

SECTION - I

Chapter - 1.1

Meaning and Definitions of Economics

Human being is a social animal and Economics is a social science. Living in the society, human being performs many economic activities. Human being purchases goods for satisfying the needs of individuals and family, performs agriculture, establishes industries, sells produced goods, does services, works in industry and gives services for earnings. All these are the economics related activities.

Economics is the study of the complete work organized by human being. Economists like Samuelsson calls Economics as the Queen of social science. The whole structure of Economics is based on two things:

1. Resources which are scarce,
2. Wants which are unlimited

Human being and society produce goods and services by using scarce resources economically and thus they satisfy their wants.

Definition of Economics :

Before study any subject, it should be defined because the definition provides the subject matter, nature and scope of a subject. Economics is a growing subject. Because of the difference in the nature of economic activities and the continuous changes in them the economists are not having the same views on the definition of Economics. Different economists had given different definitions of Economics time to time and each

economist had defined Economics according to the circumstances. Smt. Barbara Wotten correctly said "there are seven views where there is six economists." For the simplicity there are five types of definitions of Economics, namely:

- (a) Wealth centered definitions
- (b) Welfare centered definitions
- (c) Scarcity centered definitions
- (d) Wantlessness definition
- (e) Development based definitions

a. Wealth Centred Definitions:

Prof. Adam Smith, J.B.Say, Walker, and other economists gave such definitions of Economics whose centre point was "wealth". In the book of Prof. Adam Smith "An Enquiry into the Nature and Causes of Wealth of Nations," publish in 1776, The Economics was defined as "Economics is the science of wealth".

According to Walker, "Economics is that branch of knowledge which is related with wealth."

According to J.B.Say, "Economics is the science which studies the wealth."

All the classical economists assumed that the ultimate objective of economic activities of human being is to earn wealth. Many thoughts had been developed which created illusions in Economics. This resulted into the view that

Economics considers the human being who loves wealth or money. But in the beginning of the 19th century some economists started by saying that wealth is a mean for the human life and thus it is not correct to relate Economics with the analysis of emergence of the wealth. This view was criticized.

Criticism :

i. More Emphasis on Wealth:-

In these definitions more emphasis has been given to wealth. Wealth has been considered to be a goal of end while to get wealth is not a goal but a mean which is used to satisfy the wants.

ii. Improper Imagination of Economic Human Being:

According to the old economists work done by human being is governed by wealth incentive and selfishness. But this is wrong thinking. In reality, human being gets worked being governed by the incentive based on love, pity and other human spirits.

iii. Narrow Scope of Economics:

Under these definitions of Economics wealth included only the physical goods and thus services (doctors, engineers, avocats, teachers, etc.) have been ignored. Thus the scope of Economics has been narrowed down.

b. Welfare Centred Definitions :

In 19th Century, economists like Prof. Marshall, Pigou and J.S.Mill explained that the objective of Economics is not to analyse the nature and origin of wealth only. It is more important to analyse the fact that wealth should be used to satisfy the wants and to increase the material welfare of the society rather than to analyze the nature and origin of wealth. Marshall emphasized economic welfare of human being more than wealth.

According to Marshall- "Economics is the study of common business of human life. Under this that part of individual and social activities is evaluated which is deeply related with the consumption and the achievement of the resources of material bliss."

According to Pigou, "Economics studies the economics welfare and it is limited upto that part of welfare which can be directly or indirectly related with money as the measuring device,"

In brief, according to Marshall, Pigou and other economists Economics is the study of "material welfare".

Explanation of Definition of Marshall

The main points of definition given by Marshall are given as below:

1. Human being more Important than Wealth:

Marshall emphasized human welfare more than wealth. According to him "wealth is for human being and human being is not for wealth." Thus human welfare is most important.

2. Study of Human Being as Social, Normal and Real:

Economics studies the activities performed by socials, normal and real human being. Economics does not study economics activities of abnormal, unsocial and unreal people like saints, etc.

3. Study of Normal Business/Occupation of Human Life:

Marshall studies the normal occupation in Economics. political, social, moral, religious and cultural aspects of human activities are not studied in Economics and thus only economic aspects are studied. This economic aspect includes the activities of production, consumption, exchange, distribution and public finance.

4. Study of Material Welfare of Human Being:

According to Marshall human being is a social animal. Thus, study of Economics includes only those activities which are directly related with the wealth and increase of material welfare from the wealth.

Criticism of Welfare Centred Definitions:

In 1932 Prof. Robins, in his book "An Essay on the Nature and Significance of Economic Science", said that the welfare centered definitions of Economics are narrow, impractical and illusory and Marshall and his supporters criticized these definitions as below:

1. Improper Classification of Recourses as materials and Non-Material:

Marshall limited the subject matter of study of Economics only upto the consumption of and obtaining the material resources. But in reality resources are non-material also, e.g. doctor, engineer, labourer, advocate, etc. who render their services and thus these services are also studied in Economics.

2. Economics is not a Social Science only:-

It is not correct to consider Economics as social science only because economic laws are applied on people who live in society as well as on people who do not live in society. So Economics is a human science. For example, law of diminishing marginal utility, law of equi-marginal utility and other laws are equally applicable on all people.

3. Improper to Establish the Relation of Economics with Material Welfare :

According to Robins, the relation of Economics cannot be established with the causes of material welfare. Robins considered the concept of welfare as defective on the basis of these grounds.

- i. These are such activities whose production and consumption is not welfare oriented, as

liquor, but these are studied in Economics.

- ii. Welfare can not be measured with proof. Welfare can not even be measured in terms of money because welfare is a psychological and spiritual feeling.

4. Economics is Indifferent to Objectives:

When the relation of Economics is established with welfare it means that economists have to take decisions about good and bad economic activities which becomes related with normative science. Robins considers Economics as a positive science which does not take decisions about good and bad economic activities but decides on the ground of reality.

5. Narrow Scope of Economics :

According to Marshall economics does not include the production and consumption of non-material resources, unsocial and non-economic activities and these the welfare centered definitions are criticized also.

(c) Scarcity Centered Definitions:

Prof. Robins gave a new approach to Economics. He emphasized more neither to wealth nor to human welfare but he tried to establish the relation between unlimited wants and limited resources. Robins defined Economics with a new approach.

According to Robins, "Economics is the science which studies the human behavior related with the ends and the limited an multi-use resources." Thus Robins gave a new definition of Economics in which following four points are important :

- i. Human wants (ends) are unlimited and infinity
- ii. Resources with people are limited which have to be used to satisfy human wants. In this situation people have to face the problem of choice of wants.
- iii. Resources have their alternative uses. Due to

this the scarcity of resources increases more and thus problem of choice has to be solved. The problem of choice is always there with us.

- iv. There is difference in the intensity of needs some needs are more intensive while some are less intensive. This difference in the intensity of needs helps in the solution of the problem of choice. A rational person keeps his/her needs according to the preference.

It is clear from the above analysis that wants are unlimited and resources are limited and thus there is the problem of choice to be faced by human being. Robins calls it as the economic problem.

Criticism of Robins Definition:

Economists do not consider the definition of Economics given by Robins as errorless. Following are the criticisms:

1. Scope of Economics Wider than Need:

Robins considers Economics as a human science and its subject matter thus becomes the choice of all types of human activities. It makes the scope of Economics wider and thus the formulation of economic theories, analysis of economic problem and their description have become more complicated.

