This study material has been prepared by the faculty of the Board of Studies. The objective of the study material is to provide teaching material to the students to enable them to obtain knowledge and skills in the subject. In case students need any clarifications or have any suggestions to make for further improvement of the material contained herein they may write to the Director of Studies.

All care has been taken to provide interpretations and discussions in a manner useful for the students. However, the study material has not been specifically discussed by the Council of the Institute or any of its Committees and the views expressed herein may not be taken to necessarily represent the views of the Council or any of its Committees.

Permission of the Institute is essential for reproduction of any portion of this material.

Students may note that the following changes have been incorporated in the study material of General Economics:
- Presentation has been improved.
- More Multiple Choice Questions have been added at the end of each chapter.
- Data in the Indian Macro Economics portion has been updated.
- At the end of the each unit, summary is presented in bullet points for the benefit of the students.

© The Institute of Chartered Accountants of India

All rights reserved. No part of this book may be reproduced, stored in a retrieval system, or transmitted, in any form, or by any means, electronic, mechanical, photocopying, recording, or otherwise, without prior permission, in writing, from the publisher.

Price: ₹ 200.00

Revised Edition: November, 2014
Reprint: November, 2015

Website: www.icai.org E-mail: bosnoida@icai.in

ISBN: 978-81-8441-035-8

Published by The Publication Department on behalf of The Institute of Chartered Accountants of India, ICAI Bhawan, Post Box No. 7100, Indraprastha Marg, New Delhi - 110 002, India

Designed & Printed at Repro India Limited, 50/2, TTC MIDC Industrial Area, Mahape, Navi Mumbai - 400 710, India.
November / 2015 / P1854 (Reprint)

© The Institute of Chartered Accountants of India
The activity of seeking wealth is as old as civilisation. Human beings either as individuals or as groups or as large kingdoms and empires have always been engaged in acquiring and increasing the material wealth. In fact, all human decisions and activities can be ultimately linked with acquisition of material welfare. However, a disciplined study of the wealth producing activities was commenced about 235 years back when Adam Smith, the father of Economics, published “The Nature and Causes of Wealth of Nations”. Economics, as a discipline, has come a long way since then and it constitutes the most important subject to analyse activities related to wealth creation and distribution. The dimensions of the subject of Economics are truly vast and encompass all aspects of our lives. Undoubtedly, Economics has come to be known as the mother of all social sciences. A study of Economics gives a perspective and a macro attitude while analysing financial activities. It provides an insight into various economic problems faced by a country and also provides solutions to solve these problems. Since it deals with problems and questions that affect almost all kinds of individuals in their capacities as consumers and producers, an adequate knowledge of the science of Economics is a prerequisite for understanding the economy and its various components. Economics, therefore, has always been a part of the curricula of Chartered Accountancy course in India.

In the new course it is being taught and tested at the CPT level. The syllabus is systematically planned to give students an exposure to Micro economics as well as Indian economy. In Micro economics, there are four chapters namely Introduction to Micro Economics, Theory of Demand and Supply, Theory of Production and Cost and Price determination in different markets. Similarly, in Indian Economy there are four chapters, namely, Indian economy – a Profile, Select aspects of Indian economy, Economic Reforms in India and Money and Banking. Care has been taken to explain the concepts in a lucid and easy language with the help of diagrams and illustrations. In chapters relating to Indian economy, efforts have been made to provide the latest data. At the end of each chapter, lots of multiple choice questions have been given to help students test their understanding of the subject and their skills in applying economic theory to real world situations. It is hoped that these inputs will further enhance the utility of the book. I appreciate the earnest and sincere efforts taken by Ms. Prem Bhutani, Deputy Director, BOS, in bringing out this publication, incorporating many student-friendly features, well in time. Suggestions for further improvements are heartily welcome.
Objective:
To ensure basic understanding of economic systems, economic behaviour of individuals and organisations.

