Lucknow IAS Academy

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Economy: An Introduction (NCERT Summary- Class IX to Class XII)

Chpater1: Economy: An Introduction

A framework in which all the economic activities are carried out in the form of investment, production and consumption, is termed as economy.

Types of Economy

There are various classifications in relation to types of economy. Economies can be of various types as follows:

1. On the Basis of Ownership and Management of Resources

On the basis of ownership and management of resources, economies can be classified into **Capitalist Economy, Socialist Economy and Mixed Economy.**

Capitalist Economy: In this type of economy, the private enterprises are the main spheres of production. They control the operation of the price mechanism by which buyers and sellers determine what goods and services will be bought and sold in the market, in what quantities and at what prices.

The means of production in the capitalist economy are controlled by private owners, who operate for their private profit or gain. United States of America and United Kingdom are examples of capitalist economy.

Socialist Economy In this type of economy, there is existence of public enterprise or state ownership of capital in all the important sector of productive activity. In the place of free operation of market forces, the socialist economies depend on state planning of production and distribution. China and Russia are examples of a socialist economy.

Mixed Economy In this type of economy, some of the important enterprises engaged in production are owned by the government but other enterprises have private owners. India is the example of a mixed economy.

India's Mixed Economy Model

In India, all three sectors coexist, i.e. private sector, public sector and joint sector. The joint sector is jointly run by the government and private companies, with at least 51% ownership belonging to the state.
The government can regulate and direct the working of private enterprise in India to safeguard public interest through different provisions of the law.

2. On the Basis of Development

On the basis of economics development, economies can be classified into Developed rooms, Developing Economies and Less Developed Economies.

Developed Economy it is also called as industrialised economy. This economy has advanced technological infrastructure and diverse industrial and service sectors.
Countries which had been industrialised since long time like USA, UK, France, Japan, Koreas and other newly Industrialised countries of Asia are the examples of developed economy.

Developing Economies In this type of economy, the modern industrial sector, keeps increasing in size and the traditional agricultural or rural sector keeps shrinking. It has a low socio-economic indicators and moderate Human Development Index as compared to other developed countries. China and India are the examples of developing economy.

Less Developed Economy: According to the United Nations, this type of economy include developing economies that exhibit the lowest indicators of socio-economic development, with the lowest Human Development Index ratings of all countries in the world. The poorer countries are generally described as Less/Least Developed Countries (LDCs).

- They have relatively very small industrial sectors. They also have very little access to modern technology whether in industry or agriculture.
- Bangladesh, Niger, Central African Republic, South Sudan, Chad, Burundi, Sierra Leone, Burkina Faso, Mali, etc. are the examples of less developed economy.

3. On the Basis of Trade

On the basis of trade, economies can be divided into Open Economy and Closed Economy.

Open Economy It refers to a market economy, which is generally free from trade barriers and where exports and imports form a large percentage of the Gross Domestic Product (GDP).
The degree of openness of an economy determines a government's freedom to pursue economic policies of its choice and the susceptibility of the country to international economic cycles.
India after 1991 economic reforms, Chile and Argentina are the examples of open economy.

Closed Economy It refers to an economy in which no activity is conducted with other economies. It is self-sufficient, where no imports are brought in and no exports are sent out. The goal is to provide consumers with everything that they need from within the economy. India before 1991 economic reforms, is the example of closed economy.

Size of Indian Economy

- As per the Economic indicators, India is 5th largest economy of the world. On the basis of Purchasing Power Parity (PPP), India is 3rd largest economy of the world after USA and China.
- According to the UNCTAD's 2024 World Investment Report, India is the world's fifth largest hub for foreign investment (FDI). The report ranks India fifth, with the US at first, China at second, and Hong Kong at third.
- In 2021-2022, India received $83.57 billion in FDI, the highest ever annual inflow. In 2022-2023, FDI inflow was estimated to be $71 billion.

Economics

Economics is the study of labour, land and investments of money, income, production, taxes and government expenditures. Adam Smith is known as **'Father of Economics'**.

Activities in Economics

In order to fulfill desires of day-to-day life, people keep themselves engaged in different types of activities, which are as follows:

Economic Activities: The activities which create economic or financial gain by producing goods or services are known as economic activities. e.g., doctor, teacher, businessmen, etc.

Non-Economic Activities: The activities done not for earning money or any consideration of economic gain are known as non-economic activities. e.g., social services, political services, religious services, etc.

