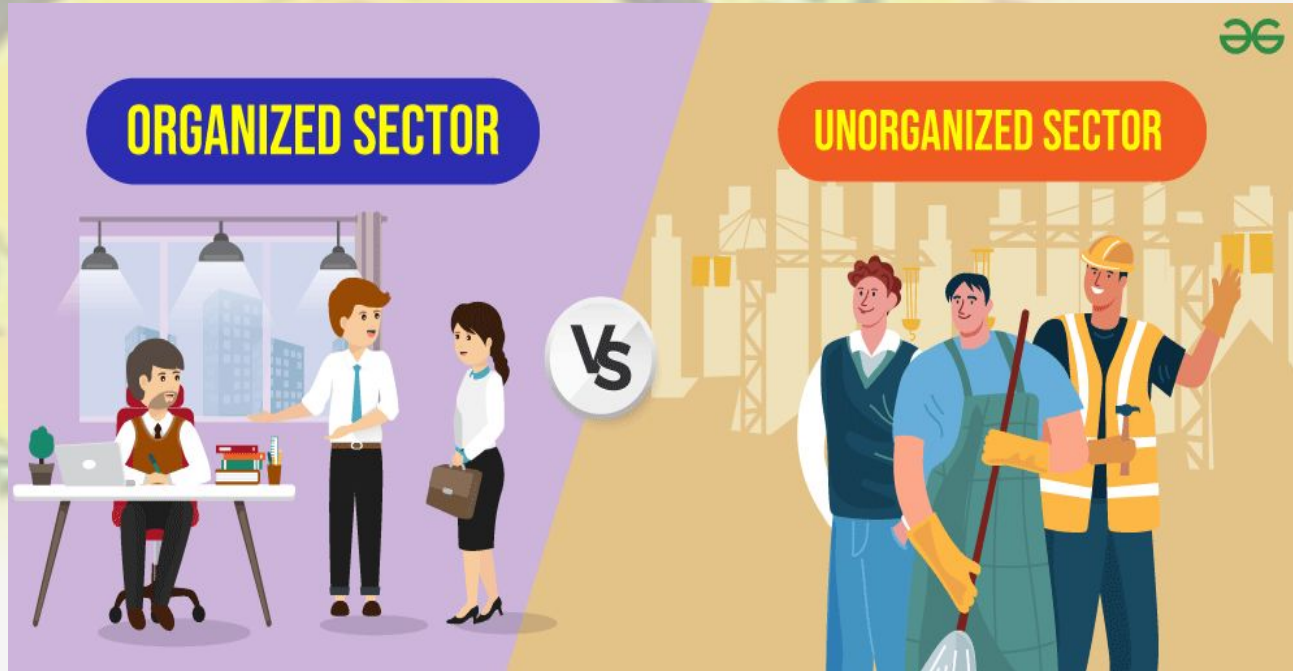


## Sectors in terms of Ownership

1. Public Sector
2. Private Sector

## Sectors on basis of Work Condition

1. Organised Sector
2. Unorganised Sector



# Difference between economic growth vs economic development



| <b>Economic Growth</b>   | <b>Economic Development</b>  |
|--|--|
| i) An increase in size of the Country's National income  | i) An increase in the size and quality of the country's National income  |
| ii) Number of people living in absolute poverty can increase despite the increase in national income | ii) Number of people living in absolute poverty does not increase  |
| iii) Increase in national income could be due to increase in income of only few people               | iii) Increase in national income is attributed to general increase of incomes of majority of the people in the country |
| iv) No tendency to bridge the gap between the rich and the poor                                      | iv) Tends to bridge the gap between the rich and the poor  |

UNDP introduced → HDI in its inaugural Human Development Report (HDR) in 1990.

HDI aimed to quantify and assess the level of development.