Contents

(I) Micro Economics

1. Introduction to Micro Economics
   (a) Definition, scope and nature of Economics
   (b) Methods of economic study
   (c) Central problems of an economy and Production possibilities curve.

2. Theory of Demand and Supply
   (a) Meaning and determinants of demand, Law of demand and Elasticity of demand – Price, income and cross elasticity
   (b) Theory of consumer’s behaviour – Marshallian approach and Indifference curve approach
   (c) Meaning and determinants of supply, Law of supply and Elasticity of supply.

3. Theory of Production and Cost
   (a) Meaning and Factors of production
   (b) Laws of Production – The Law of variable proportions and Laws of returns to scale
   (c) Concepts of Costs – Short run and longrun costs, Average and marginal costs, Total, fixed and variable costs.

4. Price Determination in Different Markets
   (a) Various forms of markets – Perfect Competition, Monopoly, Monopolistic Competition and Oligopoly
   (b) Price determination in these markets.

(II) Indian Economic Development

5. Indian Economy – A Profile
   (a) Nature of the Indian Economy
   (b) Role of different sectors – Agriculture, Industry and Services in the development of the Indian economy, their problems and growth
   (c) National Income of India – Concepts of national income, Different methods of measuring national income, Growth of national income and per capita income in various plans
   (d) Basic understanding of tax system of India – Direct and Indirect Taxation.

6. Select Aspects of Indian Economy
   (a) Population – Its size, rate of growth and its implication for growth
   (b) Poverty – Absolute and relative poverty and main programs for poverty alleviation
   (c) Unemployment – Types, causes and incidence of unemployment
   (d) Infrastructure – Energy, Transportation, Communication, Health and Education
   (e) Inflation
   (f) Budget and Fiscal deficits
   (g) Balance of payments
   (h) External debts.

7. Economic Reforms in India
   (a) Features of economic reforms since 1991
   (b) Liberalisation, Privatisation and Disinvestment
   (c) Globalisation.

8. Money and Banking
   (a) Money – Meaning and functions
   (b) Commercial Banks – Role and functions
   (c) Reserve Bank of India – Role and functions, Monetary policy.
## CONTENTS

### SECTION - I: MICRO ECONOMICS

#### Chapter 1 - Introduction to Micro Economics

1.0 What is Economics About? 2  
1.1 Definitions and Scope of Economics 3  
1.2 Nature of Economics 8  
1.3 Methods of Study 10  
1.4 Central Economic Problems 11  
1.5 Production Possibilities Curve 12  
1.6 How Different Economies Solve their Central Economic Problems? 16  
Summary

#### Chapter 2 - Theory of Demand and Supply

**Unit 1: Law of Demand and Elasticity of Demand**

1.0 Meaning of Demand 38  
1.1 What determines Demand? 38  
1.2 Law of Demand 40  
1.3 Expansion and Contraction of Demand 45  
1.4 Increase and Decrease in Demand 45  
1.5 Movements along Demand curve vs. Shift of Demand curve 47  
1.6 Elasticity of Demand 48  
1.7 Demand Distinctions 59  
Summary

**Unit 2: Theory of Consumer Behaviour**

2.0 Nature of Human Wants 62  
2.1 Marginal Utility Analysis 63  
2.2 Indifference Curve Analysis 68  
Summary

**Unit 3: Supply**

3.0 Introduction 77  
3.1 Determinants of Supply 77  
3.2 Law of Supply 78  
3.3 Shifts in the Supply Curve – Increase or Decrease in Supply 79  
3.4 Movements on the Supply Curve – Increase or Decrease in the quantity supplied 80  
3.5 Elasticity of Supply 80  
Summary

© The Institute of Chartered Accountants of India
# Chapter 3 - Theory of Production and Cost

## Unit 1: Theory of Production

1.0 Meaning of Production 106  
1.1 Factors of Production 107  
1.2 Production Function 112  
1.3 Production Optimisation 119  
1.4 Economies and Diseconomies of Scale 122  
Summary