2. No Proper Attention to Social Character of Economics:

According to Robins the activities of people living out of the society are also studied. But Economics is required only when economic problems take the form of social problems and thus activities of one human group affect the activities of another human group.

3. Economics not only the Theory of Value:

The definition of Robins studies only the fact that how the factors are allocated in the production of different goods and as result of this how the factor prices are determined. But scope of

Economics is much wider than the resource allocation and the resource price determination.

4. Indifference of Objectives:

According to Robins, Economics is related only with resources. It studies how the objectives, for which the limited resources are used, are determined. If we do not know the correct information about objectives, we can not make the maximum use of resources. If Economics is indifferent to objectives, then there will be no importance of economic plans in the present era.

5. Economics not only a Positive Science but an Art also:-

If Economics is assumed to be a positive science then it remains a subject of only the theory formulation. According to economists who criticize the Robins definition, Economics not only aims to manufacture equipments but to show the way of their application also. Thus Economics is normative science and is also along with the positive science.

6. Static Definition:

Robins assumes that ends are constant or stable which are always changed in practical life and thus resources are changed. Thus the nature of definition of Robins is static and lacks dynamic nature.

7. Cause of Economic Problems:

Economic problem is created due to scarcity. This statement of Robins is not correct. Opposite viewers are of the view that economic problem is not only due to scarcity but it is due to abundance also. For example, the cause of 1930's economic depression was the over production.

Thus, even after having some demerits, definition of Robins is logical and it strengthens the scientific foundation of Economics. This definition gives more importance to the issue of choice making. In recent years the importance of "Economic Growth" has increased and the issues of national income, increase in per capita income,

growth of productive capacity, etc. are not found in this definition.

(d) Wantlessness Definition:

The famous Indian economist and Professor of Allahabad University, Prof. J.K. Mehta, defined Economics in the view of Indian ethics. This definition of Economics is completely different from the western approach and is based on wantlessness. The western approach is concerned with the satisfaction of maximum needs while Indian approach is concerned with reduction of needs or ending the needs rather than satisfying the maximum needs. According to Indian approach the maximum satisfaction can not be obtained by want satisfaction but can be obtained by reducing the number of wants.

Thus according to Prof. Mehta, "Economics is the science which studies how the human behavior can be reached into the state of wantlessness." Following facts are clear from this definition-

1. Human behavior is governed by the lack of mental peace and balancelessness. According to Prof. Mehta, this balancelessness is the result of the difference between human wants and resources available to satisfy these wants.
2. The ultimate objective of human being is to get happiness in the life. Human mind is completely balanced in the state of wantlessness and this is the happiness. The ultimate objective of Economics is to maximize this happiness.
3. According to Prof. Mehta the objective of Economics is not to increase the satisfaction but it is to increase the real happiness in the life. The real happiness can be obtained by reducing the wants.

Prof. Mehta says that human being can experience the real happiness only in the

state of mental balance. There are two methods of achieving the mental balance:-

- i. To reduce the difference between wants and the resources to satisfy these wants.
 - ii. Mental state should not be affected by external forces.
4. To achieve the wantlessness human being should reduce the resources upto that limit so that mental imbalance can not be created. Human being should reach the ultimate objective so that no want can be experienced.

Criticism of Prof. Mehta's Approach:

Economists criticized the definition of Economics given by Prof. Mehta. According to them modern period is the materialistic period in which wants can not be reduced. Material wants are increasing continuously. Following are the main criticisms:

1. Difficult Imagination of Wantless Human Being:

In the modern time nobody is ready to sacrifice wants and tries to get the maximum bliss or happiness. People think that bliss and sorrow are the two unseparate parts of human life and thus are associated with the life. Wants can not be reduced.

2. Improper Concept of Maximum Bliss:

The critics consider the concept of Prof. Mehta as contradictory. According to them, on one hand, Prof. Mehta talks to reduce wants and on the other hand explains the concepts of maximum bliss. Practically, when we try to reduce wants slowly we feel mental dissatisfaction. In this situation it is not possible to get the maximum bliss or happiness.

3. Existenceless Economics:

Economics is mainly based on the unlimitedness of wants. If needs are reduced slowly and thus wantless situation will be

obtained. As result, it will end all the economic activities automatically and thus Economics will become existanceless.

4. Economics Completely not a Normative Science:

Prof. Mehta considers economics a normative science while Prof. Robins considers Economics a positive science.

In reality Prof. Mehta imagines such period which is not possible in the today's materialistic world. It is not also correct to say that the approach of Prof. Mehta is associated with the life of poor, saints, etc. Prof. Mehta advocates the achievement of real bliss or happiness in the life.

(e) Development Based Definitions:

Modern time is the time of development. So there have been changes in the definitions as Economics with development of the subject of Economics. After the definition the of economics given by Robins (1932) the subject matter of Economics has changed a lot. Specially the subject matter of economic development has been changed drastically. Now such type of definition of Economics should be given which emphasizes more the economic development rather than only the distribution or allocation of limited resources. Modern economists like Samuelson, Peterson, Ferguson, etc. defined Economics.

According to Samuleson, "Economics studies that how individuals and society allocated the limited resources (with alternative uses) in the production of goods and how these goods are distributed among different groups for the consumption in present and future times by using money or by not using it" This definition of Samulelson can be understood as below:

1. Samuleson gives more importance to the choice behavior of human being and the scarcity of resources.

2. According to Samuelson the problem of resource allocation under barter system is important.
3. Definition of Samuelson is dynamic. This definition includes the elements of both the definitions given by Marshall and Robins.

According to Prof. K.G.Seth- "Economics studies that human behavior which is related with the development and changes in resources in reference of the ends."

According to Prof. Hicks,- "Economics studies the specific aspects of human behavior. Economics is that science which studies the business activities." Modern economists present the development and welfare oriented approach of the Economics which is nearer to the positivity.

Important Points:-

- Economics is a developing and dynamic subject.
- Economists are not having same view on definitions of Economics.
- The wealth centered definitions have been given by Adam. Smith, J.B. Say, Walker, etc.
- In Wealth centered definitions of Economics wealth is the central point.
- Welfare centred definitions of Economics have been given by Marshall, Pigou, etc.
- The central point of welfare centred definitions is the human welfare and not the wealth.
- Scarcity centred definitions have been given by Robbins in which the relation between human behavior and scarce resources, with many applications, is studied.
- Prof. Samuelson gave development centerd definitions in which the growth and development of resources are emphasized.

- The wantless definition of Economics has been given by Prof. J.K. Mehta.