Branches of Economics

Economic analysis is usually divided into two main branches of economics **i.e., Macroeconomics and Microeconomics.**

Macroeconomics: It is concerned with problems of an economy as whole rather than individual facts and problems. e.g., National Income, employment, poverty, Balance of Payments, inflation, etc.

Microeconomics: It studies economic activities at micro level. It examines the economic behaviour of individual units such as consumers, businessmen, etc. to understand how decisions are made in the situation of scarcity and effects of these decisions on the economy.

Sectors of Economy

An economy is divided into three parts or sectors on the basis of economic activities. These activities are broadly grouped into Primary, Secondary and Tertiary sectors.

Primary Sector

- It is directly related to the extraction or utilisation of natural resources. It comprises economic activities like agriculture, mining, fishing, dairy, quarrying, etc.
- Products of primary sector do not undergo for major processing of change and are used or traded as natural products itself.
- This sector is also known as the Agriculture and Allied Sector.
- The Agriculture sector is at the third place with the contribution of 20.19% in GDP.

Secondary Sector

- It utilises the end product of the primary sector, to manufacture finished goods, through the refinement and processing of the primary products.
- It comprises construction, manufacturing, electricity, gas and water supply, etc related works.
- This sector is also known as the Industrial Sector.
- The Industry sector lags behind Service Sector with the contribution of 25.92% in GDP.

Tertiary Sector

- It provides services, instead of goods to other sectors. Thus, this sector is sometimes referred to as the Service Sector.
- Business, transport, telecommunication, banking. insurance, etc are associated with the sector.
- In India, the Service Sector accounts for almost 54% of India's GDP contribution.

Others Sectors of Economy

Quaternary Sector: The quaternary sector consists of those industries providing information services, such as computing, ICT (Information and Communication Technologies), consultancy (offering advice to businesses) and Research and Development, particularly in scientific fields.

Quinary Sector: Economists further narrow the quaternary sector into the quinary sector, which includes the highest levels of decision-making in a society or economy. This sector includes top executives or officials in such fields as government, science, universities, healthcare, culture and media.

Sunrise Sector: A sunrise sector is a business or industry that is growing rapidly and has the potential to generate a lot of wealth and employment. Typically, the sunrise industries are characterized by high growth rates, numerous start-ups, and a wealth of venture capital funding.

Features of Indian Economy

The features of Indian economy can be categorised as **traditional and modern features.**

Traditional Features of Indian Economy The traditional features of Indian economy are as follows:

Dominance of Agriculture As per the Economic Survey 2022-23, 47% of the working population of the country is engaged in agriculture and agriculture share in the Gross Domestic Product (GDP) is 15%. This share is one of the highest in India's Gross Domestic Product. In India, other sectors are also developing quiet fast, but agriculture still remains most employable sector of the country.
Low Per Capita Income: Low level of Per Capita Income is one of a major dilemma in the development of the country, due to the increasing population of the country. Due to lower levels of Per Capita Income, it gave rise to poverty in India.

Rural Economy According to Census 2011, 67% of India's population lives in rural areas which shows the rural population is quiet high. In developed economies, the percentage of rural population is quite low.

High Population Continuous and fast rising population makes the Indian economy weak. Between 2010 to 2011, the population rise in India was 17.64%. Due to rise in population, stress in the available resources is created. If a country has limited or less population, then there is a greater chances of decrease in social inequality that benefits larger masses.

Unemployment In India, there is a huge amount of workforce, but employment opportunities are few. In such a situation, it becomes very difficult to provide employment to everyone. Due to more population engaged in agriculture sector that is needed, it affects the productiveness of the country. In India, more human resource is engaged in agriculture than any other sectors.

Inequality in Income Distribution:

- There is a huge inequality in distribution of income and property in India that gives rise to problem of poverty and unemployment. Due to progressive taxation system in developed countries, there are low income inequalities.
- Equal opportunities of social security, education, training and employment decrease the scope of income inequality in an economy.
- According to the World Inequality Report 2022, India is among the most unequal countries in the world, with the top 10% and top 1% of the population holding 57% and 22% of the total national income respectively. The share of the bottom 50% has gone down to 13%.

