

Net value of all economic goods & services produced in within domestic territory in a country in an A/cing yr + NFIA

1) Usefulness and significance of NI estimates

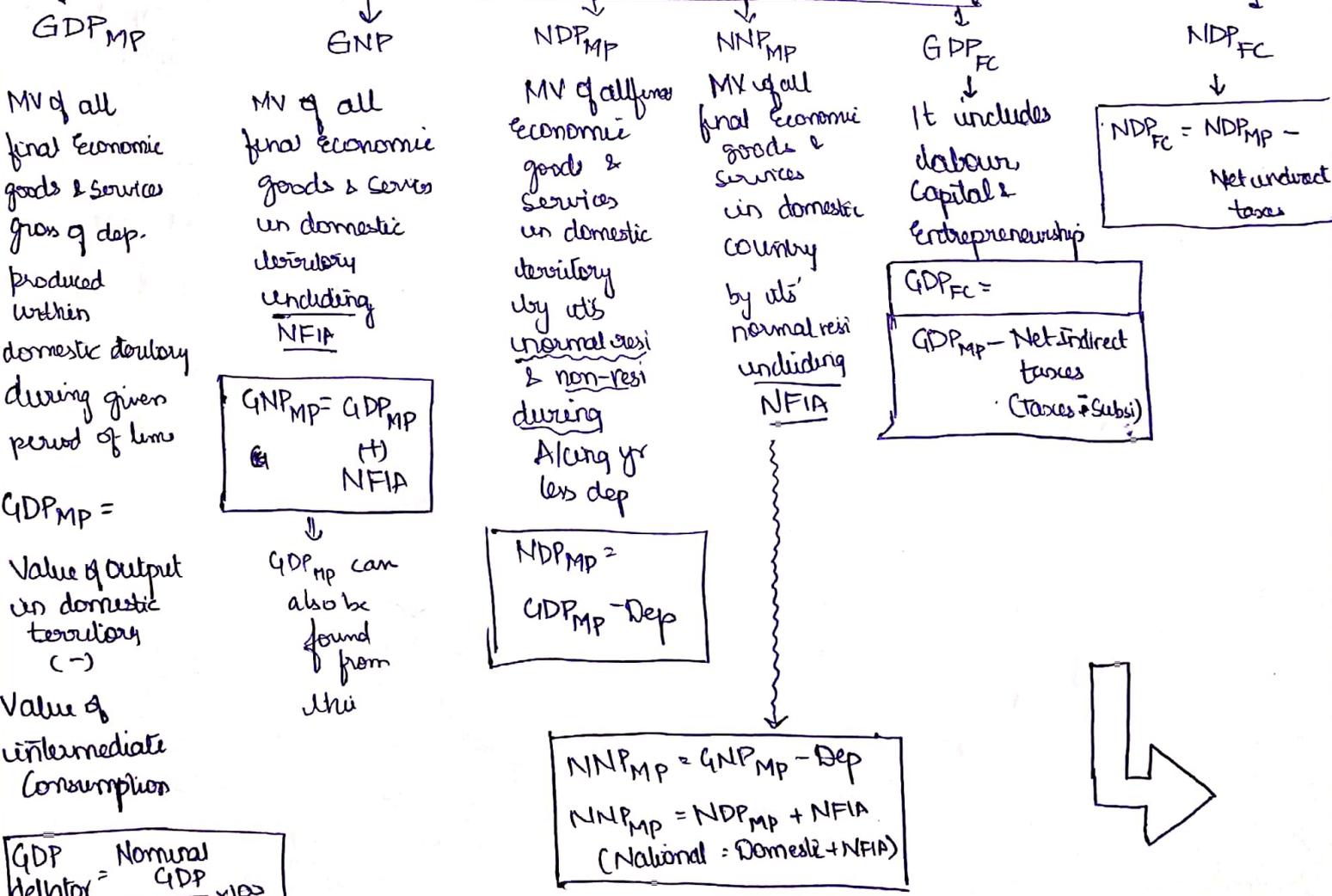
- 1) Helps in providing a conceptual, comprehensive and A/cing framework for analysing and evaluating short run performance of an economy
- 2) Distribution pattern of NI determines pattern of demand of goods.
- 3) Economic welfare depends on magnitude and distribution of NI
- 4) Study of inequality
- 5) Economic forecasting
- 6) International Comparison

National = Domestic + NFIA

MV = Market Value

FC = Market Prices - Indirect taxes

CONCEPTS OF NATIONAL INCOME



Inflation Rate =  $\frac{GDP\ deflator_2 (-)}{GDP\ deflator_1} \times 100$

Contd...

NNP<sub>FC</sub>

$NNP_{FC} =$   
 $NNP_{MP} - \text{Net indirect taxes}$

PerCapita Income

Measures a country's economic output per person.

$$\frac{GDP}{\text{Population}}$$

Personal Income

$$PI = NI + \text{Income Recd but not earned} - \text{Income earned but not recd}$$

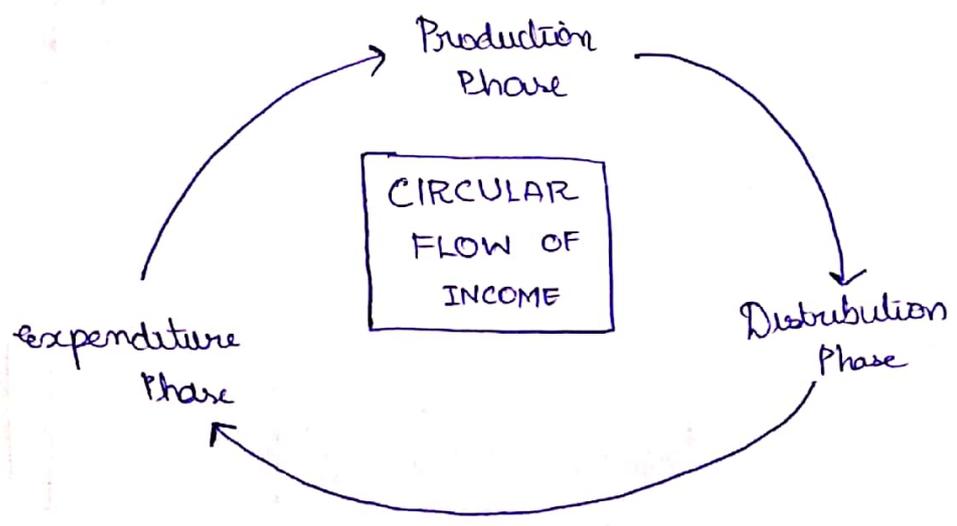
DPI (Disposable Personal Income)

$$DPI = PI - \text{Personal Income taxes} - \text{Non tax payments}$$

Private Income

$NNP_{FC} \text{ accruing to Pvt sector} = NNP_{FC} \rightarrow$  Income from property & entrepreneurship  
 (-) Saving of unemp. enterprise

Pvt Income =  $NNP_{FC}$  accruing to FC  
 (+) T/F from govt  
 (+) T/F from rest of the world  
 (+) Int on national debt.



# METHODS

Value Added Method

$$GVA = \left[ \begin{array}{l} \text{Sales} + \\ \text{Cl. Stk} - \\ \text{Op Stk} \end{array} \right] - \text{Intermediate Consumption}$$

$$GDP_{MP} = \sum GVA_{MP}$$

Income Methods

$$NDP_{FC} = \begin{array}{l} \text{Compensation to Employees} \\ + \text{Operating Surplus} \\ + \text{Mixed Income of Self Employed} \end{array}$$

$$NNP_{FC} = NDP_{FC} + NFA$$

Expenditure method

$$GDP_{MP} = \sum \text{Final Exp.} \\ = PFCE + GFCE + GDCF + X - M \\ [C + I + G + X - M]$$

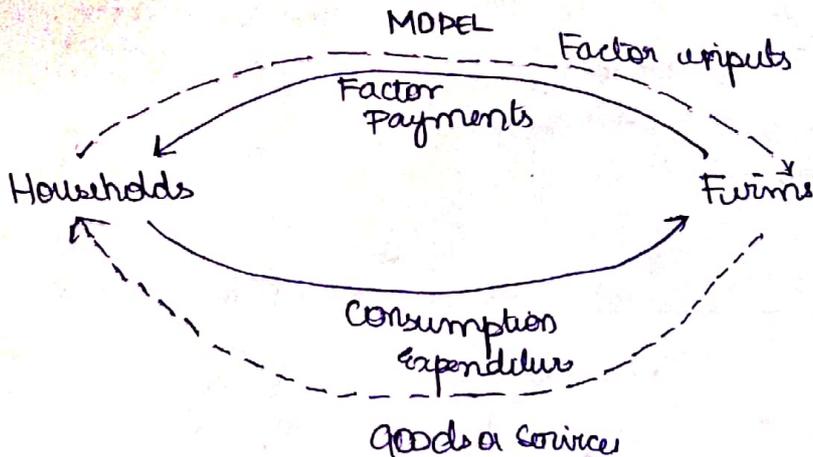
## LIMITATIONS

- 1) Issues of t/f payment
- 2) Services of durable goods
- 3) Valuation of a new goods at constant prices
- 4) valuation of govt services
- 5) Accurate distinction b/w final goods & intermediate goods

## CHALLENGES

- 1) Lack of reliability of data
- 2) Accurate estimation of consumption of <sup>fixed</sup> Capital
- 3) Presence of non-monetised sector
- 4) Production of self consumption
- 5) Lack of proper occupational classification

