Economics Module

Lecture 2

Anirban Dasgupta

Readings for economic measures

- Tim Callen (2017) Gross Domestic Product: An Economy's All
- Diane Coyle (2017) Rethinking GDP.

Widely used economic measures

- Gross Domestic Product: The monetary value of all final goods and services in an economy within a year/quarter
- Adding the value of all goods produced will lead to multiple counting
- Alternative method is to aggregate the value added at each stage of production
- A third method to arrive at GDP is to add up incomes received by all inputs of production – wages, rents, profits and interests
- GDP per capita is commonly used as a measure of welfare for a country
- Growth rates of GDP are also widely used as an index of economic performance (China, India as vibrant high growth economies as against other stagnant, low growth countries)

Comparing GDP across time and space

- Economic growth takes into account change in ‘real’ GDP i.e. accounting for change in prices.
- Across time comparison of GDP has to be made on the basis GDP deflated by price index.
- Comparing GDP across countries

 - converting GDP figures to common currency (e.g. convert INR to USD)

 - 5000 INR is $ 400

 - But purchasing power of a dollar is different in the US compared to Rs 80 in India

- For meaningful comparison, a purchasing power parity(PPP) adjustment needs to be made
- Typically, a poorer country like India will have a higher PPP adjusted GDP compared to a non-adjusted one.

Limitations of GDP as a measure of welfare

- It is mostly limited to marketed goods and services – household work mostly performed by women is not included
- Most of informal and illegal activities are not captured
- GDP can be increased through spending on war and conflict
- It does not take into account resource depletion and environmental degradation
- GDP per capita is an average measure and like any other measure of central tendency it ignores distribution (inequality is not captured at all)

Employment and unemployment

- Employment is considered another key indicator of macroeconomic health of a country
- Having access to gainful employment is critical for ensuring a decent quality of life for most people
- The employment situation is often tracked through unemployment rate
- Unemployment rate- the percentage of working age adults actively looking for employment(labour force) but not getting it at any given time.
- Some unemployment (3-4 %) is common across countries even when the economy is functioning well
- A higher unemployment rate implies an economic crisis or a recession.
- However, unemployment rate may not be a good indicator of economic distress in a poor country. Why?

Inflation and its relationship with unemployment

- Phenomenon of sustained increase in general price levels. Typically measured using general price index or consumer price index with a specific base year.
- A trade-off between inflation and unemployment was first identified by A. W. Phillips leading to the so-called (negatively sloped) Phillips curve
- The possible reason for this trade-off ?
- Policy implication was critical- targeting either high inflation or high unemployment and not both simultaneously
- However, the Phillips curve wisdom had been challenged repeatedly with situations of ‘stagflation’ i.e. economic stagnation or even recession in conjunction with high inflation.
- The current juncture in the global economy

Fiscal deficit and its role in macroeconomics

- Like any budget, government budget also has an income and an expenditure side
- Broadly, fiscal deficit is a measure of the excess of government spending over income (see different heads on each side in the next slide)
- Typically fiscal deficit is measured as a % of GDP and fiscal austerity implies have a strict limit on this percentage
- Is spending more than income a sustainable policy alternative for governments
- The dominant neoclassical position is no. Growing fiscal deficit leads to inflation and more generally into economic instability
- The Keynesian position is yes, especially if government spending is used as investment and job creation
- The New Deal as a means of overcoming the Great Depression

	Receipts	Expenditure
	1. Tax Revenue (Income, Customs,VAT)	4.Tax shared with state governments
	2. Non-tax revenue (dividends, charges, fees)	5.Salaries and materials on all government programmes (health, education, irrigation – and defence)
Revenue Deficit/Surplus (Difference)	3. Interest received on loans given Difference between revenue receipts and expenditure	6. Interest paid on loans
Capital Account		
	7. Loans Repaid by states, PSUs	10. Grants to local governments
	8. Sale of Assets	11. Investment in assets, PSUs
	9. Loans from market	
FISCAL DEFICIT	**Difference between total receipts and total expenditure(other than item 9)**	

Structural Transformation

Sustained Economic Growth is accompanied by:

- Declining share of agriculture in GDP and Employment (main characteristic)
- Migration from rural to urban sector and rapid urbanisation
- Rise of a modern industrial and service sector
- Demographic transition from high birth and death rates to low birth and death rates
- At the completion of the transformation process there is near equalisation of labour productivity in the agricultural and non-agricultural sectors
- At this stage, returns from employment become sufficiently high across sectors

Structural transformation in India (Nigam, 2021)

Post-Reform Growth in India and C

- Primary sector: agriculture
- Secondary sector: industry
- Tertiary sector: services

Table 5

Year	% Share in GDP			% Share in Total Employment		
	Primary	Secondary	Tertiary	Primary	Secondary	Tertiary
1983	41.60	28.36	33.72	66.41	14.50	19.09
1987	35.53	29.47	38.27	62.45	16.76	20.79
1993	33.60	29.48	40.79	61.67	15.66	22.67
1999	27.58	29.38	44.74	58.60	16.68	24.72
2004	22.64	30.50	46.86	53.96	19.49	26.56
2011	18.53	32.50	48.97	45.64	24.91	29.45
2017	14.90	31.22	53.88	41.06	25.70	33.24

Source: Own calculations based on CSO and NSS data, various years, and PLFS (2017–18).