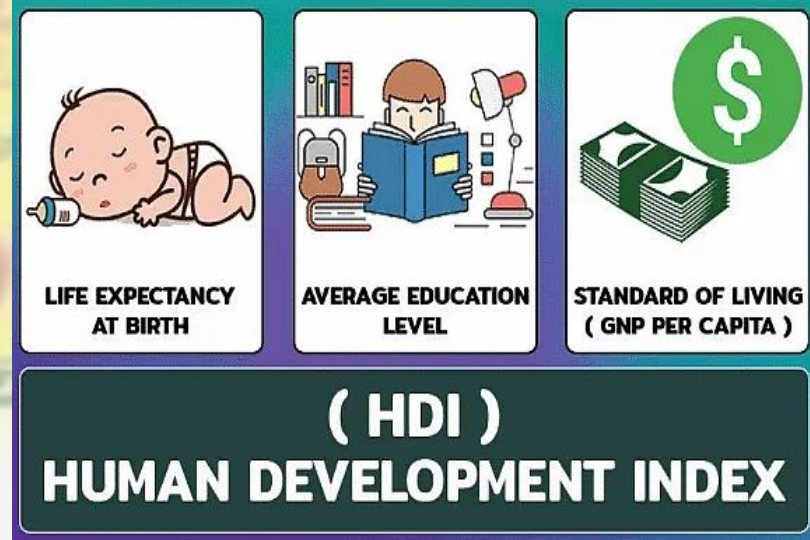
A team, led by Mahbub UI Haq and Ing Kaul, including scholars, and UNDP members, crafted this index.

HDI focuses on 'human development,' a concept related to general 'development.'

It considers three key factors, each with equal weight:

- Life expectancy
- Education (measured by literacy and school enrollment)
- Per capita income

These factors collectively gauge the development of countries featured in the report.





# Gross National Happiness

In the early 1970s, Bhutan introduced a unique development concept called Gross National Happiness (GNH), which complements the UNDP's human development approach. Since 1972, Bhutan has officially embraced GNH as its development framework. GNH prioritizes the following key parameters for achieving happiness and development:

- Increased real per capita income.

- Effective governance.

- Environmental conservation.

- Promotion of culture, emphasizing ethical and spiritual values, as essential elements for progress, ensuring it's a blessing rather than a curse.

# The concept of demand and supply in an economy



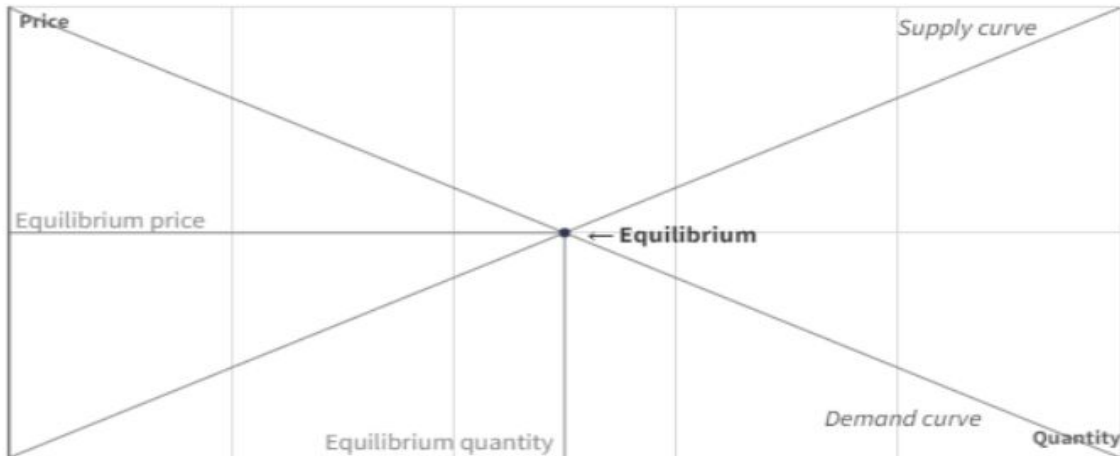
### Law of Demand

- The law of demand states that if all other factors remain equal, the higher the price of a good, the fewer people will demand that good
- The amount of a good that buyers purchase at a higher price is less because as the price of a good goes up, so does the opportunity cost of buying that good.