CIRCULAR FLOW IN A TWO SECTOR MODEL



★ Important Concepts:

1)  $AD = C + \bar{I}$  (constant)

Aggregate demand

Consumption

Investment

$C = a + bY$

$MPC = \frac{\Delta C}{\Delta Y}$

$APC = \frac{C}{Y}$

2)  $S = f(Y)$

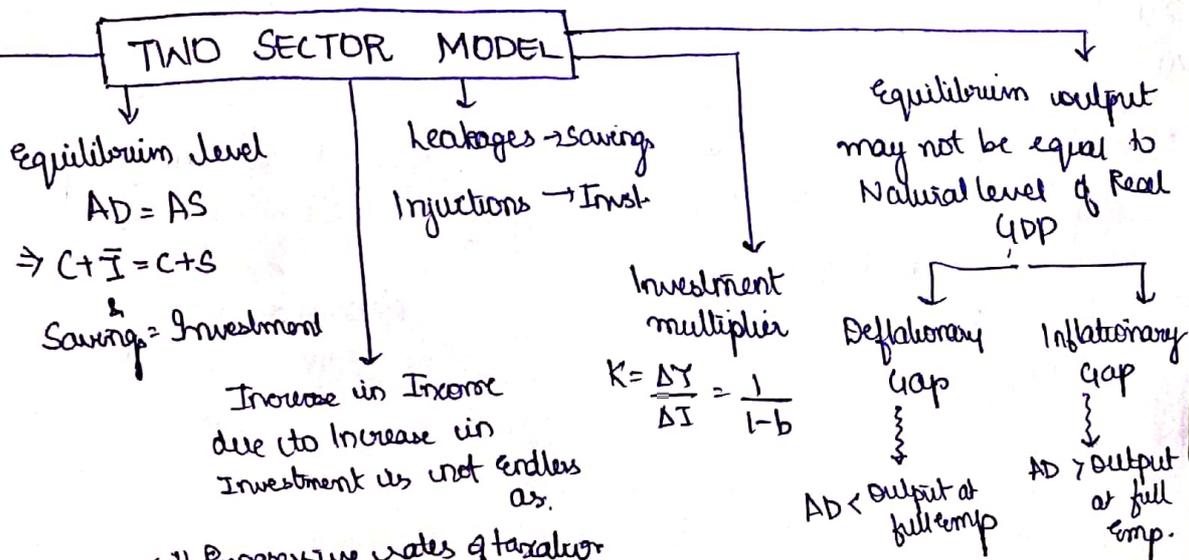
$= -a + (1-b)Y$

$MPS = \frac{\Delta S}{\Delta Y}$

$APS = \frac{S}{Y}$

$AS = C + S$  → Supply

Only 2 sectors  
1) Household  
2) Producer



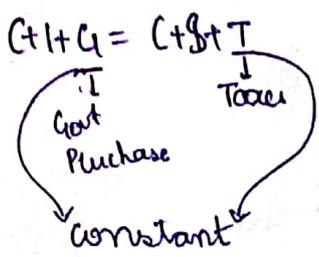
- (i) Progressive rates of taxation
- (ii) Higher Idle Saving
- (iii) Higher Imports
- (iv) Scarcity of goods
- (v) Undistributed profits
- (vi) Already at full employment

★  $MPS = 1 - MPC$

- Only 3 sector
- 1) Household
  - 2) Producer
  - 3) Govt.

### THREE SECTOR MODEL

Equilibrium level



Leakages ↓  
Savings, Taxes

Injections ↓  
Invest, Govt pur.

Inst. multipliers

Lumpsum tax  
 $K = \frac{1}{1-MPC}$

Tax as a function of income  
 $K = \frac{1}{1-b(1-t)}$

Income determination

Lumpsum tax  
(Tax not dependent on Income)

$Y_d = Y - T$

$\Rightarrow Y = C+I+G + \text{net}$

$\Rightarrow Y = a+b(Y-T)+I+G + \text{net}$

Lumpsum tax & T/F payment

$Y_d = Y - T + TR$

$\Rightarrow Y = C+I+G$

$= a+b(Y-T+TR)+I+G$

Tax as function of Income

$Y_d = Y - T - T_y$

↓  
Tax as a function of Income

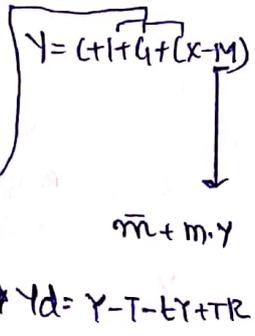
Tax as a function of Income & T/F pay

$Y_d = Y - T + TR + \bar{T} + Y$

- 4 sectors
- 1) Household
  - 2) Producer
  - 3) Govt.
  - 4) Foreign

### FOUR SECTOR MODEL

Equilibrium level



Leakages ↓  
Savings, Taxes, Import

Injections ↓  
Inst, Govt pur, exports

Inst multipliers

$K = \frac{1}{1-b(1-t)+m}$

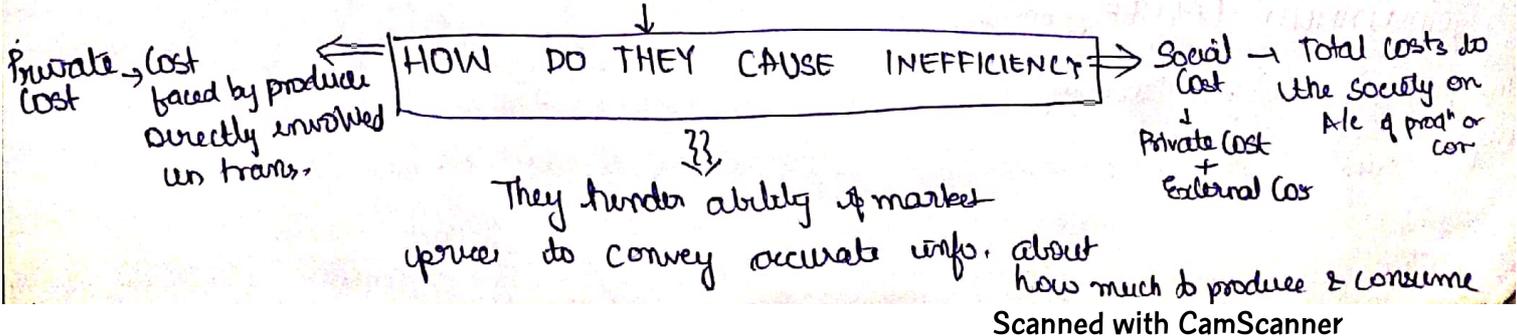
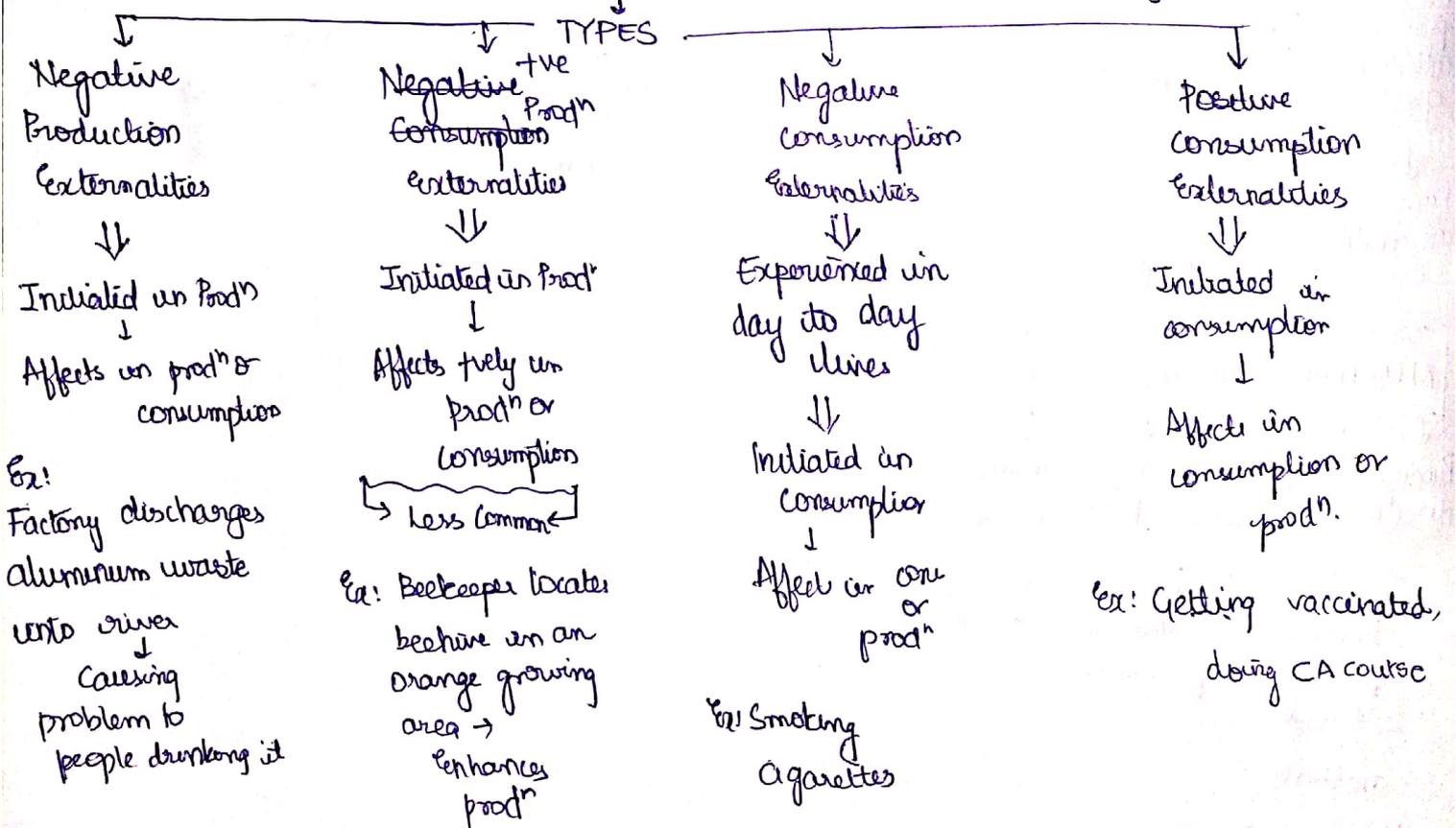
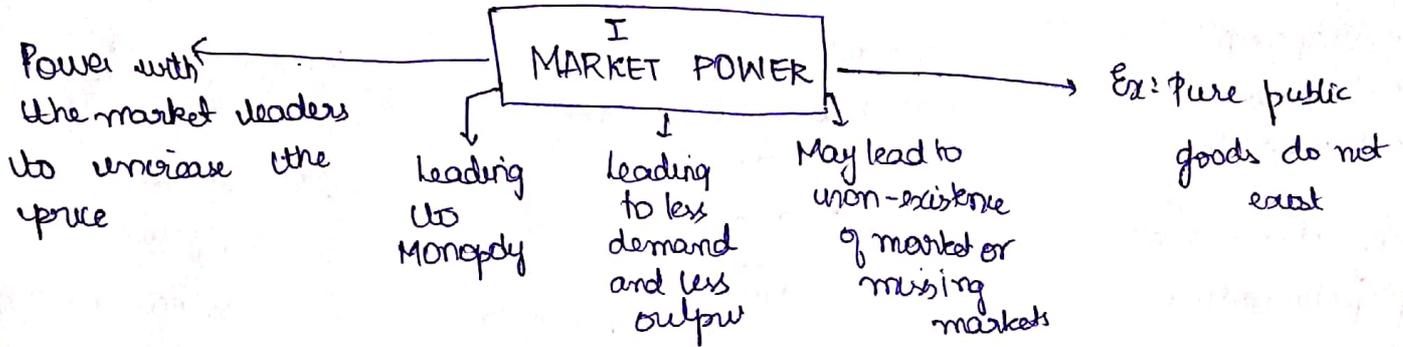
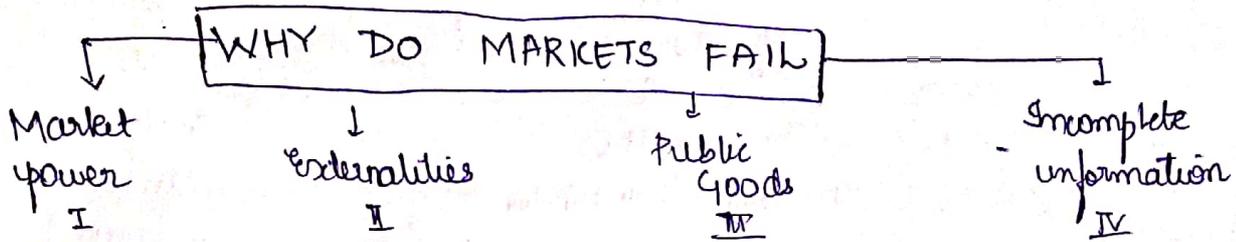
Multiplier → MPC is high & vice versa