Questions For Exercise:

Objectives Type Questions:

- Who gave the wealth centred definition ?
(a) Marshall (b) Samuleson
(c) Adam Smith (d) Robins ()
- Who gave welfare centered definition of Economics ?
(a) Robins (b) Pigou
(c) J.K. Mehta (d) All of the above ()
- The definition "Economics is the study of economic welfare" is related with –
(a) Wealth centered definition
(b) Economic development centered definition
(c) Welfare related definition
(d) Scarcity centered definition
- To which definition the effort to establish the relation of unlimited wants with limited resources, is concerned ?
(a) Wealth Centered Definition
(b) Economic Development Centered Definition
(c) Scarcity Centered Definition
(d) Welfare Related Definition
- Who considers Economics as the positive Economics ?
(a) Marshall (b) Pigou
(c) Robins (d) J.S. Mill ()
- What is the wealth centered definition of Economics according to Smith ?
- Give the scarcity centered definition of Economics.
- What type of science is the Economics according to Marshall ?
- Who is the economist according to whom Economics is the science of choice ?
- What type of science the Economics is according to Robins ?
- What is the wantlessness centered definition according to J.K. Mehta?

Short Answer Questions:

- Write any two criticisms of the wealth centered definitions.
- According to Marshall the main subject matter of Economics is the human welfare and not the wealth. Explain it.
- What is economic problem according to Robins ?
- What are the main elements of the development centered definition of Economics ?

Essay Type Questions :

- Analyse critically the definitions of Economics given by Marshall and Robins.
- Critically describe the welfare centered definitions of Economics.
- Critically evaluate the development centered definitions of Economics. Explain the Indian approach in this regard.
- "Economics was science of wealth, now it is science of human being." Explain this statement.
- Critically describe the "Scarcity" definition of Economics.

Very Short Answer Questions:

- Write the thoughts of Marshall about Economics.

Answer to Objectives Type Questions:

(1) c (2) b (3) c (4) c (5) c

Reference Books :

1. Marshall – Principles of Economics, 8th Edition.
2. Joan Robinson- The Second crisis of Economic Theory (1974).
3. Boulding- "Principles of Economy
4. Robins - Nature and Significance of Economic Science.

Chapter - 1.2

Nature and Scope of Economics

The issue of different approaches to define Economics is a debatable one which created many problems in determination of the proper area of research in this subject. Economics is a developing dynamic social science. We study all economic activities in Economics. There are many different views in economics about nature and scope of economics because of the continuous changes in economic activities of human life and naturally contradictory definitions of economics. According to some economists the scope of economics is narrow but some other economists consider it to be broad. Prof. Keynes includes three elements in the scope of economics.

- (1) Subject matter of Economics
- (2) Nature of Economics
- (3) Relation of Economics with other sciences.

Subject Matter of Economics:

Following are the main approaches to the subject matter of economics.

1. Classical View :

Adam Smith, J.B. Say, Senior, J.S. Mill, etc. are the supporters of this approach. In the wealth centered definition given by Adam Smith economics relates with earning and accumulating wealth. According to this approach issues like what is wealth, how it is utilized, how it is distributed, etc. are studied in economics.

2. Welfare Economists' Approach:

According to Marshall, Pigou and some other economists the main subject matter of economics is human welfare instead of wealth and thus wealth is for people and people are not for wealth. According to Marshall, only economic activities related with physical welfare are the subject matter of economics. Robins's scarcity centered definition extended the scope of economics. Robins considers economics as humanity based science and thus economic choice between limited resources and unlimited wants became the subject matter of economics.

As result of continuous division of economic activities the subject matter of economics became broad. The subject matter of economics can be divided in five parts as consumption, production, exchange, distribution and public finance.

1. Consumption:

Consumption is the economic activity which is related with utilization of utility of goods and services for direct satisfaction. Consumption is both the start and end of economics because all the economic activities like production, exchange, distribution, etc. are performed for consumption only.

2. Production :

Production related with the creation of utility or value of goods and services. The activity of making bread is production. Land, labour,

capital, organisation and entrepreneurship are the main factors of production.

3. Exchange:

The activity of exchange is related with buying and selling of good or factor of production. Exchange is required for the consumption of produced goods and satisfaction of wants. Due to the problems in barter system money was discovered which made the activity of exchange simpler. Now, we use money in selling and buying of goods and factors of production. Theory of price determination is based on money.

4. Distribution :

The joint effort of all the factors of production results in to production. So determination of rate of payment to factors of production is necessary which is related with the income distribution among factors of production. Under income distribution it is known that what is national income, how is national income calculated, how interest, wage, rent and profit are determined It is also ensured whether the distribution of national income is in a justified way. Presently the state interference is continuously increasing.

5. Public Finance :

In this activity we study the issues related with public revenue, public expenditure, public debt, deficit finance, tariff policy, etc. The subject matter of Economics has changed with the time.

Nature of Economics:

Under nature of economics, following issues are considered.

1. Is economics a science ?
2. If economics is a science, is it positive science or normative science ?
3. Is economics an art ?
4. Is economics both science and art ?

1. Is Economics a Science ?

The systematic and complete study of

knowledge which explains the cause and effect relationship is known as science. Science analyses and studies any event. This study is of the systematic nature. On the basis of this analysis and study for casting can be possible. On the basis of the following arguments it can be said that economics is a science.

(a) Use of Scientific Method :

Economics uses the scientific method to study cause and effect relationship between two or more variables and to construct or formulate the economics theories and laws. The behavior of individuals and groups is observed, hypothesizes are formulated & tested and then economic laws are constructed. Clearly speaking, economics uses the scientific method.

(b) Power to Explain:

Economics has the power to explain the economic phenomenon correctly and sufficiently after construction of general laws.

(c) Power of Prediction :

Because economics has the explanatory power so it can predict the economic phenomenon. The power of prediction of economics has increased more due to the use of mathematical & statistical tools and application of modern computers and more development of economic policy.

(d) Systematic Study:

Economics studies only the activities relating with wealth like consumption, production, exchange, distribution, etc. This study of all economic activities is a systematic one.

(e) Validity of Laws:

In every science the validity of laws is tested. Economic laws are based on human nature which is equally applied on the people of all the countries of the world.

(f) Cause and effect Relationship:

Many economic laws (law of diminishing

marginal utility, law of equi-marginal utilities, law of demand, etc.) explain the cause and effect relationship. Thus economics is science on this basis.

Economics is a Science - Arguments Against It:

Many economists do not consider economics as a science on the basis of the following arguments :

(a) Lack of Uniformity:

There is no uniformity about any special event of economics. In other words, analysis of any event can not be done in single way. There are different ways to analyse any event used by different economists.

(b) Disarguments:

There are disarguments among economists on the issue of considering economics as a science. They do not consider economics as a science.

(c) Not Objective :

Economics can not be an objective subject like natural sciences because its subject matter is human being. Economics studies human related economic activities and not the non-living goods. Economist is also a human being so his approach and opinion affects his analysis and research studies. In this way economics can not be objective science.

(d) Economic Laws are not Exact :

Laws of natural sciences are general and completely certain, for example, The law of gravitation. But laws of Economics are not completely certain.

2. Positive Science and Normative Science:

If Economics is a science then the question is to decide whether economics is positive science or normative science. Before the explanation, it will be appropriate to understand their meaning-

Positive Economics :

As Positive economics, Economics studies the relationship between causes and effects. It explains that what is it? Why is it ? and how is it? Positive economics does not relate with goodness or badness, correctness or wrongness of economics functions. It is based on rationality.

Normative Economics : Normative Economics explains the policy related facts, like what ought to be, what should be done in given situation, etc. as normative science highlights the goodness and badness of economic functions.

