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INDIAN ECONOMY

CHAPTER 3

National Income

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CHAPTER 3

National Income

GDP, GNP, NNP and Other Measures of Growth

IN THIS CHAPTER

- Meaning of National Income
- Important Definitions
- Measures of National Income
- Methods of Computing National Income
- Other Measures of Welfare

Meaning of National Income

Simon Kuznets gave the idea of national income in **1934**.

National income is the total money value of all **final goods and services** produced in an economy during a specific period of time.

- It includes both the **public** and **private** sectors.
- It covers everything from haircuts to housing, and from medical care to national defence.
- National income is commonly expressed as **Gross Domestic Product (GDP)**.

Important Definitions

Domestic / Economic Territory

The geographical territory administered by the Government of India, within which persons, goods and capital can move freely.

> **Foreign embassies in India are NOT** part of India's domestic territory. **Indian embassies abroad ARE** part of India's domestic territory.

Market Price (MP)

- The price a consumer pays to buy a product from the seller, i.e., the price at which a product is sold in the market.
- Market Price **includes indirect taxes** (added to the selling price) and **excludes subsidies** (deducted from the selling price).

Factor Cost (FC)

- The cost of factors of production incurred by a firm to produce goods and services, i.e., the cost of producing a good or service.
- Factor Cost **excludes indirect taxes** but **includes subsidies**.

Factor Cost (FC) = Market Price – Indirect Taxes + Subsidies

Nominal Price (Current Price)

The market price of a good or service in the **current year**. Since inflation is included in the current price, the nominal price changes with the current level of inflation.

Base Price (Constant Price)

To compare national income of different years, it is calculated with reference to a fixed year called the **Base Year**. The market price in the base year is called the **Base Price** or **Constant Price**.

Depreciation

Also called **Consumption of Fixed Capital**. It is the loss in value of fixed assets (e.g., cars, mobiles, TVs, machines) due to **wear and tear, accidental damage and obsolescence**.

Net Factor Income from Abroad (NFIA)

The difference between factor income (rent, wages, interest and profit) earned by normal residents of India abroad and factor income earned by non-residents in India.

NFIA = Factor Income from Abroad to India – Factor Income from India to Abroad

Transfer Payments

- One-sided (unilateral) payments for which **no goods or services** are exchanged.
- Examples: scholarships, gifts, donations.
- Transfer payments are **not included** in National Income.

Capital Output Ratio (COR)

- The amount of capital (investment) needed to produce **one unit of output**.
- It reflects the efficiency of an economy: the **higher the COR, the lower the efficiency**, and vice versa.

COR = Capital / Output

Incremental Capital Output Ratio (ICOR)

The additional capital needed to produce an **additional** unit of output.

ICOR = Incremental Capital / Incremental Output

Measures of National Income

The main measures are **Gross Domestic Product (GDP)** and **Gross National Product (GNP)**.

Gross Domestic Product (GDP)

GDP measures the total production of **final goods and services** produced **within the domestic territory** of a country during a year. Two key phrases:

- **Final goods and services:** only final goods are counted, not intermediate goods.

- **Within the domestic territory:** production by resident citizens as well as **foreign nationals** living within the country's boundary is counted.

GDP = C + I + G + NX

Where **C** = consumption by people living in India, **I** = investment, **G** = government spending, and **NX** = net exports (**Exports – Imports**).

GDP at Market Price (GDP MP)

- Market value of all final goods and services produced within the domestic territory in one financial year.
- **Includes indirect taxes, excludes subsidies.**

GDP at Factor Cost (GDP FC)

- Total income earned by the factors of production: **land, labour, capital and entrepreneurship**.
- **Excludes indirect taxes, includes subsidies.**

GDP FC = GDP MP – Indirect Taxes + Subsidies

Real GDP and Nominal GDP

Basis	Real GDP	Nominal GDP
Prices used	**Constant prices** (base year prices)	**Current market prices**
Inflation	**Not included**	**Included**
Formula	Real GDP = GDP at Constant Price	Nominal GDP = GDP at Current Price

GDP Deflator

The ratio of Nominal GDP to Real GDP. Since it compares national income at current prices with that at base-year prices, it is a **measure of inflation**.

GDP Deflator = Nominal GDP / Real GDP

New Series of GDP

- In **2015**, the government shifted the base year from **2004-05 to 2011-12**, and started measuring GDP at **market prices** instead of factor cost.
- On **27 February 2026**, a new GDP series with base year **2022-23** was released. India now uses **2022-23** as the base year for calculating national income.

> **REMEMBER**
>
> Current GDP base year: **2022-23** (released 27 February 2026). Previous base years: 2011-12 and 2004-05.

Gross National Product (GNP)

GNP is the total value of all final goods and services produced in a given period by the **citizens of a country** (wherever they are).

- **Final goods and services:** only final goods are counted.
- **Owned by a country's citizens:** production by resident and **non-resident citizens** is counted, but production by **foreign nationals** living in the country is **not** counted.

GNP = GDP + Net Factor Income from Abroad (NFIA)

Difference between GDP and GNP

Basis	GDP	GNP
Defines economy by	**Territory**	**Citizens**
Measures	Production within the domestic territory	Production by the citizens of the country

Gross Value Added (GVA)

GVA is the value of output minus the value of intermediate consumption. It shows the contribution of **labour and capital** to production.

GVA = GDP – Indirect Taxes + Subsidies

Net National Income (NNI)

NNI is Gross National Income **minus depreciation**. Its main measures are NDP and NNP.

Net Domestic Product (NDP) = GDP – Depreciation
Net National Product (NNP) = GNP – Depreciation

Methods of Computing National Income

National income (GDP or GNP) is calculated by three methods:

1. **Income Method**
2. **Expenditure Method**
3. **Production Method** (also called Value Added Method or Output Method)

Other Measures of Welfare

Gross National Happiness (GNH)

- Measures not only economic output but also environmental impact, spiritual and cultural growth, mental and physical health, and the strength of corporate and political systems.
- The term was coined by **Jigme Singye Wangchuck**, the **King of Bhutan**, in the early **1970s**.

Gross Sustainable Development Product (GSDP)

- Measures the economic impact of environmental and health degradation or improvement, resource depletion, and the effect of human activity on the environment.
- Developed by the **Global Community Assessment Centre** and the **Society for World Sustainable Development**.

Human Development Index (HDI)

A summary measure of average achievement in three dimensions:

Dimension	Measured through
Health	Life expectancy at birth
Education	Mean years of schooling and Expected years of schooling
Standard of Living	Gross National Income per capita (PPP basis)

- Developed by Pakistani economist **Mahbub ul Haq** with Indian economist **Amartya Sen**.
- Published every year by the **UNDP** in its **Human Development Report**.

Green GDP

GDP adjusted for **environmental damage** (such as biodiversity loss and climate change). It shows economic growth with environmental factors taken into account.

QUICK REVISION

1. Simon Kuznets gave the concept of national income (1934).
2. FC = MP – Indirect Taxes + Subsidies.
3. Foreign embassies in India are not part of India's domestic territory.
4. GDP = C + I + G + (Exports – Imports).
5. GDP = territory based; GNP = citizen based; GNP = GDP + NFIA.
6. NDP = GDP – Depreciation; NNP = GNP – Depreciation.
7. GDP Deflator = Nominal GDP / Real GDP (a measure of inflation).
8. Current GDP base year is 2022-23.
9. GNH – Bhutan; HDI – Mahbub ul Haq and Amartya Sen, published by UNDP.
10. Three methods: Income, Expenditure and Production (value added).