Exports > Imports → NI Increase

Exports < Imports → NI decrease

Trade Balance ↓  
Compare Export & Import

When there is misallocation of society's scarce



Richard Musgrave

Allocation function

Optimum and efficient allocation of resource (Scarce)

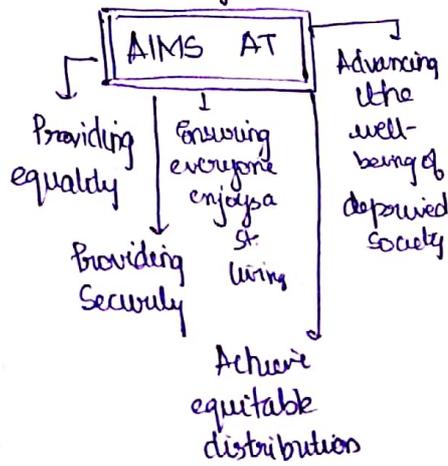
So that they are put to the best use & there is no wastage

In reality there cannot be perfectly competitive



Redistribution function

Changing the pattern of distribution of income, wealth and opportunities from what the market would prefer forward to a more socially optimal and equilibrium one



Stabilisation function

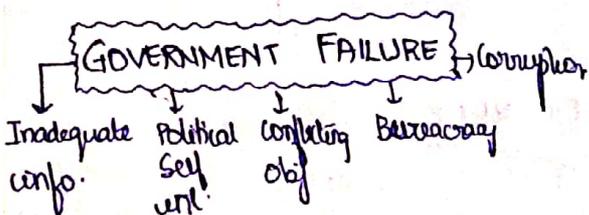
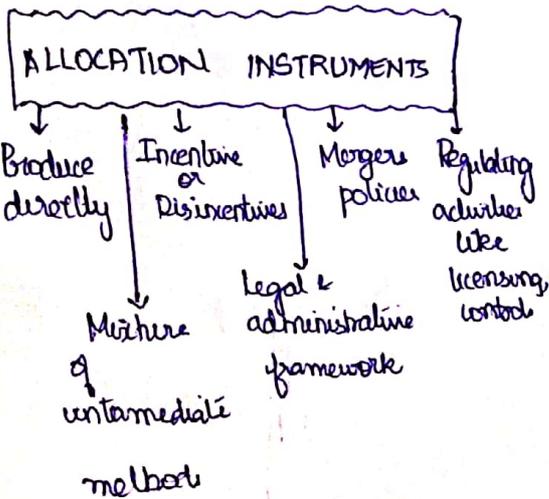
Government intervention is required

If govt. does not interfere then

- 1) Instabilities
- 2) stagflation (Inflation + Unemp.)

Recession  
Deficit balance budget exp. is increased

Inflation  
Surplus budget exp. is reduced.



\* MPC = Marginal Private Cost

↓  
Change in producer's total cost due to additional unit of goods or service

MEC = Marginal external Cost

↓  
Change in cost to parties other than producer

MSC = Marginal Social Cost

↓  
MPC + MEC

MPB = Marginal Private benefit

MEB = Marginal external benefit

MSB = Marginal Social benefit  $\Rightarrow$  MPB + MEB

If externality is present  
MSC  $\neq$  MPC  
or  
MSB  $\neq$  MPB  
Equilibrium  $\Rightarrow$  MPC = MPB

↓

Socially optimum output  $\Rightarrow$  MSB = MSC

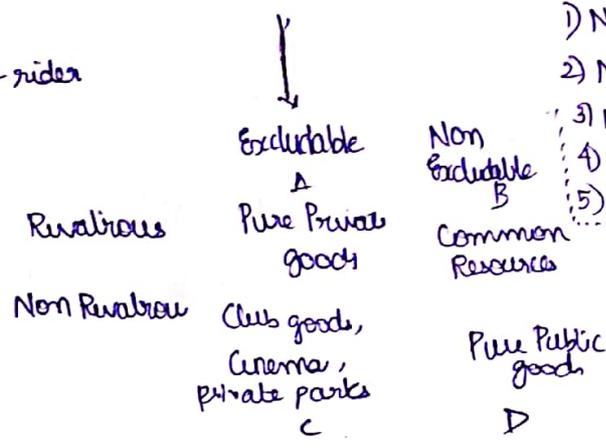
Manufacture  $\Rightarrow$  MSB = MPC

- Characteristics of Private goods
- 1) Yield utility. Scarce. Purchasing is req.
  - 2) Private property rights
  - 3) Rivalrous
  - 4) Excludable
  - 5) Do not have free-rider problem

III  
PUBLIC GOODS

$\Rightarrow$  Public goods are those which do not deter the benefits of others when one individual consumes it.

↓  
CLASSIFICATION



Characteristics

- 1) NO direct payment
- 2) Non-rival
- 3) Non-excludable
- 4) Free-rider problem  $\rightarrow$
- 5) Indivisibility

Free rider is a person who experiences goods without paying for it

If it is not solved, it will result in  
1) No public goods  
2) Under produce public goods

Quasi Public Goods  $\rightarrow$  Mixed Goods  $\rightarrow$  Near Public Goods

↓  
Market for these kinds of goods are considered to be uncomplete market and lack of provision by free market would be considered as inefficiency and market failure

Common Access Resources  $\rightarrow$  Utilization of one will affect the other

↓  
Leads to Tragedy of Commons when exercised to disadvantage  
Ex: Cattle owners let their cattle graze the grass to an extent that affected the welfare of people.