### Law of supply

- The law of supply demonstrates the quantities sold at a specific price.

### Law of Supply and Demand



## Factors Affecting Supply

Supply is largely a function of production costs, including:

- Labour and materials
- The physical technology available to combine inputs
- The number of sellers and their total productive capacity over the given time frame
- Taxes, regulations, or additional institutional costs of production.
- Competitors and Supply chains

## Factors Affecting Demand

These include:

- Consumer preferences among different goods
- The existence and prices of other consumer goods
- Changes in conditions that influence consumer preferences
- Changes in incomes can also be important in either increasing or decreasing the quantity demanded



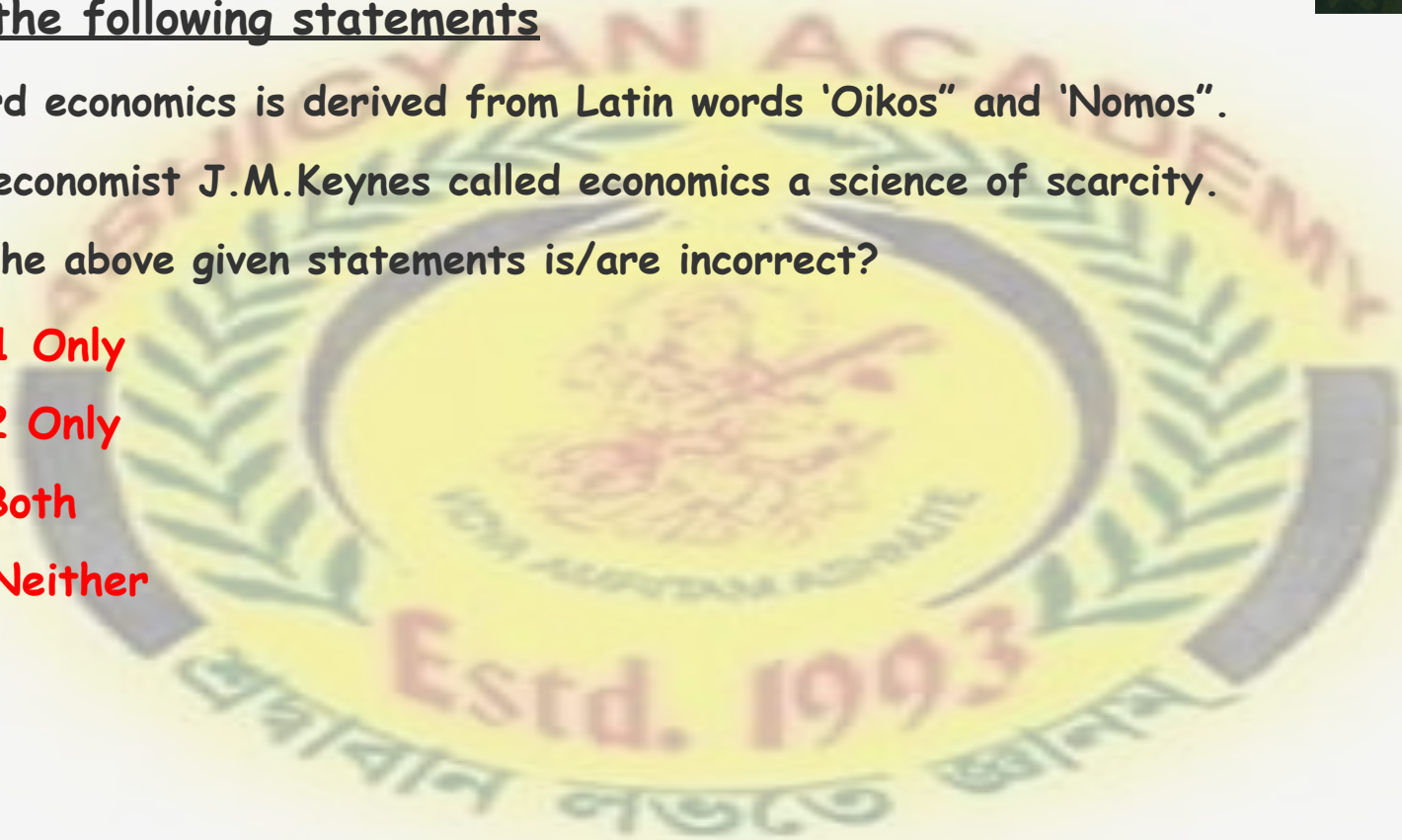


Consider the following statements

1. The word economics is derived from Latin words 'Oikos" and 'Nomos"'.  
2. British economist J.M.Keynes called economics a science of scarcity.

Which of the above given statements is/are incorrect?

- A. 1 Only
- B. 2 Only
- C. Both
- D. Neither



**'The general theory of Employment, Interest and Money' written by J.M.Keynes was published in**

- A. 1776      B. 1936      C. 1884      D. 1952

**The ministry which is responsible for GDP estimation is**

- A. Ministry of Finance
- B. Ministry of home affairs
- C. Ministry of commerce and industries
- D. Ministry of statistics and programme implementation

Which economic system led to increase in inequality, class conflicts and economic depressions?

- A. Capitalism      B. Communism      C. Mixed economy      D. Both a and b

Which of the following is not a characteristic of a command economy?

- A. Public ownership of means of production      B. State monopoly in economic sphere  
C. Prominence to customer's choice      D. Less impact of market forces like demand and supply

\_\_\_\_\_ provides better and cheaper goods and services to consumers but often leads to exploitation of workers.

- A. Free market economy      B. Command economy      C. Mixed economy      D. All of the above

The French word 'Laissez faire' means

- A. Hands off      B. Hands on      C. Hands around      D. No hands