Modern Features of Indian Economy

The modern features of Indian economy are as follows:

- Planned Economy In India, the phase of planned economy started from establishment of Planning Commission and preparing of Five Years Plan. In between 1951 and 2017, 12 Five Years Plan have been prepared so far. NITI Aayog was established on 1st January, 2015. At present, this organisation is responsible for preparing both short-term and long-term development plans.
- **Industrial Development** In many Five Years Plans, establishment of industrial plans gave rise to the industrial development in India.
- In the year 1991, the process of liberalization, privatization and globalization also began for development along with the initiation of 'New Economic Policies'. This gave rise to the industrial development in India.

Economic Development

In economic growth, the concept of social justice and fair distribution is termed as Economic Development. It is a qualitative concept.

Indicators of Economic Development

Alternative indicators have been developed by different national and international organisations to provide better measures of a nation's quality of life. These include:

- The Human Development Index (HDI)
- Multi-dimensional Poverty Index (MPI)

- World Happiness Report (WHR)
- Gender Inequality Index (GII) Global Hunger Index (GHI)

Each of these indexes is a composite measure weighing both income and non-income variables such as life expectancy, literacy rates, environmental indicators, measures of inequality and so on. By including these variables, they provide a measure of life quality that goes beyond the narrowness of a nation's GDP value.

1. **Human Development Index (HDI)**

The United Nations Development Programme (UNDP) introduced the HDI in its first Human Development Report (HDR), prepared under the stewardship of Mahbub-ul-Haq in 1990. HDR, 1990 defined human development as the process of widening people's choices as well as raising the level of well-being achieved.

Three main indicators of HDI are as follows:

- **Life Expectancy Index (LEI)** Infant mortality is not considered as a separate indicator in this index. Thus, life expectancy refers to life expectancy at birth, not at age one.
- **Educational Attainment Index (EAI)** It is a combination of adult literacy rate and combined enrolment ratio. The weight assigned to Adult Literacy Rate (ALR) is two-third while for Combined Enrolment Ratio (CER) is one-third.
- **Standard of Living Index (SLI)** It is represented here by the concept of Purchasing Power Parity (PPP). Per Capita Income is converted into Purchasing Power Parity in terms of US dollar. It is also known as GDP Index. The value of HDI is scaled on 1 to 0, where 1 represents the best and 0 (zero) represents the worst.

After a drop in its Human Development Index (HDI) value in 2021 and following a flat trend over the past few years, India's HDI value has increased to 0.644 in 2022, placing the country 134 out of 193 countries and territories in the just released 2023/24 Human Development Report (HDR) titled, "Breaking the Gridlock: Reimagining Cooperation in a Polarized World."

2. Multi-dimensional Poverty Index (MPI)

The Multi-dimensional Poverty Index was launched by the United Nations Development Programme (UNDP) and the Oxford Poverty and Human Development Initiative (OPHI) in 2010.

MPI is based on the idea that poverty is not unidimensional (not just depends on income and one individual may lack several basic needs like education, health etc.), rather it is multi-dimensional.

The index shows the proportion of poor people and the average number of deprivations each poor person experiences at the same time.

MPI uses three dimensions and ten indicators are as follows:

1. **Education Years of schooling and child enrollment.**
2. **Health Child mortality rate and nutrition.**
3. **Standard of living Electricity, flooring, drinking water, sanitation, cooking fuel and assets.**

A person is multi-dimensionally poor if she/he is deprived in one third or more (means 33% or more) of the weighted indicators (out of the ten indicators). Those who are deprived in one half or more of the weighted indicators are considered as living in extreme multi-dimensional poverty.

3. World Happiness Report (WHR)

- The phrase 'Gross National Happiness' was first coined by the fourth King of Bhutan, King Jigme Singye Wangchuck, in 1972.
- The concept implies that sustainable development should take a holistic approach towards notions of progress and give equal importance to non-economic aspects of wellbeing.
- The World Happiness Report ranks 149 countries by how happy their citizens perceive themselves to be.
- The rankings are based on polling (Gallup World Poll), which looks at six variables:

i. Gross Domestic Product Per Capita (Purchasing Power Parity)
ii. Social Support
iii. Healthy life expectancy at birth
iv. Freedom to make life choices
v. Generosity
vi. Perceptions of corruption

4. Gender Inequality Index (GII)

It measures gender inequalities in following three Important aspects of Human Development:

1. Reproductive health, measured by maternal mortality ratio and adolescent birth rates;
2. Empowerment, measured by proportion of parliamentary seats occupied by females and proportion of adult females and males aged 25 years and older with at least some secondary education;

3. Economic status, expressed as labour market participation and measured by labour force participation rate of female and male populations aged 15 years and older.

