Revision Notes

Class 12 - Economics

Chapter 1 - Macroeconomics

Macro Economics:

- The term macro is derived from the Greek word ‘makro’, which means “large”. It is a branch of economics concerned with the description and explanation of economic processes involving aggregates.
- An aggregate is a collection of economic subjects that have some characteristics in common.
- Macroeconomics emerged after the publication of John Maynard Keynes' book, ‘The Theory of Employment, Interest, and Money’ in 1936. This branch investigates the economic relationships or issues that affect an economy as a whole, such as saving and total consumption.
- It investigates the principles, problems, and policies associated with attaining full employment and expanding production capacity.

Economic Agents:

- Individuals or institutions making economic decisions are referred to as economic units or economic agents.
- They could be manufacturers or service providers who decide what and how much to produce.
- They could be entities such as the government, corporations, or banks that make economic decisions such as how much to spend, what interest rate to charge on credit, how much to tax, and so on.

Great Depression:

- The Great Depression is widely regarded as the worst and longest economic downturn or recession in modern history. It all started in the United States. It then had a cascading effect on the world's economies.
- The Great Depression is said to have begun with the October 1929 stock market crash in the United States. To be more specific, the stock market crashed on October 24, 1929, which became known as Black Thursday in American history.
- The stock market crash caused panic among Wall Street investors, causing the stock market to lose nearly billions of dollars. This resulted in the failure of major financial institutions, such as banks.
- The depression was caused by an overabundance of food grains in the market, which resulted in a drop in agricultural prices.

- During the war, Canada, Australia, and the United States emerged as new alternate wheat-producing centres. Stocks of finished goods began to pile up because of underconsumption and excessive investment, resulting in low prices and, as a result, low-profit margins.
- Money in the economy was converted into unsold finished goods, resulting in a sharp drop in employment and, as a result, income levels fell drastically. The economy's demand for goods was so low that production was reduced, resulting in unemployment.
- In the United States, the unemployment rate rose from 3% to 25%.
- The Great Depression has its own set of implications and significance in economics since it leads to the collapse of the classical economic approach.
- Those who believed in the market dynamics of demand and supply, created the ground for the Keynesian approach to emerge.
- This occurrence supplied economists with enough evidence to identify macroeconomics as a distinct field of economics.
- This flow chart summarizes the cause-and-effect relationship of the Great Depression:
  Low demand → Overinvestment → Low level of employment → Low level of output → Low income → Low Demand

Capitalist Country/Economy:
- In a capitalist country, capitalist enterprises perform a majority of the production activity.
- A typical capitalist enterprise has one or more entrepreneurs. They may provide the capital required to run the enterprise themselves or borrow it.
- According to Ralph Waldo Emerson – "Doing well is the result of doing good. That's what capitalism is all about."
- In this type of economy the means of production is privately owned.
- It is primarily governed by the price mechanism, with no intervention from the government.
- The government's role is solely to maintain law and order.
- Profit is the driving force behind these means of production.
- This economic structure is also referred to as a free-market economy or laissez-faire.
- Capitalist economies include Hong Kong, Singapore, Canada, the United Arab Emirates, Ireland, and others.

Important characteristics of the capitalist economy
- Private property
- No government interference
- Profit motive

- Freedom of enterprise
- Freedom of ownership
- Flexibility in labour markets
- Consumer sovereignty
- Price mechanism

Revenue:
Revenue is the amount of money earned from normal business operations and is calculated by multiplying the average sales price by the number of units sold.

Investment Expenditure:
Investment expenditure is defined as any expense incurred by an individual, a business, or the government for the development of new capital assets such as machinery, buildings, and so on.

Wage Rate:
The wage rate is the price charged for the sale and purchase of labour services.

Wage Labour:
Wage labour is defined as labour that is sold or purchased in exchange for a wage rate.

Entrepreneurs:
An entrepreneur is an individual who takes the risk of starting their own business based on an idea or a product they developed, assuming most of the risks and earning most of the gains.

Main Objectives of Macro Economic Policies:
Macroeconomic policies are implemented by the government or statutory bodies such as the Reserve Bank of India (RBI), the Securities and Exchange Board of India (SEBI), and other similar organisations.

1. Sustainability
2. Price stability
3. Full employment
4. External balance
5. Social objectives

Four Major Sectors of Economy from Macro Economic Point of View:
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These four functions oversee four expenditures on Gross Domestic Product (GDP).

i) Household Sector: This sector covers everyone, consumers, individuals, and every member of society. The household sector purchases products and services for consumption while also supplying producing inputs such as land, labour, capital, and entrepreneurs. This sector oversees the consumption expenditures component of GDP.
In a nutshell, a household is defined as a single or group of people who make independent decisions about their economic activities, such as consumption and production.

ii) Firms: People in the household sector work as workers in firms and make a living. Firms are economic units that produce goods and services. They utilise and organise production factors and carry out production processes for the purpose of profit.
This comprises sole proprietorships, partnerships, and corporations. This sector oversees the GDP's investment expenditure.

iii) Government Sector: A government preserves law and order, promotes growth and stability, and administers government services. This sector is in charge of the government's purchase involvement in GDP.
A government's primary goal is to levy taxes to fund development projects such as dams, roads, and heavy industries, which typically have extended gestation periods.
The government also invests in education and health sectors and delivers these services at a low cost. Examples include the Department of Transportation and the Environmental Protection Agency.
iv) Foreign/ External Sector: This sector deals with the export and import of products and services. Export occurs when domestically produced goods and services are sold to the rest of the world. When goods and services are purchased from the rest of the world, this is referred to as import.
Apart from the export and import of goods, there can be an inflow of goods, i.e., a country welcoming capital from other countries, and an outflow of foreign capital, i.e., investing in foreign countries. Net exports(Exports minus Imports) are the foreign sector's expenditure on GDP.