IV  
INCOMPLETE  
INFORMATION

Assumption of Perfect information is not satisfied

- (i) Nature of product / Service is complex
- (ii) Time consuming to gather info.
- (iii) Ignorant on many matters

Asymmetric  
info

↓  
One has  
more knowledge  
than other

Adverse  
Selection

↓  
leads asymmetric  
info leads to  
adv. selection

Moral hazard

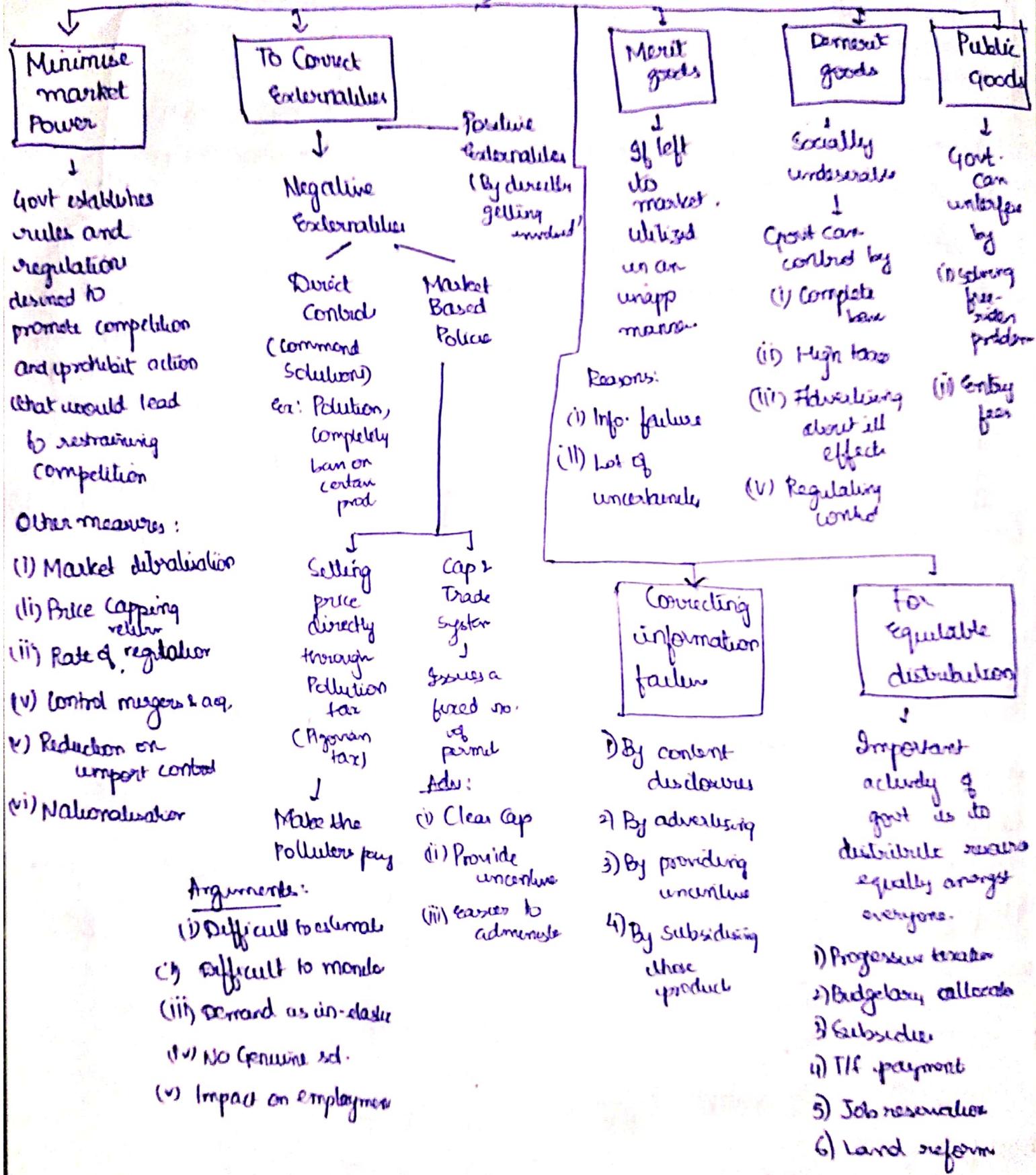
↓  
losses due to  
externality  
Cost can be shifted

\* Lemons problem

Bad Quality Cars (Lemons)

Good Quality cars (Peach)

Buyer is made to buy the bad quality cars at any price. This would eliminate good quality cars from market; leaving only bad quality cars.  
(This is Lemons Problem)



**OBJECTIVES OF FISCAL POLICY**

- 1) Achieving & maintenance of full employment
- 2) Maintenance of Price stability
- 3) Equitable distribution of Income and wealth
- 4) Acceleration of the rate of Economic development

**AUTOMATIC VS DISCRETIONARY FISCAL POLICY**

Depends upon level of economic activity (lower economic level or higher economic level)

Discretionary policy is where govt deliberately controls the actions.

↓  
Thus it is more beneficial

**Instruments of Fiscal Policy**

Government Expenditure as an Instrument of Fiscal Policy

- Govt. Exp includes:
- (i) Current exp
  - (ii) Cap exp
  - (iii) Int payments

During recession  
↓  
fresh wave of public work like road const, sanitary work, etc

**\* Pump Pricing**

Govt spending multiplier  
Higher MPS, lower multiplier

$$\frac{\Delta Y}{\Delta G} = \frac{1}{MPS} = \frac{1}{1 - MPS}$$

Tax as an instrument of Fiscal Policy

Changes in tax rate aimed at encourage/restricting private exp.

Recession  
Higher DPI, Higher cons. exp

Inflation  
Reduced DPI

Tax multiplier  $\Rightarrow \frac{-b}{1-b}$

Balanced budget multiplier  $= \frac{1-b}{1-b} = 1$

Public Debt as an instrument of Fiscal Policy

Can be internal or external

Market loan  
↓  
By issue of treasury bill

Small Saving  
↓  
PPF  
National Saving Certificate

Inflation  
Borrowing  
reduce money supply

Recession  
Repayment  
Infuse funds

Budget as an instrument of Fiscal Policy

Balanced budget,  
Deficit budget,  
Surplus budget.

Recession  
Deficit

Inflation  
Surplus

# TYPES OF FISCAL POLICY

2-4-2

Expansive  
Fiscal Policy

Contractionary  
Fiscal Policy

Used to address recession

Real income decreases,  
Unemployment increase.

## Limitations of Fiscal Policy

1) Lags

2) Borrowing money from market may lead to crowding out

3) Taxes cannot be changed easily

4) Conflicts in objectives

5) Printing money to fund deficit can lead to inflation

Totally a liquid asset

**FUNCTIONS OF MONEY**

- 1) Medium of exchange
- 2) Unit of account
- 3) Unit of deferred payment
- 4) Acts as a store of value

**CHARACTERISTICS**

- 1) Generally acceptable
- 2) Relatively scarce
- 3) Durable & long lasting
- 4) Effortlessly recognizable
- 5) Difficult to counterfeit
- 6) Possessing uniformity
- 7) Divisible into smaller parts
- 8) Portable

**DEMAND FOR MONEY**

The quantity of nominal money depends on

- 1) Income
- 2) General price level
- 3) Rate of Int
- 4) Real GDP
- 5) Level of financial innovation

**THEORIES OF DEMAND FOR MONEY**

**Classical Approach**  
 [Qty theory of money]  
 Price level  
 $MN = PT$  → Total no. of trans.  
 Money in circulation → Velocity of trans.  
 $MN + M'V' = P \cdot Y$  fixed in short run  
 Constant

**Cambridge Approach**  
 [Neo classical Approach]  
 Money increases utility in a way  
 Enabling possibility of split-up of sales & Pur.  
 Being a hedge against uncertainty  
 $M_d = KPY$   
 Demand for money → Proportion of nominal income

**Keynesian Theory (Liquidity Preference Theory)**  
 Acc. to Keynes, Money in cash has 3 motives  
 Transaction: Turn lag b/w transactions, Pur & sales do not occur at same time  
 $L_1 = K_1 \cdot Y$   
 Precautionary demand: Money kept for unforeseen circumstances  
 Speculative: Desires to hold cash to be equipped to exploit low

## POST KEYNESIAN DEVELOPMENTS

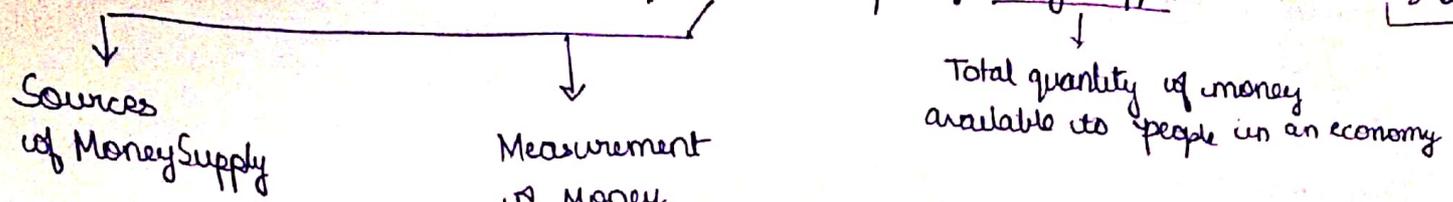
Inventory  
Approach to  
Transaction  
Balances

↓  
Friedman's  
Restatement of  
Quantity theory

↓  
Demand for  
money as  
behaviour towards  
risk

\* Four determinants of  
demand for  
money

- 1) Is a function of total wealth
- 2) Positively related to price level
- 3) Rise of the opp cost of money holding declines & vice versa
- 4) Is influenced by inflation.