Arguments in favour of Economics is Positive Science :

Classical economists, Prof. J.B. Say, Senior, and modern economist Robins consider economics as positive science. According to Robins, "Economics studies testable facts while ethics studies the facts of evaluations and discoveries."

- i. Positive approach in economics gives systematic, logical and correct economic conclusions because logic is the base of cause and effect relationship.
- ii. Positive approach can postulate strong economic theory on the basis of positive assumptions and scientific analysis.
- iii. If only the positivity of economic activities are studied in economics then differences in economists will be less, they will be having more common views and nature of economics will be more intensive.
- iv. According to Robins, human being must work according to the best efficiency keeping in view the scarcity of resources. People should do that work in which they have specialization. If all the activities are done, the time and money are wasted. Thus, economists must keep themselves limited upto causes and effects. Economists should

not touch the issues relating with what should be done and what should not be.

Arguments in favour of "Economics is Normative Science :

Fraser, Henderson and Quandt and some other economists considers economics as normative science. Following arguments can be given in this favour-

i. Human being is sensitive and logical :

Human being is sensitive and logics oriented so it is necessary to study both approaches of human behavior namely positive and normative. Thus economics is both positive science and normative science.

ii. More Useful:

Economics really aims the social welfare so, use of economics as normative science is more important. Economists should also think (alongwith the study of economic activities) how these activities can be more useful and effective.

iii. Wrong Argument of Division of Labour:

It is not correct to say that economist should study a subject, explain the cause and effect relation and the responsibility of getting solutions to be given to ethicists and political leaders. As result of this the positive analysis will become interest less and without incentives and thus there will be no saving of labour and power. So, capacity of taking decisions should be given to economists.

iv. More Realistic:

The nature of economics is a changing phenomenon. Today Economics is being developed rapidly as welfare economics. Subjects like economic planning and social security have become vary important. In this situation the normative approach of economics can not be ignored. More realistic situation will take place when economists give suggestions about concrete measures like rapid economic

growth rate, increase in employment levels and economic stability.

v. Helpful in Social Betterment :

If economics works for social betterment then the normative approach to economics can not be forgotten. Economics is social science also.

It is clear from above analysis that economics is both of positive and normative science. Economics can be considered as pure and realistic economics.

3. Economics as an Art:

Economists do not have same opinion whether economics is an art. Adm Smith, Ricardo, Mill., Marshall, Pigou etc. say that economics is an art. While Walras, Shumpeter, Senior and some economists do not consider economics as an art.

Before judging whether economics is an art, we should look into the meaning of art.

Meaning of Art :

Generally getting any work done with efficiency is known as art. Art provides us applied knowledge. Art not only analyses the problem but it solves it also. Prof. Keynes says- Art is that branch of knowledge which shows the best way for the satisfaction of certain objectives.

Arguments Against Treating Economics as an Art :

Following are the arguments in this regard-

- i. There is difference in the nature of art and science. Science discovers something and then explains it while art gives the applied information of a subject. Science constructs theories while art gives the real shape to these theories. So, if economics is considered as science it can not be an art.
- ii. Economic problems are not always economic but they are also affected by

social, political and religious circumstances. So it is not possible that economists frame proper policy for the solution of problems only on the basis of the economic approach.

- iii. Policy making is not the only work of economy but it analyses the problems also. Economic theories do not give such definite conclusions which can at once be used as policies. Economics is a method not a faith. When economic laws can not at once be used in policy making, it is not correct to consider economics as an art.
- iv. Economics is just like the pure science so to keep this type of nature of economics maintained it is not correct to consider economics as an art. Economist should work as an expert only.
- v. According to Keynes, theories of economics do not give such perfect conclusions which can be used in policy framing at once. This is a way of analysis, a method of thinking and an instrument of the mind which helps in deriving the correct conclusions. It means economists do not provide solution of economic problems at once.

Arguments in Favour of Treating Economics as an Art:

These arguments are as given below:

- i. Last decision on the purely economic problems can be taken only by economists. For example, problems of exchange rate, bank rate, etc. are associated with economists who solve them. Political leaders can decide the employment policy, tax policy, etc. when they have the sufficient economic knowledge.
- ii. The one of the main objectives of economics is to maximize the welfare of individuals or society. To achieve a certain goal, framing policy by government can be considered to be an art.

- iii. As science economics postulates theories and laws which are verified when these theories and laws are implemented. Thus the applied use of economic laws and theories makes economics an art.
- iv. Importance of applied economics is continuously increasing. Most of time of economists is being utilized in solving the real problems of life as inflation, unemployment, economics growth, etc. So it is correct to consider economics as an art.
- v. If economics is studied as an art it will be helpful in verifying the economic theories and thus it will be known whether economic theories are correct. This helps in the postulation of new theories.
- vi. In present time the planning system is becoming the base of whole of the world. Most of the countries of the world are trying to achieve higher level of economic growth through planned economic growth strategies. For this economics should be studied as an art.
- vii. The art form of economics does not create any problem in its scientific nature. It is not only sufficient to search truth in economics but it is also necessary that this truth should solve the economic problems. Economics should also be helpful in the solution of human problems also.

4. Real Nature of Economics :

Economics is Science as well as Art.

It is clear from above analysis that economics is both science and art. As a science Economics is both positive science and normative science. Economics studies both theoretical and applied aspects of a subject. The theoretical aspect relates with the scientific nature of economics while the applied aspect relates with the art.

Theoretical economics is science and applied economics is art. As a scientist, an economist has two types of role as a scientist and as a good citizen. Koussa rightly says, "Science requires art and art requires science. Both are complementary to each other."

Important Points :

- Economists are having different views on nature of economics that whether economics is science or art or both science and art.
- Subject matter of economics is divided into 5 parts- consumptions, exchange, distribution, production and public finance.
- Economics is both positive science as normative science.
- Economics is human science also which studies moral decisions related with different economic phenomena.
- Science is that branch of study which relates with the analysis of cause and effect.
- That branch of study is known as art which suggests the best way of getting definite objectives fulfilled.
- A new branch of economics is "development economics" in which we study the main elements, criteria, etc. of development.

Questions for Exercise:

Objective Type Questions:

1. Normative Science is related with.
 - (a) What is
 - (b) What should be
 - (c) Where is
 - (d) Where was ()
2. Positive science is related with.
 - (a) What is
 - (b) Where was
 - (c) Where is
 - (d) Where was ()
3. 'What should be' is the subject matter of –

- (a) Positive Science
- (b) Normative Science
- (c) Art
- (d) None of Above ()

Very Short Answer Questions

1. What are the parts in which the subject matter of economics is divided ?
2. What is consumption activity ?
3. What is production activity ?
4. What is distribution ?
5. What is exchange ?
6. What is positive science ?
7. What is normative science ?
8. What is an art ?
9. What are the questions solved by economics as a normative science ?

Short Answer Questions.

1. Explain the parts of subject matter of economics.
2. Explain the statement "Economics is positive science."
3. Explain the statement "Economics is normative science."
4. "Art is the action or activity on doing any work in the best way". Explain this statement.

Essay Type Questions:

1. Economics is science or art or both. Explain.
2. Explain the nature and scope of economics.
3. What is the meaning of science ? Is economics a science ? Explain.
4. Economics is positive Science or normative science or both. Explain.