The concept of 'collective ownership' of means of production is associated with which of the following?

- A. Only communism
- B. Only socialism
- C. Both a and b
- D. Neither

Which of the following is not a feature of capitalism?

1. Limited role of the government in economic activities.
2. Freedom of competition
3. Efficiency, innovation and creativity
4. Classless society

- A. 2 and 3
- B. 1 and 4
- C. Only 3
- D. Only 4

The concept of 'invisible hand' propagated by Adam Smith means

- A. Every person, by looking out for themselves, inadvertently helps to create the best outcome for all.
- B. A wealthy nation is one that is populated with citizens working productively.
- C. An institutional framework is necessary to steer humans toward productive pursuits that are beneficial to society.
- D. None of the above.

Which type of economy is also called 'dual economy'?

- A. Free market economy
- B. Socialist economy
- C. Communist economy
- D. Mixed economy





- Normal Goods - A good whose quantity demanded is directly proportional to the consumer income.
- Inferior Goods - A good whose quantity demanded is inversely related to the consumer income.
- By the way, classification of goods into normal and inferior is quite subjective.
- Complimentary Goods - a good whose appeal increases with the popularity of its compliment. For example : Car & Petrol ; Shoe & Polish etc.
- Substitute Goods - these are goods that a consumer perceives as similar or comparable, so that having more of one good causes the consumer to desire less of the other good. For example : Tea & Coffee ; Honda city & Hyundai Verna etc.



# Micro-economics BASIC TERMS

## WANT / Desire

- Primary (Basic)- Food shelter, Clothing
- Secondary: comfort, luxury

## Consumption

- Using goods/services To Satisfy WANTS
- Aggregate Demand, Std. Of Living.....

**DEMAND:** Willingness to buy @certain price @certain time

## Utility

- "Want" satisfying power of goods/services
- Marginal Utility...price equilibrium

## Production

- Making goods/ services that have "utility"
- 4 Factors of Production

Let's Solve this (UPSC's CDS- 2015 (1))

Demand of a particular commodity refers to

A.Desire

B.Need

C.Quantity demanded

D.Quantity demanded at certain price during a particular period of time.