- 1) Decision of Central Bank
- 2) Supply responses of commercial banking system of the country

Measurement of Money Supply  
 → Most liquid

$$M_1 = \text{Currency with Public} + \text{Demand deposit with banking system} + \text{Other deposit with RBI}$$

$$M_2 = M_1 + \text{Savings Deposit with Post office savings Banks}$$

$$M_3 = M_1 + \text{Term Deposit with Banking System}$$

Least liquid ←  $M_4 = M_3 + \text{Total deposit with Post office savings Organisation}$

$$NM_1 = \text{Currency with Public} + \text{Demand deposit with bank} + \text{Other deposit with RBI}$$

(Same as  $M_1$ )

$$NM_2 = NM_1 + \text{Short term term time deposits}$$

$$NM_3 = NM_2 + \text{Long term time deposits}$$

$$L_1 = NM_3 + \text{All deposit with Post office saving Bank}$$

$$L_2 = L_1 + \text{Term deposit with term lending institutions}$$

$$L_3 = L_2 + \text{Public deposit of NBFIs}$$

$$\text{Reserve money} = \text{Currency in Circulation} + \text{Banker's deposit with RBI} + \text{Other deposit with RBI} - \text{RBI's net non monetary liab.}$$

$$\text{Money multiplier } (c) = \frac{\text{Money Supply}}{\text{Monetary Base}}$$

$$M = m \times MB$$

$$\text{Credit multiplier} = \frac{1}{RRR}$$

$$\text{Multiplier} \Rightarrow \frac{1+C}{C+e+r}$$

otherwise  $\frac{1+C}{C+e+r}$

If  $c=0, e=0$

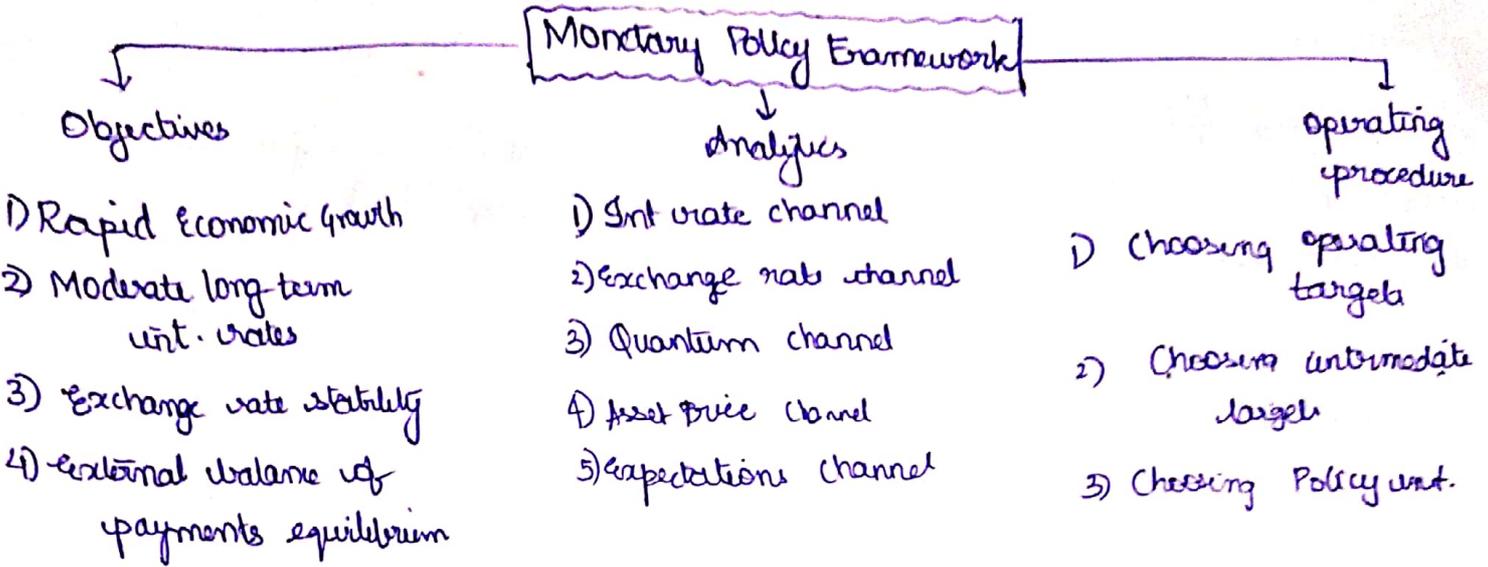
$$\text{Credit multiplier} = \frac{1}{r}$$

# Determinants of money supply

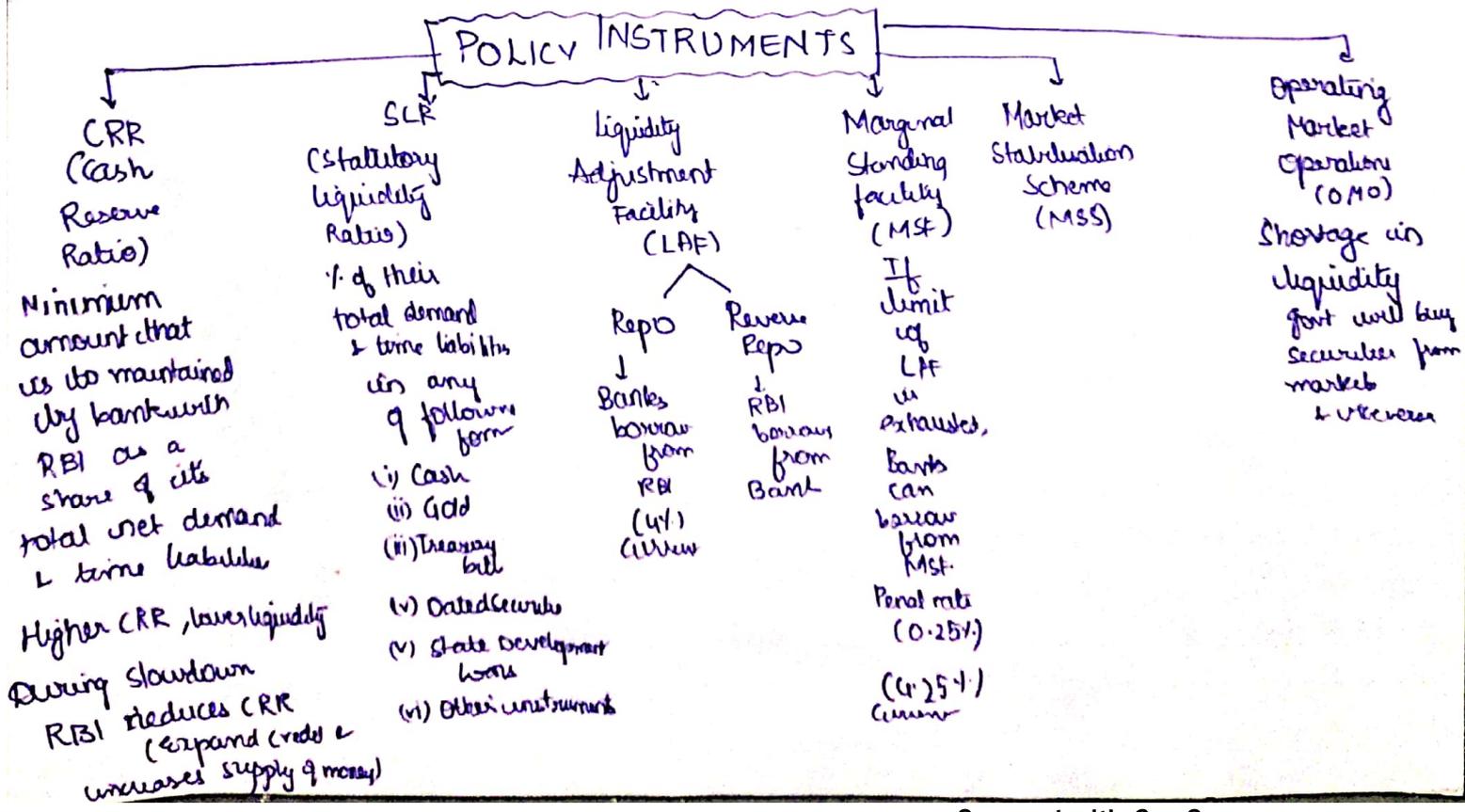
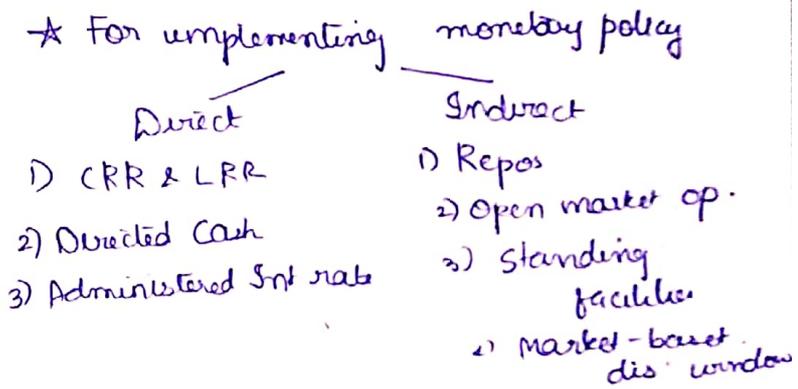
1<sup>st</sup> view  
Exogenously