## Unit 2: Theory of Cost

2.0 Cost Analysis 128  
2.1 Cost Concepts 128  
2.2 Cost Function 130  
2.3 Short run Total Costs 130  
2.4 Long run Average Cost Curve 136  
Summary

# Chapter 4 - Price Determination in Different Markets

## Unit 1: Meaning and Types of Markets

1.0 Meaning of Market 156  
1.1 Types of Market Structures 158  
1.2 Concepts of Total Revenue, Average Revenue and Marginal Revenue 159  
1.3 Behavioural Principles 160  
Summary

## Unit 2: Determination of Prices

2.0 Introduction 163  
2.1 Determination of Prices – A General View 163  
2.2 Changes in Demand and Supply 164  
2.3 Simultaneous Changes in Demand and Supply 167  
Summary

## Unit 3: Price-output Determination under Different Market Forms

3.0 Perfect Competition 170  
3.1 Monopoly 179  
3.2 Imperfect Competition-Monopolistic Competition 188  
3.3 Oligopoly 192  
Summary
## CONTENTS

### SECTION - II : INDIAN ECONOMIC DEVELOPMENT

#### Chapter 5 - Indian Economy - A Profile

<table>
<thead>
<tr>
<th>Unit 1: Nature of Indian Economy</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.0 India - An Underdeveloped Economy</td>
</tr>
<tr>
<td>1.1 India - A Developing Economy</td>
</tr>
<tr>
<td>1.2 India - A Mixed Economy</td>
</tr>
<tr>
<td>Summary</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Unit 2: Role of Different Sectors in India</th>
</tr>
</thead>
<tbody>
<tr>
<td>2.0 Agriculture</td>
</tr>
<tr>
<td>2.1 Industry</td>
</tr>
<tr>
<td>2.2 Services</td>
</tr>
<tr>
<td>Summary</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Unit 3: National Income in India</th>
</tr>
</thead>
<tbody>
<tr>
<td>3.0 Basic Concepts in National Income and Output</td>
</tr>
<tr>
<td>3.1 Methods of Measuring National Income</td>
</tr>
<tr>
<td>3.2 Trends in India’s National Income Growth and Structure</td>
</tr>
<tr>
<td>Summary</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Unit 4: Basic Understanding of Tax System in India</th>
</tr>
</thead>
<tbody>
<tr>
<td>4.0 Meaning of Direct and Indirect Taxes</td>
</tr>
<tr>
<td>4.1 Merits and Demerits of Direct and Indirect Taxes</td>
</tr>
<tr>
<td>4.2 Tax Structure in India</td>
</tr>
<tr>
<td>Summary</td>
</tr>
</tbody>
</table>

#### Chapter 6 - Select Aspects of Indian Economy

<table>
<thead>
<tr>
<th>Unit 1: Population</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.0 Meaning of Population</td>
</tr>
<tr>
<td>1.1 Demographic Trends in India</td>
</tr>
<tr>
<td>1.2 Causes of the Rapid Growth of Population</td>
</tr>
<tr>
<td>1.3 Growth of Population in India and its effects on Economic Development</td>
</tr>
<tr>
<td>1.4 Government Measures for solving the Population Problem</td>
</tr>
<tr>
<td>Summary</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Unit 2: Poverty</th>
</tr>
</thead>
<tbody>
<tr>
<td>2.0 Absolute Poverty and Relative Poverty</td>
</tr>
<tr>
<td>2.1 Poverty in India</td>
</tr>
<tr>
<td>2.2 Causes of Poverty</td>
</tr>
<tr>
<td>2.3 Government Programmes for Poverty Alleviation</td>
</tr>
<tr>
<td>Summary</td>
</tr>
</tbody>
</table>
CONTENTS