Answer to objective Type Questions

(1) b (2) a (3) b

Reference Books :

1. Marshall - Principles of Economics, 8th Edition.
2. Joan Robinson- The Second Crisis of Economic Theory (1974).
3. Boulding – Principles of Economy
4. Robins – Nature and Significance of Economic Science.

Chapter - 1.3

Economy or Economic System

Meaning of an Economy :

"By economy we mean the legal and institutional structure in which all the economic activities are performed." It is clear that in the institutional structure where human related economic activities of consumption, production, exchange, distribution and finance are performed is known as economic systems or economic organization. In an economy people earn their living and under economic system the ways of working, rules and institutions of persons are included by which the economy is run.

Definition of Economy:

Many economists have defined economy or economic system. In words of **Prof. A.J. Brown,** "Economy is mostly used for such system by which people earn their living." In simple words, by economy or economic system we mean that system by which people of any area cooperate with each other to produce goods and service so that they can satisfy their wants.

In Present time economists put more emphasis on the aspect of economic growth and economic development. So in all nations human economic activities are more or less affected by the state and thus the nature of economy or economic system is mostly depends on the interference of the state, nature and social customs.

Salient Features of an Economy :

Following are the salient Features of an

Economic System:

1. Base of Economy is the Human Group:

The concept of economy is related with the way of living of people of a special private area who become part of the production process to earn living and thus satisfy their wants. Thus economy is human made and studies economic activity.

2. Essential Processes of Economy :

There are three essential processes of economy, namely- production, consumption and investment which are related with the living of individuals and groups. These processes are run continuously in life.

(a) Production :

In this process we include production of goods and services which depends on needs, efficiency, technique and quantity of economic resources.

(b) Consumption:

Under consumption goods and services are used to satisfy the wants of human groups.

(c) Investment:

The net increase in the capital stock in the current year in comparison to the last year is known as investment.

3. Exchange is Necessary for Economy :

The ultimate aim of consumption is to

satisfy the consumer wants. In all economic systems there is freedom of consumer choice and for it exchange is required, e.g. food shops, consumer stores, etc.

4. Government Control Over Economy –

There are many development responsibilities over the economy or economic system. Thus, now the ‘Policy of Freedom’ of capitalism is not much believed and the important role of government is accepted more. Economic growth rate and level of employment can rapidly be increased through the coordination of monetary and fiscal policies.

Forms of Economic Organization or Economic System :

The factors like increasing state interference, different nature, social laws, economic customs and structure of economic organization have effect on the economic activity being performed by people. Due to this there are many forms of economic system. The economy can be classified according to the below given bases.

Classification of Economy

Base of Classification	Types of Economy
Ownership of factors of Production	Capitalist Economy Socialist Economy Mixed Economy
Level of Development	Developing Economy Developed Economy

All the above forms of economy can briefly be analyzed as below:

Capitalism or Free Economy:

The capitalism or capitalist system emerged in 18th century in England and Europe with the industrial revolution. Capitalism is the economic system in which the resources of distribution and output are owned and controlled by private hands.

In the words of Ferguson and others, "Capitalism is that system in which there is private property and economic decisions are taken privately."

Main Characteristics of Capitalist Economy

Following are the main characteristics of the capitalist economic system-

1. Right to Own Private Property-

In capitalism every person has the right to own private property which can be used according to the own desire. Private property can be transferred to the future generations on the basis of inheritance.

2. Economic Freedom :

In capitalism each person has the freedom to use the own property and to choose the industry according to the own will and need.

3. Consumer's Sovereignty :

In this economic system there is a very important place of the consumer's sovereignty. Consumers are free to consume according to their own interest and preference.

4. Objective of Private Profit :

In capitalism the main objective is to get the private profit. Each work is governed by the objective of the private profit.

5. Competition :

There is competition between buyers and sellers in the goods and factor markets in the capitalism.

6. Price Mechanism :

In capitalism all the economic activities are governed, coordinated and controlled by the price mechanism and not by any central authority.

Merits of Capitalism:

We find following merits in the capitalism :

1. Effective Production :

Due to profit incentive and perfect competition each entrepreneur produces good quality and durable products. The producer use the new techniques of production. It is also tried to keep the cost of production at the minimum level.

2. Flexibility :

An important merit of capitalism is that it is flexible form of economy. It has the power to change itself as per the need of the time.

3. Development of Individual :

Under capitalism each person tries to increase own ability because success goes to the best person.

4. Increase in Standard of Living:

There is diversity in production of goods which results into the large scale production and the levels of cost and price are lower. Thus the life standard of poor persons increase in capitalism.

5. Optimum Use of Resources :

The only objective of producer is to earn profit so the available resources are used optimally. These resources are used in the economic manner in capitalism.

6. Automation :

The price system plays important role in this type of economy. There is not any type of interference from any side.

7. Technical Progress :

There is mutual competition among the producers in capitalist economy. Each producer tries to produce maximum output at the minimum cost. Producers use new techniques of production. This all results into capital formation.

Demerits of Capitalism :

There are many good points in favour of

capitalism but it is not free from some demerits. These are:

1. Unequal Distribution of Income and Wealth :

In capitalism there are inequalities in the distribution of income and wealth. This is due to the presence of factors like inequality of private property, free competition, desire to earn more profit, etc. Thus rich becomes richer and poor becomes poorer.

2. Class Struggle :

The inequality of incomes and wealth divides the society in two classes in capitalism as rich class and poor class. The rich class leads a wealthy life while poor class (labour class) is not able to arrange even two time meal. This situation gives birth to class conflict further.

3. Trade Cycles and Economic Unstability :

Due to Automation there are ups and downs in economic activity always in capitalism. Sometime there is inflation and sometimes there is deflation in the economy. During inflation the levels of price and output increase rapidly and during deflation price, employment and output levels decrease. Thus, trade cycle and economic unstabilty take place in capitalism.

4. Unemployment and Social Insecurity:

As results of trade cycles, unemployment is created in the economy. Labourers do not get work and they become dependent on the rich class. The labourers have low level of income due to unequal distribution of wealth and thus they always face the insecurity in their life. In accidents, unemployment, disease, and old age they get less sources of income.

5. Exploitation :

There is maximum exploitation of labour class in capitalism. Labourers do not get wages according to their marginal

productivity. They get very low wage rates and thus the labour class is exploited.

6. Unearned Income and Social Dependence :

In capitalism some people get income due to private ownership in property and inheritance laws and thus they get unearned income without any effort. Landlords get rent and capitalists get interest and rent and they live on the labour of others generation to generation.

7. Lack of Public Welfare:

Under capitalism entrepreneurs are governed by own profit motive and due to this they use resources for national product. But their objective is to earn maximum profit so they have interest in the production of those goods only which give maximum profit, for example, luxuries. The producers are less interested in producing the goods of public welfare.

8. Other Demerits :

Some other demerits of capitalism are as given below:

- i. There is uneconomic use of resources in capitalism due to cut throat competition.
- ii. Some collusions can be emerged which reduce the competition or by showing artificial shortage of goods the way of exploitation is created.
- iii. Lack of coordination can be seen in capitalism. There is lack of mutual cooperation and organization in capitalism.