2<sup>nd</sup> view  
Endogenously  
↓  
By considering the  
impact of other  
variables

Monetary Policy → Programme of action undertaken by the monetary authority (ie) Central bank with control and regulate the demand for and supply of money



RBI is the apex institution in controlling the issue of currency and credit system in country



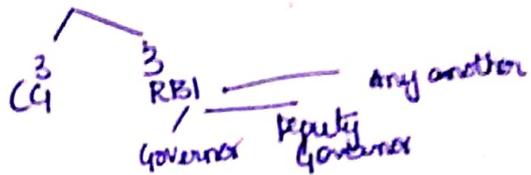
# Organisational Structure for monetary Policy Decisions

Monetary  
Policy Framework  
Agreement

- Official target for inflation is known as inflation targeting
- CG has notified 4% CPI (Max 6% min 2%)

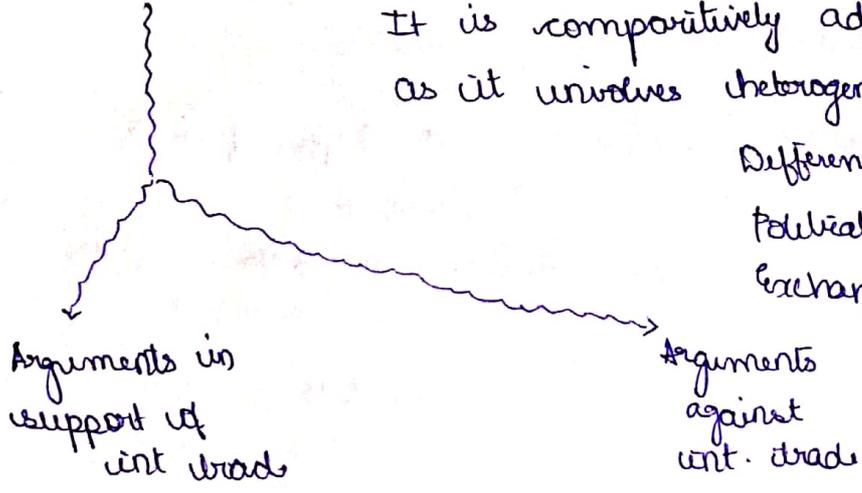
Monetary  
Policy  
Committee (MPC)

6 Members



1) International Trade  $\Rightarrow$  Exchange of goods and services b/w two countries.

It is comparatively advantageous than internal trade as it involves heterogeneity in customers and currencies  
 Difference in legal systems  
 Political system  
 Exchange rate risk (disadv)



- |  |  |
|--|--|
| 1) Provides stimulus to eco. efficiency    | 1) Negative labour market outcomes   |
| 2) Provides access to new markets          | 2) Often lacks transparency & predictability   |
| 3) Employment generally, invest, incl. FDI | 3) Not equally beneficial to both countries  |
| 4) Bonds b/w nations                       | 4) Often criticised for its excessive stress on exports  |
| 5) HR development                          | 5) May lead to over-indebtedness   |
| 6) Opening of new markets                  | 6) May ignore people's welfare and jeopardised for sake of profit  |
| 7) Stimulate econ. growth by creating jobs | 7) Too much export orientation may distort actual investments away from genuine investment needs of a country. |
| 8) Enhances extent of market               | 8)   |

2) Important theories of International Trade

(i) Merchantile Theory of Int. Trade

Zero Sum game  $\Rightarrow$  One person's gain is other's loss.  
 It said that country has to import precious metal to maximise Nation's wealth and power.

It is an important theory to explain policies followed by many big and fast-growing economies in Asia.

\* Specie  $\rightarrow$  Money in the form of precious metal rather than notes.

(ii) Theory of Absolute Advantage:

Adam Smith has given this theory stating that international trade is beneficial to both the countries

How?  $\rightarrow$  Absolute Cost Advantage. One country has to specialise in one and another has to specialise in other

Considers only 2 countries and 2 products. (labour is the only factor of prodn).

Ex:	Country A	Country B	
Wheat (Bushels/hr)	6	1	→ Country A ⇒ Absolute adv
Cloth (Yards/hr)	4	5	→ Country B ⇒ Absolute adv

How is it beneficial?

↓  
If Country A exchanges 6 Bushels of wheat with 6 yards of cloth

Country A

To mfg add 6 Bushels  
time req. → 1hr

Receiving 6 Yards of  
Cloth, Time → 1.5hr  
( $\frac{1-4}{2-6}$ )

Net Saving 30 min  
which was otherwise 2hr

Country B

To mfg add 6 yards of cloth  
time req. → 1.2hrs

Receiving 6 Bushels of wheat  
Time → 6hr

Net Saving 4.8hr

Thus beneficial

→ Only labour as cost of Prod

(ii) Theory of Comparative Advantage

→ David Ricardo

Said that int. trade can be mutually beneficial even if a country specialises in both the products.

Here Country which has lower absolute DISADVANTAGE has to export and import the product in which there is higher absolute DISADVANTAGE (in a good)

Ex:	Country A	Country B	B's Output in comparison to A
Wheat (Bushels/hr) (W)	6	1	$\frac{1}{6}$ th of A
Cloth (Yards/hr) (C)	4	2	$\frac{1}{2}$ th of A

} Country has absolute adv. in both

BUT; B has lower absolute DISADVANTAGE in case of cloth. Hence it has to export cloth and import wheat

\* Range of Negotiation →  $4C \leq 6W \leq 12C$

↓  
A's advantage  
Minimum that Country A would want is 4 Yards of cloth otherwise, not beneficial (Against 6 bushels of wheat)

↓  
B's advantage

Against receiving 6 Bushels of wheat, B would get 6 hrs of time  
Thus max cloth that can be mfg is 12C.

But this was modified by Haberler:

This fellow introduced opportunity cost

	Country A	Country B
Wheat	6	1
Cloth	4	2
	↓	↓
	$6W = 4C$	$1W = 2C$
	$W = \frac{2}{3}C$	$W = 2C$

Country A can forgo  $\frac{2}{3}C$  [ $0.67C$ ]  
 while Country B can forgo  $2C$

Country A has lower <sup>opp. cost</sup> absolute disadvantage for wheat so A has to mfg wheat

(iv) Heckscher - Ohlin Theory of Trade: (H-O theory)

F.K.A Factor Endowment Theory  $\Rightarrow$  H-O theory  
 Modern Theory of Trade  $\Rightarrow$  Samuelson

2 Countries etc, 2 Products, 2 Factors of Prod<sup>n</sup>  
 Capital / Labour

Country which is capital intensive  $\rightarrow$  Should specialise in capital products and import labour.  
 and vice versa.

H-O theory

H-O Trade Theorem

Factor Price Equalization Theorem (Samuelson)

Country's specialisation will depend on Factor Endowment overall availability of Resources.

Product mobility becomes a substitute for factor mobility

Export on those which req. abundant Resources  
 Import those which req. scarce Resources

(v) New Trade Theory

Developed and big countries offer trade amongst each other They create similar goods and services

2 key concepts give advantage  $\left\{ \begin{array}{l} \text{Economies of Scale} \\ \text{Network effect} \rightarrow \text{Utility increases when people use same product} \end{array} \right.$

\* Diff b/w Comparative Costs & Modern Theory

**Tariffs**  
 ↓  
 Is a form of tax collected at the border on imports or exports.

**Forms of Import Tariffs**

**Special**  
 ↓  
 fixed amount of money per unit or according to weight.  
 ↓  
 Does not involve value of merchandise

**Ad valorem**  
 ↓  
 fixed %  
 ↓  
 Widely used across the world

- a) Mixed Tariffs (Mix of Special or ad valorem)
- b) Technical/Other Tariffs  
 Ex: 3000 / solar panel + 50 / kg on battery
- c) Tariff Rate Quota → Limit Above the limit have higher tariffs
- d) Most-Favored Nation Tariffs (MFN) → Countries promise to pay on imports (agreement b/w members of WTO)
- e) Variable Tariffs → Duty fixed to bring the price of imported commodity to level of domestic support price
- f) Preferential tariffs → Lower rate than MFN  
 Ex: US - Canada - Mexico (USMCA)

**Non-Tariff Measure**

Policy measures other than ordinary customs tariffs, that can potentially have an economic effect on international trade in goods

NTBs → Non Trade barriers (Subset of NTMs)

**Technical measures**  
 ↓

**Product Specific properties**  
 (Characteristic of product, technical specifications & prod<sup>n</sup> processes)

(i) SPS measures (Sanitary & Phytosanitary)

Protect human, animal & plant life from additives, pests ...

(ii) TBT. (Technical barriers to trade)

Relating to food & non food traded products

**Non-technical measures**  
 ↓

**Trade requirements**  
 (Shipping, customs, trade rules, taxation policies)

(i) Import Quotas

**Binding**  
 ↓  
 Set below free trade level

**Non-Binding**  
 ↓  
 Set above free trade level

Absolute Quotas

↓  
 limit quantity of imports to sp. limit

(iii) Price Control measures

(ii) Non-automatic licensing & Prohibitions

**export related measures**

(i) Ban on exports (includes both technical & non-technical measures)

(ii) export taxes (Tax collected on exported goods, specific or ad-valorem.)

