BUSINESS ECONOMICS III
SYBCOM SEMESTER III
GLOSSARY

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The document gives a brief explanation of different concepts in Business Economics III, SemesterIII. It is also an assignment for practicing diagrams.

MODULE 1

1. **Macroeconomics** is the branch of economics that studies the behavior and performance of an economy as a whole. It focuses on the aggregate changes in the economy such as unemployment, growth rate, gross domestic product and inflation. Macroeconomics (from the Greek prefix makro- meaning "large" + economics) is a branch of economics dealing with the performance, structure, behavior, and decision-making of an economy as a whole. This includes regional, national, and global economies.

2. **Two sector Economy**: It is the economy which consists of two sectors: households and firms. Households spend all of their income (Y) on goods and services or consumption (C). There is no saving (S). All output (O) produced by firms is purchased by households through their expenditure (E).

3. **The three-sector economy** is one in which economics divides economies into three sectors of activity: extraction of raw materials (primary), manufacturing (secondary), and services (tertiary).

4. **Four sector economy/ Open economy**: The circular flow model in four sector economy provides a realistic picture of the circular flow in an economy. Four sector model studies the circular flow in an open economy which comprises of the household sector, business sector, government sector, and foreign sector.

5. **Closed Economy**: A closed economy is self-sufficient, which means no imports come into the country and no exports leave the country. A closed economy's intent is to provide domestic consumers with everything they need from within the country's borders. An economy that does not interact with the economy of any other country.

6. **The circular flow of income** or circular flow is a model of the economy in which the major exchanges are represented as flows of money, goods and services, etc. between economic agents. The flows of money and goods exchanged in a closed circuit correspond in value, but run in the opposite direction.

7. A **Financial market** is a market in which people trade financial securities and derivatives such as futures and options at low transaction costs. Securities include stocks and bonds, and precious metals.

8. **National Income** is the total value of all final goods and services produced by the country in certain year. The growth of National Income helps to know the progress of the country. In other words, the total amount of income accruing to a country from economic activities in a year's time is known as national income.

9. **GDP**: Gross Domestic Product (GDP) is a monetary measure of the market value of all the final goods and services produced in a period of time, often annually or quarterly. Nominal GDP estimates are commonly used to determine the economic performance of a whole country or region, and to make international comparisons.

10. **GNP/GNI**: The gross national income (GNI), previously known as gross national product (GNP), is the total domestic and foreign output claimed by residents of a country, consisting of gross domestic product (GDP), plus factor incomes earned by foreign residents, minus income earned in the domestic economy by non-residents.

11. **Depreciation:** It is defined as the reduction of recorded cost of a fixed asset in a systematic manner until the value of the asset becomes zero or negligible.

12. **Green GDP**: The green gross domestic product (green GDP or GGDP) is an index of economic growth with the environmental consequences of that growth factored into a country's conventional GDP. Green GDP monetizes the loss of biodiversity, and accounts for costs caused by climate change.

13. **NDP**: The net domestic product (NDP) equals the gross domestic product (GDP) minus depreciation on a country's capital goods. Net domestic product accounts for capital that has been consumed over the year in the form of housing, vehicle, or machinery deterioration.

14. **NNP:** Net national product (NNP) refers to gross national product (GNP), i.e. the total market value of all final goods and services produced by the factors of production of a country or other polity during a given time period, minus depreciation.

15. **PCI** : Per capita income (PCI) or average income measures the average income earned per person in a given area (city, region, country, etc.) in a specified year. It is calculated by dividing the area's total income by its total population.

16. **National Income at Factor cost** is a measure of national income or output based on the cost of factors of production, instead of market prices. This allows the effect of any subsidy or indirect tax to be removed from the final measure.
    National Income at Factor Cost = NNP at Market Price – Indirect Taxes + Subsidies.

17. **National Income at Market Price** : Gross (or net) national income (at market prices) represents total primary income receivable by resident institutional units: compensation of employees, taxes on production and imports less subsidies, property income (receivable less payable), (gross or net) operating surplus and (gross or net) mixed income. Gross national income (at market prices) equals GDP minus primary income payable by resident units to non-resident units plus primary

income receivable by resident units from the rest of the world. Gross national income (at market prices) is conceptually identical with gross national product (GNP) (at market prices), as hitherto understood in national accounts generally.

18. **National Income at Constant Price**: It is the money value of final goods and services produced by normal residents of a country in a year, measured at base year price. Base Year is a normal year which is free from price fluctuations.

19. **National Income at Current Price**: It is the money value of final goods and services produced by normal residents of a country in a year, measured at the prices of the current year. For example, measurement of India's National Income of 2013-2014 at the prices of 2013-2014.

20. **The Business cycle/ Trade cycle**, also known as the economic cycle or trade cycle, is the downward and upward movement of gross domestic product around its long-term growth trend. The length of a business cycle is the period of time containing a single boom and contraction in sequence.

21. **Say’s Law of Market**: Say's law of markets is a classical economic theory that says that production is the source of demand. According to Say's law, the ability to demand something is financed by supplying a different good. An important element of classical economics is Say's Law of Markets, after J.B. Say, a French economist who first stated the law in a systematic form. Briefly stated, this law means that 'supply always creates its own demand.'

MODULE 2

22. **Aggregate demand**: It is the total demand for final goods and services in an economy at a given time. It specifies the amounts of goods and services that will be purchased at all possible price levels. This is the demand for the gross domestic product of a country. It is an economic measurement of the sum of all final goods and services produced in an economy, expressed as the total amount of money exchanged for those goods and services.
    Agg Demand = C+I+G+(X-M)

23. **Aggregate supply** or domestic final supply : It is the total supply of goods and services that firms in a national economy plan on selling during a specific time period. It is the total amount of goods and services that firms are willing and able to sell at a given price level in an economy.