Modern form of Capitalist Economy

Due to many defects in capitalism there have been changes in it time to time and thus a new refined form of capitalism has emerged. Imperfections in the market, preference to modern rules and integration, increasing effect of trade union, increase in public enterprises control of state etc. are the features of the modern

capitalism but there are some characteristics of pure capitalism still present in the modern capitalism. Although governments are not silent observers now a days and thus they are playing their significant required role in capitalist economy.

Socialistic Economy or Socialism :

Due to defects of capitalism a new form of economy emerged which is known as socialistic economy. The economic systems of Cuba, China, Vietnam etc. are the socialistic economies. In this economy, government controls and performs the main economic activities for the social welfare. Different economists have defined socialism in their own ways.

Meaning of Socialism:-

Socialism is that form of the economic system in which main resources of output and distribution are owned and controlled by government and these resources are used for the maximum social benefit on the basis of cooperation.

Definition of Socialism :-

According to Leftwithch, in socialistic economy the main and central role is of the government. Government owns the factors of production and directs the economic activities.

Joad writes about socialism that "Socialism is a type of cape which has got its shape deteriorated because everybody puts it on. Socialism has the temper of multi aspects. Government interference is all of the above. It is only the state which effectively controls and runs the economic system."

Characteristics of Socialism or Planned Economy :

Characteristics of a socialistic economy or a pure communalism are exactly opposite to the characteristics of the capitalism. These are:

1. Government Ownership:

In socialism all the main factors of production are owned by the government. Private

property and all factors of production are nationalized and kept under the ownership of government. Resources are used in the planned way for the maximum benefit of the society.

2. Central Planning :

There is an effective system of central planning in socialism. Economy is run by central planning for obtaining certain objectives. All the decisions regarding production and distribution are taken by the central planning. According to Pigou, "Central Planning with the ownership of government on the factors of production is the main feature of socialism."

3. Objective of Maximum Social Welfare :

The objective of government in socialism is to maximize the social welfare. Private benefit is not given any importance in this economic system. Central organization formulates policy by keeping the maximum social benefit in the centre.

4. Lack of Exploitation :

There is no scope of exploitation of people in the socialist economy because the economy is governed by government whose objective is the maximum welfare. Labourers and consumers are not exploited because there is spirit of equality in this economy.

5. Equality :

In socialism whole of the control is of the government, there is no objective of private property and private profit, there is no place of exploitation and the principle of equality works. Economic inequalities are found less because of the equal opportunity and equal right on profit.

6. Full Employment:

It is an important characteristic of socialism that there is full employment in the economy. There are efforts of the government for the best and full utilization of human resources and thus unemployment is not seen.

7. Concrete Objectives :

Socialistic economy works with objectives

and these objectives are certain. Various objectives are made and achieved by working according to plans. Rapid industrialization, increasing life standard, achieving full employment, reducing inequalities in income and wealth, etc. are the main objectives of socialism.

8. Lack of Competition :

In socialism there is lack of competition because government is the main entrepreneur and the economy is under the central control. We see government monopoly instead of cut throat competition.

9. Development of Basic Heavy Industries :

Economy under socialism is completely controlled and planned and these heavy industries and basic industries are rapidly developed.

10. Social Security :

Due to government control each person is secured from hunger, disease, accident, etc.

Advantage or Merits of Socialism:

Main merits of socialism are as under:

1. Optimum use of Economic Resources :

All the natural and human resources are used by central planning in socialistic economy which aims the maximum social welfare and social security.

2. Freedom from Trade Cycles :

Socialism is a planned economy so trade cycles occur less in comparison to free market economy. Government uses resources in a planned way keeping in view the maximum welfare and social security. So there is less possibility of ups and downs in economic activities.

3. Rapid Economic Growth:

The main decision maker in socialism is the planning authority which coordinates economic resources efficiently and thus rate of growth increases rapidly. This is also due to the

participation of all people in economic growth process.

4. Better Solution of Basic Problems :

What to produce, how much to produce and how to produce are the basic economic problems of an economic system. In socialism these problems are solved by the central planning. Here is the perfect freedom to the government to use resources efficiently and to produce goods and services according to the real needs of the society.

5. Balanced Development :

In this economic system the planning authority has the objective of economic development along with the effort of the balanced economic development. All the areas and regions of the state should have the balanced development.

6. No Exploitation and class Struggle:

The main motive of socialism is the equality. There is no separate recognition of capitalists and the poor class. Only one class does not participate in economic development. All the sections of society participate simultaneously so there is no chance of strikes, lockouts etc.

7. Economic Equality :

No inequality of income and wealth is found in socialism because decision regarding distribution of income is taken by the central authority. Rich section is taxed heavily which now income section is provided free services.

Demerits of Socialism:

Many economists like Robins, Dikins, Georjholm, Moriss Dob, etc. criticised this economic system as below:

1. Defective Allocation of Factors of Production :

Prof. Hayak writes, "in socialistic economy resources are allocated without price system by

the central authority." Through Price system resources are allocated automatically in important uses. There is no free market system in socialism and thus without price system there is no way out to allocate resources rationally. According to some modern economists like Tailor, price system is theoretically considered proper in capitalism while practically the resource allocation in socialism is proper and in the planned way.

2. End of Consumer Sovereignty:

In socialistic economic the sovereignty of consumer gets ended. Issues like what to produce, how to produce etc. are decided by the central planning which takes decisions in keeping view the needs of consumers. Goods and services actually required by consumers are not available in this economic system. The output which is decided by the central planning has to be accepted by all people.

3. Lack of Individual Motivation :

Owning private property and individual benefit are the elements which give motivation to human being for doing work. These both elements lack in socialism. There are new experiments being carried out in the socialistic economies.

4. Lack of Productive Efficiency :

In socialism there is neither rational resource allocation nor the incentive of individual benefit. As result, there is lack of productive efficiency. On the other hand in capitalism the objective of the producer is to maximize the profit and for this the producer produces at the level of minimum cost.

5. Presence of Servant Culture:

Socialism is a servant culture oriented economy which is an important demerit of it. All the decisions are taken by the central organization. Servants are appointed to implement these decisions who do not have their

own interest. Promotions are based on seniority and not on qualification and work efficiency. This results into red tapism and thus corruption takes place.

6. Concentration of Power :

Some experts have the opinion that in socialism there is more concentration of power which misutilizes the man power. The man power is used in the work of planning formulation, counting and implementation. Actually, this is not a demerit but it is the planning of the main power to make socialism more sensitive and effective.

Conclusion :

Although the supporters of capitalism criticize the socialism but this is beyond reality. There are less defects of socialism than capitalism. Unemployment and inflation are the long term problems in capitalism while these problems are kept under control in socialism. There is no price stability in capitalism while it is there in socialism. According to Prof. Shumpeter, "Socialism is better economic system than capitalism because in socialism output efficiency is managed by government and resources are used with more rationality. Trade cycles are absent and monopoly tendencies are ended. Economic inequalities are less and there is end of unemployment and exploitation."

Presently, some changes can be observed in socialistic economies. Training, concentration of power, innovations for development and limited personal freedom are being more emphasized.

