Gross Domestic Product

Shomesh Kumar (RIA)
SEBI Registration No.
INA200015088

Friday, 16 October 2020

Private & Confidential
Only for Shomesh Kumar's Clients
For Private Circulation Only

Website – www.shomeshkumar.in
Twitter – https://twitter.com/shomeshk?s=08
LinkedIn – https://www.linkedin.com/in/shomesh-kumar-b172801a

Disclaimer: Shomesh Kumar is a SEBI Registered Investment Adviser. The write-up is educational in nature as the output of research and reading of financial markets. It is no endorsement to trade or invest based on the content of the write-up. Please take the necessary advice from your investment adviser before acting on any type of trading or investment. Stock market investments are not risk-free. Shomesh Kumar intends to earn no income out of these write ups. This is to spread awareness and educate general public.

GROSS DOMESTIC PRODUCT (GDP)

Gross Domestic Product – In its simplest form of definition, GDP is the total value of everything produced within the boundaries of a country. The value of GDP is also known as the **size of the economy**. The value that is used to calculate GDP is the final value of the products & services and not the intermediate value of goods & services i.e. the value of the components leading to the final products & services are excluded. For example, the final price of a bike will be considered as a part of calculation of GDP. The value of its components such as wheels, tank, seat, engine etc. will not be considered while accounting for the value of the bike. This is followed to avoid "double counting". The value of wheels, tank, seat & engine would have already been accounted in GDP when it would have been sold to the manufacturer of the bike to be used as different parts in the bike.

GDP can be of two types viz. Nominal GDP & Real GDP. Nominal GDP includes Inflation, while Real GDP excludes inflation. The country's reported GDP numbers are Real GDP numbers i.e. after excluding the impact of inflation.

There are 3 methods to compute the GDP. The formula under each method is enumerated as below

Output Method – This method measures the market value of all the goods and services produced inside the country. This method calculates GDP as Real GDP - Taxes + Subsidies.

Expenditure Method – This method measures the total expenditure incurred by all entities on goods and services inside the country. Under this method GDP is calculated as **C + I + G + X – M**

C – CONSUMPTION, I – INVESTMENT, G – GOVERNMENT EXPENDITURE, X – EXPORTS, I – IMPORTS

Income Method – It measures the total income earned by the factors of production, i.e. labour and capital inside the country. GDP as per income method is calculated as GDP at factor cost + Taxes – Subsidies.

GDP Growth Rate – It is the percentage increase in GDP, either quarter on quarter or year on year. If the GDP of a country increases from USD 1 trillion to USD 1.1. trillion then the GDP growth rate is 10%. If the growth rate is positive then it is called **Economic Expansion**. If the growth rate is negative then it is called **Economic Contraction**. If an economy contracts for few quarters then it signals **Economic Recession** and if it contracts for few years then it is called **Economic Depression**.

GROSS DOMESTIC PRODUCT (GDP)

There are some conventions followed while measuring the GDP of a country which are enumerated as below.

- The most popular method to compute GDP is Expenditure method.
- GDP computation considers the value of Goods & Services at their market price and not at cost price.
- The value of intermediate goods & services are not considered. Only the value of final goods & services are considered. This is to avoid double counting as the value value of final product already accounts for the value of intermediate goods.
- GDP considers the output produced in the country i.e. if a foreign company is producing goods & services in India then it will be included in the GDP of India and not the GDP of the country to which the company belongs to; however, it will be included in the Gross National Product (GNP) of the country to which the company belongs to.
- GDP growth is represented in Real terms, excluding the impact of inflation.
- GDP is measured on time scale, usually year on year.

The overall GDP is represented in terms of contribution of 3 major sectors viz. Agriculture, Industry & Services. These are also known as Primary, Secondary & Tertiary sectors. Agriculture contributes for about 17% of GDP, Industry 29% and Services about 55%. These contributions of sectors vary over time based on their individual performance.

The top 5 countries and their approximate GDP values are enumerated below as per the latest available data.

United States – USD 20 trillion, **China –** USD 13 trillion, **Japan –** USD – 5 trillion, **Germany –** USD 3.70 trillion, **India –** USD 2.70 trillion.

Per Capita GDP – Sometimes, the GDP of a country could be high due to its population and hence it makes sense to calculate Per Capita GDP to measure the standard of living of the country. Per Capita GDP is arrived at by diving the GDP of a country by the population/residents of the country.

Gross National Product (GNP) – GNP is calculated as GDP plus Net Factor Income from abroad. If an Indian company has foreign operations then the value of goods & services produced in the foreign country are added to the GDP of the origin country to arrive at the GNP of the origin country. Though GDP and GNP both calculate the value of goods & services produced by a country; GDP is the most popular measure used by a country to measure the overall health and size of the economy.