(iii) Export Subsidies & incentive

(iv) Voluntary Export Restraints (Refer to a degree of unilateral quota administered by an exporting country voluntarily restraining the quantity of exports).

g) Bound Tariff → Setting an upper limit (by a WTO member)

h) Applied Tariff → actually charged on imports on MFN basis

i) Escalated tariff → Rate increases as the value of the product increases  
It is discriminatory

j) Prohibitive tariff → Sets the tariff so high that imports cannot be made

k) Import subsidies → Payment/unit or % of value of importations of goods

l) Tariff as a response to trade distortion

m) Anti-dumping duties

n) Countervailing duties

### Effects of Tariffs

- 1) effects the imports and exports
- 2) Discourage domestic consumers from experiencing foreign goods
- 3) Increase domestic production
- 4) Help an existing firm to make profits
- 5) Encourage consumption of domestic goods.
- 6) Increase govt revenues of importing country.
- 7) Create trade distortion by disregarding comparative advantage and prevent countries from enjoying gains from trade arising from competitive advantage.

(iv) Financial measures

(v) Measures affecting competition

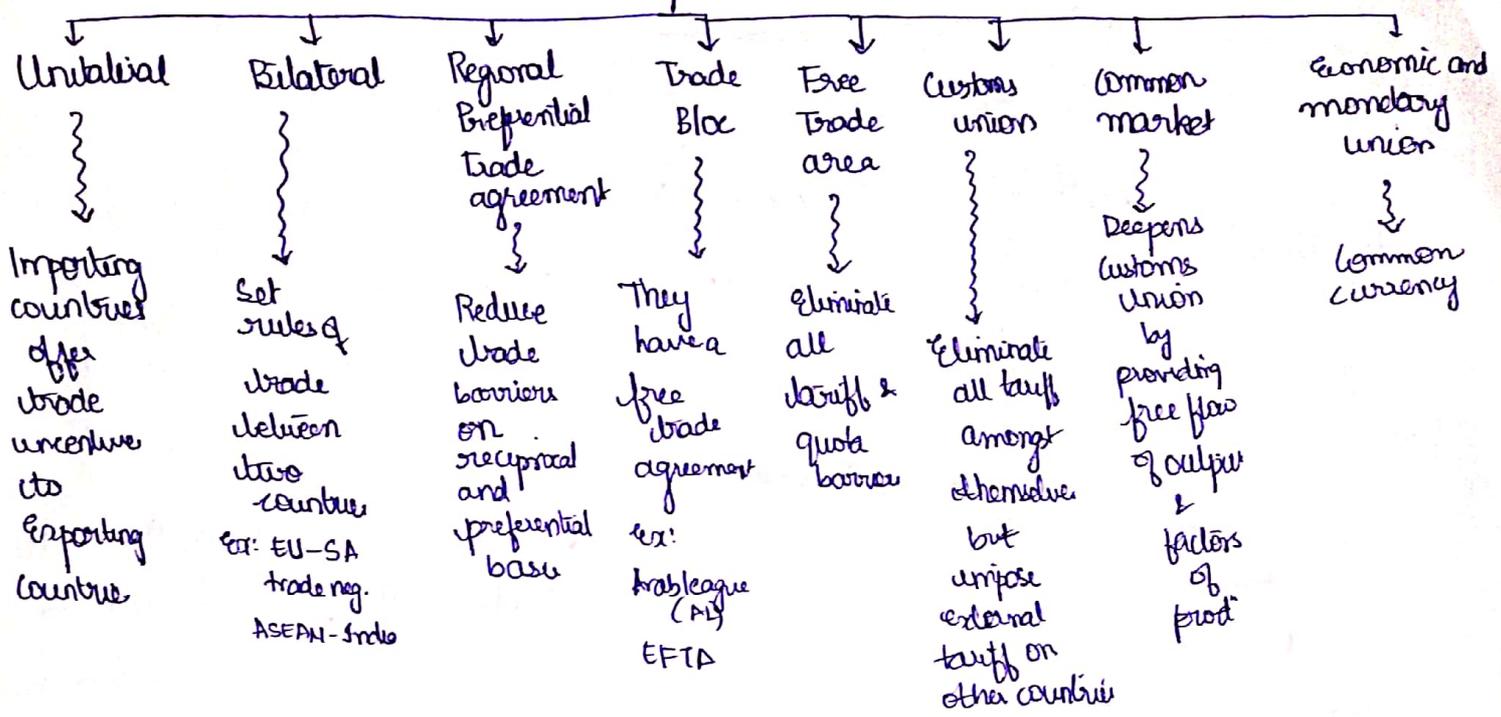
(vi) Govt. procurement policies

See T.B.

Embargoes

(Total ban imposed by govt on imports or exports)

**(CRTAS) REGIONAL TRADE AGREEMENTS**



**(GATT) GENERAL AGREEMENT ON TARIFFS AND TRADE**

1948 - 1994  
 8 Rounds ⇒ 8<sup>th</sup> Round being the last (1968-1994)  
 Birth of WTO

- Lost its relevance in 1980s.
- 1) IPR and Trades were not included
  - 2) World merchandise grew by leaps & bounds
  - 3) Idea of liberalising agricultural trade was not successful
  - 4) Ambiguous in multilateral system
  - 5) International investment had expanded substantially.

Uruguay Round  
 Birth of WTO

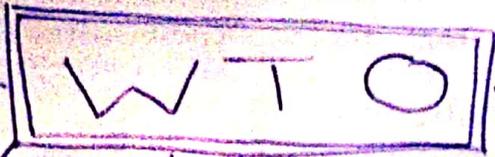
**The World Trade Organisation (WTO)**

- 6 Key Objectives**
- 1) Co-operation with major int. eco. un.
  - 2) Developing countries are beneficiaries
  - 3) Settle & enforce rules
  - 4) Forum for negotiation and monitoring bilateral trade
  - 5) Increase transparency in decision making
  - 6) Resolve trade disputes

Important outcome from Uruguay Round  
 Principle Objective  
 Facilitate flow of intl. trade smoothly, freely, fairly & predictably

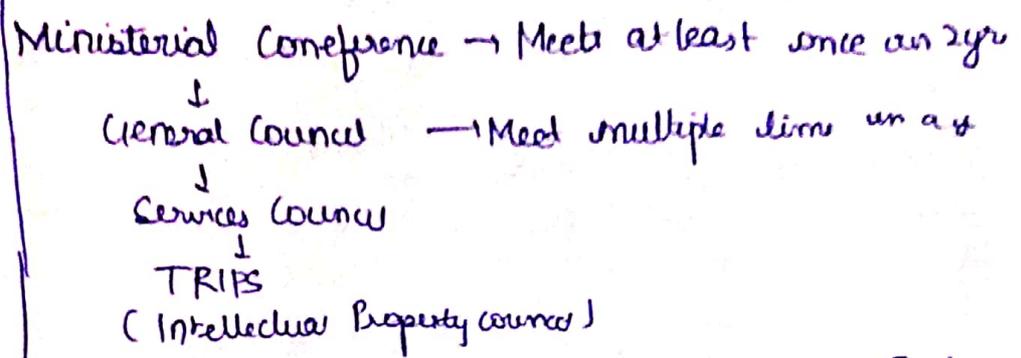
- Other Objectives**
- 1) Full employment
  - 2) Large & steady growing volume
  - 3) Effective demand
  - 4) Expanding prod.

- Functions**
- 1) Forum for trade negotiations
  - 2) Administering trade agreements
  - 3) Reviewing national trade policies
  - 4) Assisting developing countries
  - 5) Co-operating with other intl. org.



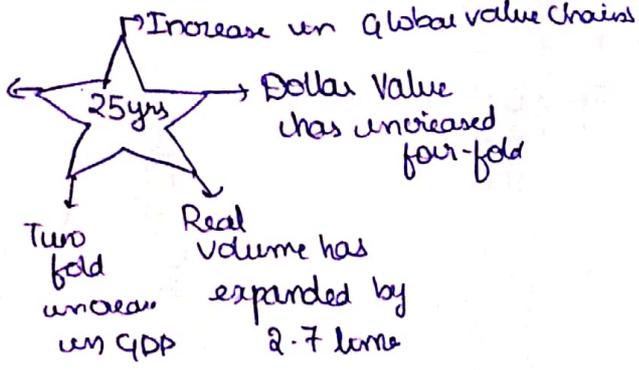
Accounts for more than 95% of world trade  
 ↓  
 164 members (112 developing)

Structure



Doha Round

Doha Development Agenda  
 9th Round since II<sup>nd</sup> WW  
 ↑ Increase in global value chains



Guiding Principle

- 1) Trade without discrimination
- 2) Free trade (through negotiation)
- 3) Predictability
- 4) General Competitiveness
- 5) National Treatment Principle
- 6) Market access
- 7) Protection of health & environment