24. **Effective demand**: It is the total demand for goods and services in an economy at various levels of employment. Total demand for goods and services by the people is

the sum total of all demand meant for consumption and investment. In other words, the sum of consumption expenditures and investment expenditures constitute effective demand in a two-sector economy. According to Keynes, the level of employment is determined by the effective demand which, in turn, is determined by aggregate demand function or aggregate demand price and aggregate supply function or aggregate supply price. In Keynes' words; "The value of D (Aggregate Demand) at the point of Aggregate Demand function, where it is intersected by the Aggregate Supply function, will be called the effective demand."

25. **Consumption Function** is a "functional relationship between two aggregates, i.e., total consumption and gross national income." Symbolically, the relationship is represented as C= f(Y), where C is consumption, Y is income, and/is the functional relationship. Thus the consumption function indicates a functional relationship between C and Y, where C is the depend at and Y is the independent variable, i.e., C is determined by Y. This relationship is based on the ceteris paribus (other things being equal) assumption, as such only income consumption relationship is considered and all possible influences on consumption are held constant.

26. **Marginal Propensity to Consume** : The marginal propensity to consume may be defined as the ratio of the change in consumption to the change in income or as the rate of change in the average propensity to consume as income changes." It can be found by dividing change in consumption by a change in income, or MPC – $\Delta C/\Delta Y$.

27. **Investment Function** : An investment multiplier refers to the concept that any increase in public or private investment spending has a more than proportionate positive impact on aggregate income and the general economy. The multiplier attempts to quantify the additional effects of a policy beyond those immediately measurable. The Size or Value of Investment Multiplier: The multiplier tells us how much increase in income occurs when autonomous investment increases by Rs. 1, that is, investment multiplier $\Delta Y/\Delta I$ is and its value is equal to 1/1-b where b stands for marginal propensity to consume (MPC).

28. **Liquidity Trap:** The liquidity trap is the situation in which the current interest rates are low and savings rates are high, rendering monetary policy ineffective. In a liquidity trap, consumers choose to avoid bonds and keep their funds in savings because of the prevailing belief that interest rates will soon rise. liquidity trap is a situation, described in Keynesian economics, in which, "after the rate of interest has fallen to a certain level, liquidity preference may become virtually absolute in the sense that almost everyone prefers [holding] cash [rather than] holding a debt which yields so low a rate of interest."

MODULE : 3

29. **The IS curve** represents all combinations of income (Y) and the real interest rate (r) such that the market for goods and services is in equilibrium. It shows inverse relation between rate of interest and national income.

30. **The LM curve** gives the combinations of income and the interest rate for which the demand for money (or desired liquidity) equals the money supply and hence for which the domestic economy is in asset or stock equilibrium.

31. **The Phillips curve** is an economic concept developed by A. W. Phillips stating that inflation and unemployment have a stable and inverse relationship. The theory claims that with economic growth comes inflation, which in turn should lead to more jobs and less unemployment.

32. **Stagflation:** It is a condition of slow economic growth and relatively high unemployment, or economic stagnation, accompanied by rising prices, or inflation. It can also be defined as inflation and a decline in gross domestic product (GDP). Stagflation occurs when the government or central banks expand the money supply at the same time they constrain supply. It is the economic phenomenon in which unemployment increases along with rising inflation causing demand to remain stagnant.

MODULE 4

33. **The Demand for money** is the desired holding of financial assets in the form of money that is, cash or bank deposits rather than investments. It can refer to the demand for money narrowly defined as M1. The demand for money balances is the total stock of money that the private sector wishes to hold.

34. **The Supply of money** is the total stock of money available for use in transactions, and held by the private sector. It includes all currency (notes and coins) in circulation, all checkable deposits held at banks (bank money). A somewhat broader measure of the supply of money is M2, which includes all of M1 plus savings and time deposits held at banks.

35. **Velocity of circulation of money** is the amount of units of money circulated in the economy during a given period of time. Description: Velocity of circulation is measured by dividing GDP by the country's total money supply. A high velocity of circulation in a country indicates a high degree of inflation.

36. **The Transaction velocity of money** is the rate at which money is exchanged from one transaction to another. It also refers to how much a unit of currency is used in a given period of time.

37. **The Income velocity of money**, is the frequency at which the average same unit of currency is used to purchase newly domestically-produced goods and services within a given time period.

38. **Core inflation** represents the long run trend in the price level. In measuring long run inflation, transitory price changes should be excluded. Core inflation is the change in costs of goods and services, but does not include those from the food and energy sectors. This measure of inflation excludes these items because their prices are much more volatile.

39. **Headline inflation** is a measure of the total [inflation] within an economy, including commodities such as food and energy prices (e.g., oil and gas), which tend to be much more volatile and prone to inflationary spikes.

40. **Reflation** is the act of stimulating the economy by increasing the money supply or by reducing taxes, seeking to bring the economy (specifically price level) back up to the long-term trend, following a dip in the business cycle. Reflation is a fiscal or monetary policy, designed to expand a country's output and curb the effects of deflation, which usually occurs after a period of economic uncertainty or a recession. Reflation policies can include reducing taxes, changing the money supply and lowering interest rates.

41. **Deflation** is a decrease in the general price level of goods and services. Deflation occurs when the inflation rate falls below 0% (a negative inflation rate). Inflation reduces the value of currency over time, but deflation increases it.

42. **Food inflation** refers to the condition whereby there exist increase in wholesale price index of essential food item (defined as food basket) relative to the general inflation or the consumer price index.

43. **Disinflation** is a decrease in the rate of inflation – a slowdown in the rate of increase of the general price level of goods and services in a nation's gross domestic product over time. It is the opposite of reflation.