Unit 3 : Unemployment

3.0 Meaning and Types of Unemployment 295
3.1 Nature of the Unemployment in India 296
3.2 Causes of Unemployment in India 297
3.3 Extent of Unemployment in India 297
Summary

Unit 4 : Infrastructural Challenges

4.0 Energy 304
4.1 Transportation 308
4.2 Communication 312
4.3 Health 314
4.4 Education 315
Summary

Unit 5 : Inflation

5.0 Meaning and Types of Inflation 321
5.1 Price Trends in India 322
5.2 Causes of Inflation in India 323
5.3 Measures to Check Inflation 325
Summary

Unit 6 : Budget and Fiscal Deficits in India

6.0 Meaning of Budget and Fiscal Deficits 328
6.1 Trends in India’s Budget and Fiscal Deficits 329
Summary

Unit 7 : Balance of Payments

7.0 Meaning of Balance of Payments and Balance of Trade 333
7.1 Trends in Balance of Payments of India 333
Summary

Unit 8 : External Debt

8.0 External Debts in India 339
Summary
## CONTENTS

### Chapter 7 - Economic Reforms in India

#### Unit 1: Economic Reforms in India

1.0 Background .......................................................... 354  
1.1 Industrial Sector ................................................ 355  
1.2 Financial Sector ................................................ 356  
1.3 External Sector .................................................. 358  
1.4 Tax Reforms ....................................................... 362  
1.5 Impact of Economic Reforms on the Indian Economy 363  
Summary

#### Unit 2: Liberalisation, Privatisation and Disinvestment

2.0 Meaning of Liberalisation, Privatisation and Disinvestment 367  
2.1 Privatisation and Disinvestment in India .................. 368  
2.2 Progress of Disinvestment ..................................... 369  
Summary

#### Unit 3: Globalisation

3.0 Meaning of Globalisation ....................................... 372  
3.1 Cases for Globalisation ........................................ 372  
3.2 Cases against Globalisation ................................... 373  
3.3 Measures towards Globalisation ............................. 373  
3.4 Effect of Globalisation on Indian Economy ............... 375  
3.5 Main Organisations for Facilitating Globalisation ...... 376  
Summary

### Chapter 8 - Money and Banking

#### Unit 1: Money

1.0 Meaning of Money .............................................. 390  
1.1 Functions of Money ............................................ 390  
1.2 Money Stock in India ......................................... 392  
Summary
## CONTENTS

### Unit 2: Commercial Banks

<table>
<thead>
<tr>
<th>Section</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>2.0 Introduction</td>
<td>394</td>
</tr>
<tr>
<td>2.1 Role of Commercial Banks</td>
<td>394</td>
</tr>
<tr>
<td>2.2 Functions of a Bank</td>
<td>395</td>
</tr>
<tr>
<td>2.3 Commercial Banking in India</td>
<td>396</td>
</tr>
<tr>
<td>2.4 Nationalisation of Commercial Banks</td>
<td>397</td>
</tr>
<tr>
<td>2.5 Progress of Commercial Banks after Nationalisation</td>
<td>398</td>
</tr>
<tr>
<td>2.6 Shortcomings of Commercial Banking in India</td>
<td>398</td>
</tr>
<tr>
<td>Summary</td>
<td></td>
</tr>
</tbody>
</table>

### Unit 3: The Reserve Bank of India (RBI)

<table>
<thead>
<tr>
<th>Section</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>3.0 Meaning and Functions of a Central Bank</td>
<td>402</td>
</tr>
<tr>
<td>3.1 Central Bank Vs Commercial Bank</td>
<td>402</td>
</tr>
<tr>
<td>3.2 Role of the Reserve Bank of India</td>
<td>403</td>
</tr>
<tr>
<td>3.3 Functions of Reserve Bank of India</td>
<td>403</td>
</tr>
<tr>
<td>3.4 Indian Monetary Policy</td>
<td>405</td>
</tr>
<tr>
<td>Summary</td>
<td></td>
</tr>
</tbody>
</table>