Mixed Economy:

Demand for interference in capitalism raised because of its defects like cut throat competition, unemployment, inflation, economic instability, class struggle, etc. On the other hand, socialistic economics had been criticized on the grounds of hard control, concentration of power, servant orientation, lack of personal freedom, excess state interference, etc. As a result, such an

economic system was developed in which there are presence of characteristics of both capitalism and socialism. This type is known as the mixed economy.

Meaning of Mixed Economy :

Generally mixed economy is the economic system in which there is sufficient co-existence of private and public sectors. In mixed economy the work areas of both sectors are controlled and determined in such a way to get rapid economic growth and maximum social welfare.

According to Prof. Samuelson, "mixed economy is that economy in which there is control of both public and private institutions in economic life."

Features of Mixed Economy :

Mixed economy has the following characteristics

1. Co-existence of Private and Public Sectors:

It is an important characteristic of the mixed economy that there is co-existence of both private and public sectors. Both sectors work together. Industries of national interest like basic industries, industries of war goods, electricity etc. are found in public sector and consumer goods industries, small industries, agricultural industries and such other are run under private sectors. The objective behind this co-existence is to cooperate each other. Both industries are complementary to each other.

2. Private Property and Economic Equality :

In mixed economy on one hand, People can own and accumulate private property and on the other, government formulates strict policy regarding equal distribution of income and wealth. Government imposes tax on income, property etc. and thus controls the private property and on the other side, government launches welfare schemes for poor people like old age pension, etc.

3. Price System and Government Control –

In mixed economy both price system and central planning system work. The price system controls the economy through its effects on demand and supply forces. Main economic decisions like what to produce, how to produce for whom to produce are taken with the help of the price system. Planning system plays important role in achieving the objectives like economic growth, full employment, price control and inequality of income.

4. Personal Profit Motive and Social Welfare :

Mixed economy works with both the objectives of personal profit and maximum social welfare. Production is done with the incentive of self interest and benefit and like socialism the main objective of planning system is to maximize the social welfare.

If private industries do not work in social interest, government nationalizes them and thus transferred into the public sector.

5. Controlled Economy :

Progressive taxation, expenditure on social security functions, control on the monopoly tendencies and other such policies are adopted to keep the equal distribution of income. The maximum limit of land is also fixed.

6. Economic Planning :

The socio-economic objectives are achieved through the economic planning in the mixed economy. No economy can be said mixed economy if there is no economic planning even if there is control and interference of the state. Important economic decisions are taken with the help of economic planning.

Merits of Mixed Economy :

The mixed economy has the merits both of socialism and capitalism. These are:

1. Sufficient Freedom :

People have the sufficient freedom in

economic sphere. People can use income at their will and they can choose business according to their ability and interest. Private profit can be earned and personal property can be owned but upto a certain limit only.

2. Efficient Use of Resources :

In mixed economy both private and public sector co-exist and thus try to make the efficient use of resources. Private sector tries to use the resources efficiently according to the objective of the private benefit. The public sector uses resources efficiently but for maximizing the social welfare. In this way the mixed economy establishes the coordination between private and public sectors.

3. Decrease in Economic Disparity :

Economic inequality is a curse for the economy. Government imposes progressive taxation to reduce the economic inequalities in the mixed economy. Monopoly practices are controlled for this purpose. The increasing prosperity of private sector is controlled and efforts are made for social security and economic equality.

4. Lack of Exploitation :

Mixed economy tries to keep society safe from the monopolistic tendencies and exploitation of zamindars. There are welfare schemes for private labourers and farmers. Necessary laws are enacted and cooperation is developed.

5. Planned and Rapid Economic Growth:

Price system works in mixed economy but it is not given full freedom. The role of private sector in economic growth is decided through proper planning and for this purpose available resources are sufficiently surveyed and used for the economic growth. Public sector plays its significant role in the balanced economic growth of the country and capital formation gets momentum.

Defects or Disadvantages of Mixed Economy :

In mixed economy there are demerits of both capitalism and socialism. This economy incorporates the objectives of maximum social welfare, economic growth, reduction in unemployment, reduction in income inequalities, social security, etc. But due to the capitalism the exploitative tendencies are developed and become intensive. If the socialistic elements are strengthened then the problems of red tapism and inefficiency are developed. This mixed economy can not be free from any defects. Following are such some demerits of this economic systems.

1. Difficulty in Efficient Implementation :

Mixed economy is a joint form of capitalism and socialism which are opposite to each other. Due to this fact there is problem in its efficient implementation. In mixed economy neither economic planning becomes successful nor the price system works efficiently.

As Shumpeter says, mixed economy is capitalism in oxygen tent.

2. Unstable Economy :

There is instability in the mixed economy. Either private sector harms the public sector and thus public sector loses its importance with changing itself into capitalism. Or public sector becomes so powerful and thus it ends the private sector and thus the economy becomes socialistic.

3. Inefficient Planning:

In mixed economy a large part of economy remains out of the government control and thus this part works only for under the selfishness which creates big problems in the success of plans. Under this situation public sector fails in achieving its objectives.

4. Corruption:

There is wide spread corruption in the mixed economy. Public sector is misused by political parties for their defective motives and thus create

obstacles in the success of plans.

5. Black Money :

In mixed economy black money is created. Political parties misuse the public sector due to selfishness and private sector tries to disobey the rules and thus corruption is created which leads the black money in the economy. This black money becomes an obstacle in the process of economic growth.

6. Challenge to Democracy :

Economic planning and government policies challenge the economic democracy slowly. There is fear of dictatorship in the economy. In reality, it is only a fear. In democracy it is respected that the real power is in the hand of the public.

Even there are many demerits of mixed economy, it always supports the path of economic growth and social welfare. Although there is fear of inefficiency and dictatorship in mixed economy but co-existence of private and public sectors makes the economy healthy which leads the economic progress. Trade cycles, unemployment, exploitation and class struggle are controlled by the government.

Indian Economy as a Mixed Economy :

The emergence of mixed economy in India can be considered from the industrial policy of 1948 and after first five year plan in industrial policies of 1956, 1977 and 1991 in which industries were categorized.

Separate objectives were fixed both for private and public sectors in first five year plan also. In 1954 we took the objective of the establishment of socialistic society and accepted the important role of public sector in planned economic development which followed the rapid industrialization. In India, as result of the planned development policies we got progress in the areas of rapid economic growth, poverty and unemployment removal, control over concentration of economic power, balanced

industrial development, agriculture development, social welfare, etc. Prof. K.N. Raj writes- Although Indian Economy is the mixed economy but the elements of mix have kept it capitalism made nor equal as the socialism.

Classification of Economy on the Basis of Development:

On the basis of development economy can be divided into two parts as – (i) Developed economy, and (ii) Developing economy.

Developed Economy:

It is that economic system in which there is rapid economic growth and levels of per capital income and national income are very high. U.S.A., Canada, France, Germany, Japan, etc. are the examples of developed economy. Following are the characteristics of developed economies.

1. High National and Per Capita Incomes:

The rates of growth of national income and per capita income are high in developed economies where the living standard of people is very high. According to the world Bank Report 2012, in 2010 the per capita gross national product in capitalist countries was on an average of \$38745. The per capita gross national product was \$47340 in U.S.A.

2. High Rate of Capital Formation :-

Economists always accept the importance of capital formation for increasing the levels of output. When a large part of national income is saved and then reinvested, it is known as capital formation. In developed countries the rate of capital formation is very high and thus there are no vicious circles of poverty.