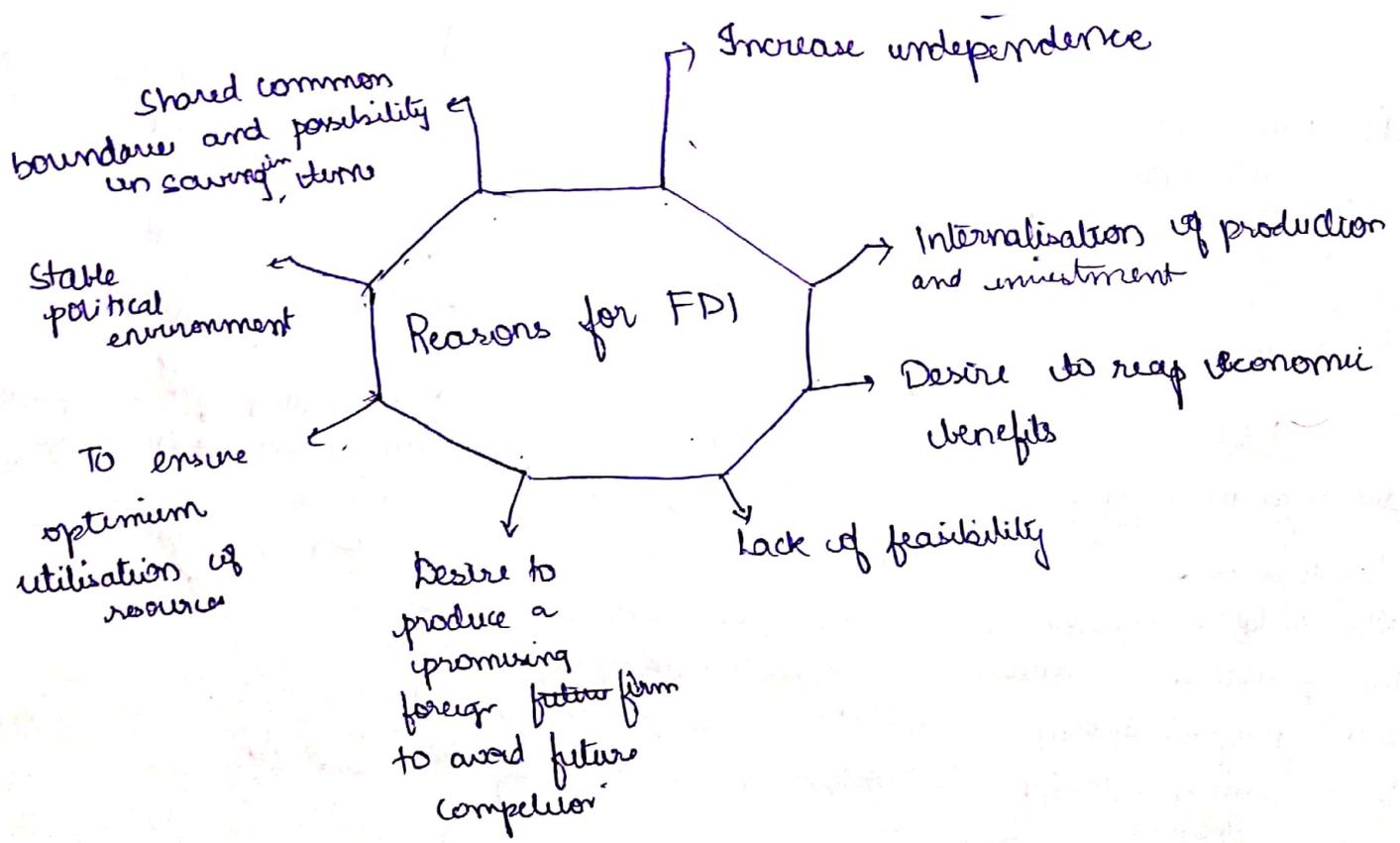
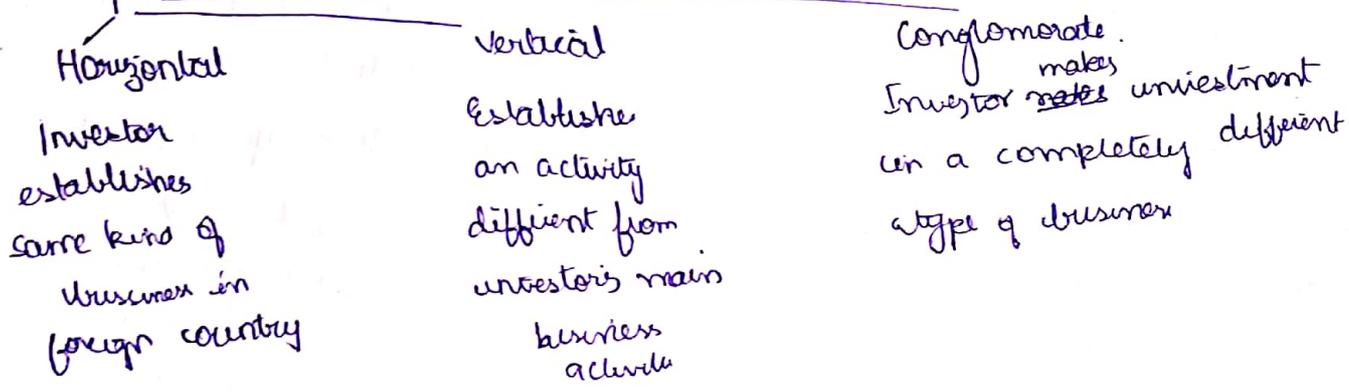
1) Foreign Capital → Any inflow of capital into the home currency

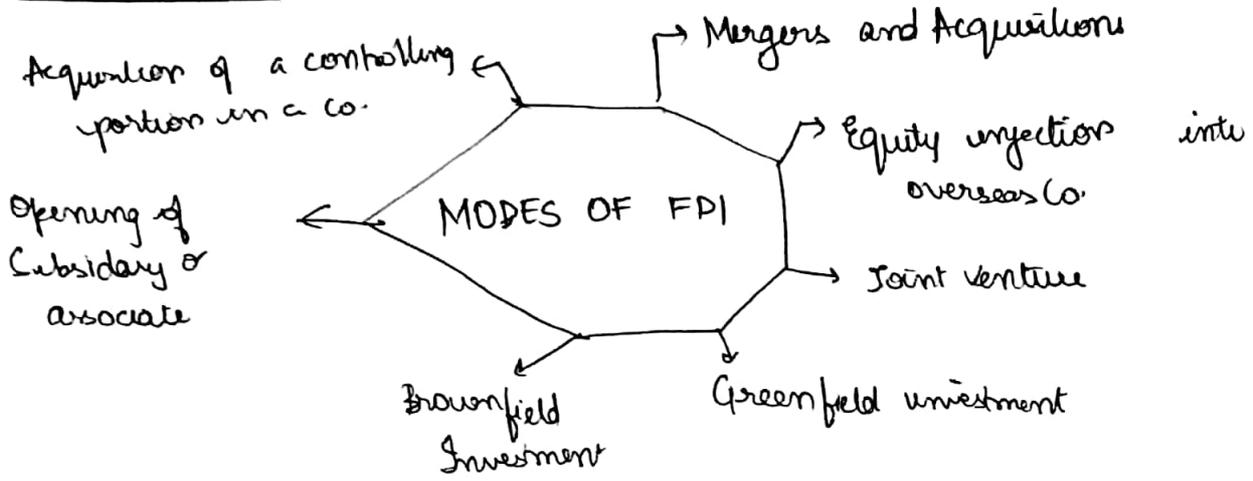
Components of foreign capital flows are



**Foreign Direct Investment**

The act of acquisition or construction of a physical capital by a firm from one country in another country





**BENEFITS OF FDI**

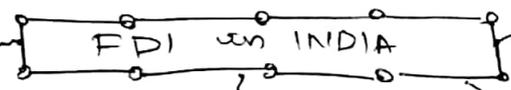
- 1) Foster Comp. & generate Comp. adv
- 2) Quality increase, efficiency & variety of products
- 3) Direct employment
- 4) Through backward & forward linkage - Indirect employment
- 5) Higher wages for skilled jobs
- 6) Provide access to foreign markets
- 7) Helps finance more investment what can supported to domestic saving

**PROBLEMS ASSOCIATED WITH FDI**

- 1) It is generally - Capital intensive. Might not be useful in labour-intensive countries
- 2) Ruthless exploitation of natural resource
- 3) Possibility of dual economy.
- 4) Distorted pattern of investment
- 5) Crowding out effect → Int. rates may increase as part of finance is done through domestic investment
- 6) May demand only low level of skill & ability.

**FDI Compliant instruments**

- 1) Eq. Shares
- 2) Partly Paid up Eq. shares
- 3) Warrant
- 4) Compulsory Convertible Pref. Share etc



They are on repatriation basis

- Route**
- Automatic (Airports, Biotech...)
  - Approval (Food Retail)
  - Automatic + Approval

**PROHIBITED**

**FDI VS**

- FDI**
- 1) Investment in creation of physical assets
  - 2) Long term int.
  - 3) Relatively difficult to withdraw
  - 4) Not speculative in nature
  - 5) Direct impact on emp.
  - 6) Int. in mgmt & control

**FPI**

- FPI**
- 1) Investment only in financial assets
  - 2) Short term int.
  - 3) Easier to withdraw
  - 4) Speculative in nature
  - 5) NO direct impact on emp.
  - 6) NO int. in mgmt & control

- PROHIBITED**
- 1) Manufacturing of tobacco products
  - 2) Activities not open to private (atomic)
  - 3) Nuclear Co.
  - 4) Trading in T/able development right
  - 5) Real estate Business
  - 6) Lottery
  - 7) Gambling
  - 8) Chit funds