India was ranked 127 out of 146 countries in the **Global Gender Gap Report, 2023**, and faces the perennial issue of "missing women" from the workforce – which is a wicked problem.

5. Global Hunger Index (GHI)

This index is jointly published annually by Concern Worldwide and Welthungerhilfe. It was first prepared in 2006 and is published in every year in October. The 2023 Global Hunger Index gives India a rank of 111 out of 125 countries.

It is calculated on the basis of four indicators:

1. Under nourishment Share of the population with insufficient caloric intake.
2. Child Wasting Share of children under the age of five who have low weight for their height, reflecting acute undernutrition.
3. Child Stunting Share of children under the age of five who have low height for their age, reflecting chronic undernutrition.
4. Child Mortality The mortality rate of children under the age of five.

- Based on the values of the four indicators, the GHI determines hunger on a 100-point scale, where zero is the best possible score (no hunger) and 100 is the worst.
- Each country's GHI score is classified by severity, from low to extremely alarming.

Human Capital and Human Development

The two terms sound similar but there is a clear distinction between them.

Human Capital

- Population becomes human capital, when there is investment made in the form of education, training and medical care.
- Human capital considers education and health as a means to increase labour productivity.
- In fact, human capital is the stock of skill and productive knowledge embodied in them.
- People as Resource' is a way of referring to a country's working people in terms of their existing productive skills and abilities.
- When the existing 'human resource' is further developed by becoming more educated and healthy, we call it human capital formation' that adds to the productive power of the country just like 'physical capital formation'

Sources of Human Capital

- Investment in education is considered as one of the main sources of human capital.
- There are also several other sources such as investments in health, on the job training, migration and information are the other sources of human capital formation.

Difference between Human Capital and Physical Capital

Physical Capital	Human Capital
Physical capital is tangible and can be easily sold in the market like any other commodity.	Human capital is intangible, it is endogenously built in the body and mind of its owner.
The physical capital is separable from its owner.	Human capital is inseparable from its owner.
Physical capital is completely mobile between countries except for some artificial trade restrictions.	Human capital is not perfectly mobile between countries as movement is restricted by nationality and culture.

Human Capital and Economic Growth

- Human capital allows an economy to grow. When human capital increases in areas such as science, education and management it leads to increase in innovation, social well-being, equality, increased productivity, improved rates of participation, etc. All of these contribute to economic growth.
- The causality between human capital and economic growth flows in either direction. That is, higher income causes the building of a higher level of human capital and vice versa, that is, high level of human capital causes growth of income.
- India recognised the importance of human capital in economic growth long ago. The Seventh Five Year Plan says, "Human resources development has necessarily to be assigned a key role in any development strategy, particularly in a country with a large population."

Human Development

Human development is based on the idea that education and health are integral to human well-being. Only when people have the ability to read and write along with the ability to lead a long and healthy life, then they will be able to make other choices, which they value.

Economic Growth

- It is an increase in the production of goods and services in an economy.
- It is a quantitative concept. It means an increase in real national income/national output.
- Increases in capital goods, labour force, technology, and human capital can all contribute to economic growth.
- Gross Domestic Product, Gross Value Added, Gross National Product, etc. are the measures of Economic Growth.

Sustainable Development

- The term sustainable development is defined as "the development to achieve the needs of present generation without compromising future generation's needs."
- When the World Commission on Environment and Development (Brundtland Commission) published its report in 1987, it presented 'sustainable development' as a new concept.
- Sustainable development ensures the well-being of individuals by integrating social development, economic development, environmental conservation and protection.
- Sustainable Development Goals (SDGs) or Global Goals are a collection of 17 interlinked global goals designed to be a 'blueprint to achieve a better and more sustainable future for all'. The SDGs were set up in 2015 by the United Nations General Assembly and are intended to be achieved by the year 2030.

These 17 goals are as follows:

1. No poverty
2. Zero hunger
3. Good health and well-being
4. Quality Education
5. Gender equality
6. Clean water and sanitation
7. Affordable and clean energy
8. Decent work and economic growth
9. Industry, innovation and infrastructure
10. Reduced inequalities
11. Sustainable cities and economies
12. Responsible consumption and production
13. Climate action
14. Life below water

15. Life on land
16. Peace, justice and strong institutions
17. Partnership for the goals

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