3. Dominance of Industries and Non-agricultural Occupations:

In developed economies a large part of population is engaged in non-agricultural occupations like industries, transport, communication, banking insurance, etc. The

contribution of service sector in national income is higher.

4. High Technology :

Developed economies are technically efficient economies. A large portion of national income in these economies is used on innovation and technique. The production techniques are always changed for increasing levels of production.

5. Other Characteristics:

In developed economies human resources are managed and used in efficient manner also, the sensitiveness of increasing the process of economic growth is found comparatively more.

Developing or Under Developed Economy :

According to Samuelson, "An under developed or developing economy is that one in which per capita real income is less than that in Canada, U.S.A., Great Britain or generally western european countries. Optimistically it is understood that in developing countries there is capacity to improve the levels of income sufficiently." Indian planning commission has defined the under development in first five year plan as, "that country is said to be underdeveloped in which, on the one hand, there is low level of utilization of man power and on the other hand, natural resources are not fully utilized." In this way, all those economies of the world are developing economies where the level of per capita income is lower than that of U.S.A., Australia and the countries of the west Europe. India, Bangladesh, Pakistan, etc. are the examples of developing economies.

Characteristics of Developing Economies :

General characteristics of developing economies are as given below:

1. Low Level of National Income and Per Capita Income :

In developing economies levels of national

income and per capita income are lower in comparison to developed economies. According to World Bank Report 2010, it was \$528 in low income developing countries and \$3725 in medium income developing countries. It was \$1270 in India in 2010. Due to low per capita income level the standard of living is very low and civil amenities are less.

2. Low Living Standard :

The low levels of per capita income in developing countries result in low living standards and thus there are low levels of work efficiency. Levels of consumption of food, cloth, housing, etc. are low.

3. Dependence on Agriculture :

In these countries 30 to 70 percent, population depends on agriculture. Even after being dependent on agriculture the agricultural growth is lower and thus it is also a characteristic of developing economies. Due to slow growth of agriculture the contribution of agriculture in national income is reduced.

4. Backward Industrialization :

Industrial structure in underdeveloped economies is generally backward and imbalanced. The basic and heavy industries like iron and steel, heavy engineering, machine tools, heavy chemicals, transport, etc. are less developed. Due to this there are lower employment opportunities and the reduced contribution in the national income.

5. Lower Labour Productivity:

Productivity of labour is lower in these economies. It is both cause and effect of the low living standard. This lower productivity causes lower income levels which gives birth to poverty. Health of labourers, work efficiency, incentive to work, infrastructure facilities are the factors which affect the lower productivity of labour.

6. Wide Poverty :

There are vicious circles of poverty in

developing economies. Low level of per capita income and income inequality are the causes of widespread poverty. Malnutrition, less food, diseases and lack of health facility are the some other causes of this problem.

7. Backward Technology:

Due to low level of research and development in developing economies there is backwardness of technology. There are obstacles in new technology due to lack of resources, lack of capital and excess of labour. Due to these causes there are negative effects on productivity and quality of production.

8. Unemployment and Disguised Unemployment :

Unemployment is seen at the high level in these economies. Involuntary unemployment is mostly found both in rural and urban sectors. Agriculture sector has the disguised unemployment. In agriculture there is low level of employment due to the traditional nature of it. Due to increasing population in developing countries, disguised unemployment continuously increases.

9. Other Characteristics:

Low levels of human welfare, health facilities, educational achievement and probable real income are seen in these economies. Inequalities in the distribution of income and wealth are present there. In developing economies the issues like tax system, social security system, education and training and employment are not considered seriously as done in developed economies.

Classification of Economies according to World Bank:

World Bank divided the economies of the world in 2003 on the basis of per capita national income in four parts as below.

1. **Lower Income Countries :-** These are the countries where per capita income is \$675 or less.
2. **Medium Lower Income Countries:-** In these countries per capita national income is between \$676 and \$3035.
3. **Medium Higher Income Countries:-** Here the per capita national income is between \$3036 and \$9385.
4. **Higher Income Countries:-** These Countries have their per capita national income more than \$9386.

Important Points :

- Economies system or economy is that structure of institutions where there is social control on the consumption of goods and services produced by factors of production and the factors of production.
- On the basis of the ownership of factors of production economies are of three types- Capitalism, Socialism and Mixed economy.
- On the basis of development economies are of two types – (i) Developed Economies (ii) Developing Economies.
- World Bank divided economies into 4 parts on the basis of per capita national income. These are:
lower income countries, medium lower income countries, medium higher income countries and higher income countries.

Questions for Exercise

Objective Type Questions:

1. Capitalism is the economy in which-
 - (a) Public ownership on property
 - (b) Equality in income distribution
 - (c) Price property
 - (d) Effective planning system ()
2. The important objective of capitalism is –
 - (a) Welfare of labourer
 - (b) Economic equality
 - (c) Maximization of private profit
 - (d) Establishment of socialism ()
3. The oldest system of economy is –
 - (a) Socialism (b) Mixed
 - (c) Communalism (d) Capitalism ()
4. Socialistic Economy is –
 - (a) Planned economy
 - (b) Unplanned economy
 - (c) Price system based economy
 - (d) Economy of Private ownership of factor of production. ()
5. The possible danger of capitalism is-
 - (a) Class struggle
 - (b) Increase in trade cycles
 - (c) Economics exploitation
 - (d) All of the above ()
6. Main objective of socialism is-
 - (a) Personal benefit
 - (b) Increase in employment
 - (c) Increase in national income
 - (d) None of above ()
7. Which one is not a characteristic of socialism–
 - (a) Central planning
 - (b) Role of price system
 - (c) Maximum social welfare
 - (d) Public ownership of factors of production ()
8. In mixed economy factors of production are controlled by –

- (a) Government
- (b) Private people
- (c) Both Government and private
- (d) None of above ()

9. Central problems in mixed economy are solved by –

- (a) Price system
- (b) Central planning
- (c) Both price system and central planning
- (d) None of above ()

10. On the basis of per capita national income World Bank divides economies into number of parts –

- (a) Two (b) Three
- (b) Four (c) Five ()

Very Short Answer Questions:-

1. What is economy or economic system ?
2. Write name of any three countries having capitalism.
3. Write name of any two countries having socialism.
4. What is a developed economy ?
5. What is a developing economy ?

Short Answer Questions :

1. What are the important elements of economy?
2. Write important characteristics of an underdeveloped economy.
3. What are the different forms of economic systems ?
4. What is mixed economy ?
5. What is capitalism ?
6. State the difference between developing and developed economies.

Essay Type Questions :

1. Describe the characteristics of the mixed economy. Show that upto what extent the mixed economy is a mixture of merits of both capitalism and socialism.
2. What type of economy is known as socialism?
3. Describe the characteristics of capitalistic economy. What are the important merits and demerits of capitalism ?
4. Describe merits and demerits of mixed economy. Why is Indian economy known as a mixed economy ?
5. Describe merits and demerits of socialism.

Answer to Objective Questions :

- (1) c (2) c (3) d (4) d (5) d (6) b
(7) b (8) c (9) c (10) c

Reference Books:

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