The Investment function

Investment is the determinents of leve of National income and employment. Invest-ment means "Real investment"

if a person constructs the new building (house) by their saved money then it is said to be real investment or investment.

but a person buy the old house by their saved money then it is not investment, it is only property transfer one to anther person.

Thus, when savings is used in buying new Machine, equipments etc then it is called Invest-ment.

Yet, Investment refers to buy new machine, new house, other ~~Capitalistig~~ Capitlistic goods which increase the stocks of available capital.

□ The Relation between Capital and Investment

Capital and investment are related each other by the Net investment. The total expenditure for the new capital properties in one year is called Gross investment.

But, Every year Capital has Depreciation and Relplacement. So the Net Investment is

Net Investment = Gross Investment $\overset{\text{Minus}}{-}$ Depreciation & Replacement.

if Gross investment = Depreciation
then Net investment = 0 (zero)
in the above case, there is no increase the Capital Stock.

if Gross Investment < depreciation
then Disinvestment will be occure in an economy and capital stack is decreased.

Yet, Gross investment must be greater than Depreciation to increase the Capital stock in an economy. It means It should be Net Investment.

☐ Types of Investment —

1) Induced investment
2) Autonomous Investment.

1) Induced Investment ⇒ The Investment to the purpose of more and more profit then It is called induced investment.

(i.e.- prices, wage, change in interest)
The factors effects the profit ~~is~~ is also effect the induced investment.

When, income is increased then demand of the consumer goods are increased and the over come to this ~~problem~~ demand, investment is increased.

Thus It may be said to be investment is effected by income or, Investment is the functional relation of income. like -

$$I = f(Y)$$

where,
I = Investment
f = functional Relation
Y = Income.

2) Autonomous Investment ⇒

Autonomous investment is not effected by level of income. It is also not ~~not~~ effected by change in demand but It effects the demand.

The investment by the Government fe the social overheads is autonomous.

The exogenous factor of the autonomous investment i.e innovation, invention, ~~and~~ population, and increase in labor power, Research, social and legal intitution, war, etc effect the autonomous investment.

Any types of private investment in long run is autonomous due to it is effected by exogenous factor.

☐ Determinants of investment.

There are two determinants of investment —

1) Marginal effeciency of capital (MEC)
2) Rate of interest

1) MEC (Marginal efficiency of capital) ⇒ The MEC is the highest rate of return expected from an additional unit of a capital Assets over its cost.

If in the future the expectation of the return is increased then Capital investment is profitable.

MEC is determined by two factors given below
a) prospective income from the Capital Assets.
b) Supply price of Capital Assets.

a) prospective income from the capital Assets ← It refers to

= prospective income from the use of Capital Assets — minus Variable cost of Capital Assets.

prospective income from the use of Capital Assets may be determined by Quantity increased in total production due to used of that Capital Assets. It is also called marginal revenue productivity of Capital.

Variable Costs refers to expenditure on raw materials, wage, Transport, advertising etc.

b) Supply price of Capital Assets ⟹ It refers to Cost of Capital Assets. in other words, during the investment, the expenditure on Capital goods is called Supply value or Supply price.

therefore — To expend by the new Machine

2. Rate of Interest

The cost of the essential funds for the finance of a project is called rate of interest.

If the MEC is greater than Rate of Interest then investor is induced to the investment and vice-versa.

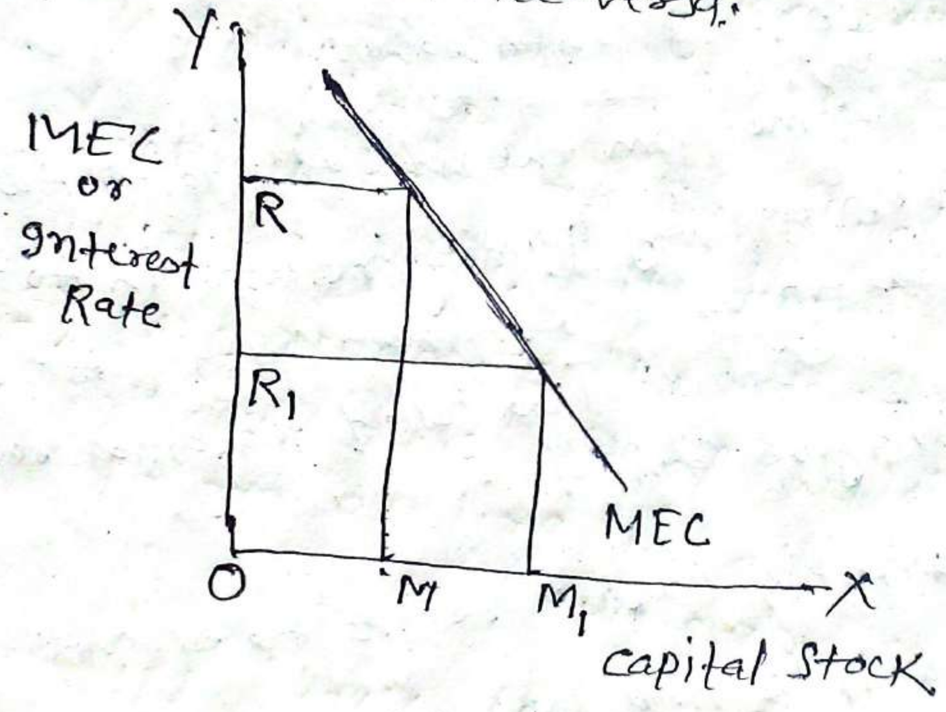

Fig:- Interest Rate and Investment

In the above figure, if the rate of interest is increased then ~~cut~~ investment of capital is decreased and vice-versa.

~~The Negative downward slop~~
Left to right, downward Negative Slop of MEC curve indicates the Negative Relation b/w

Rate of Interest and Investment.

When Interest Rate OR, then Investment OM and when Interest Rater is decreased OR to OR_1 then Investment increased OM to OM_1.

☐ The Marginal efficiency of Investment - MEI

The MEI is the rate of return expected from a given Investment on a Capital Assets after covering all ~~the~~ its cost, except the rate of interest.

if the rate of Interest is height then the level of Investment is low and vice-versa.

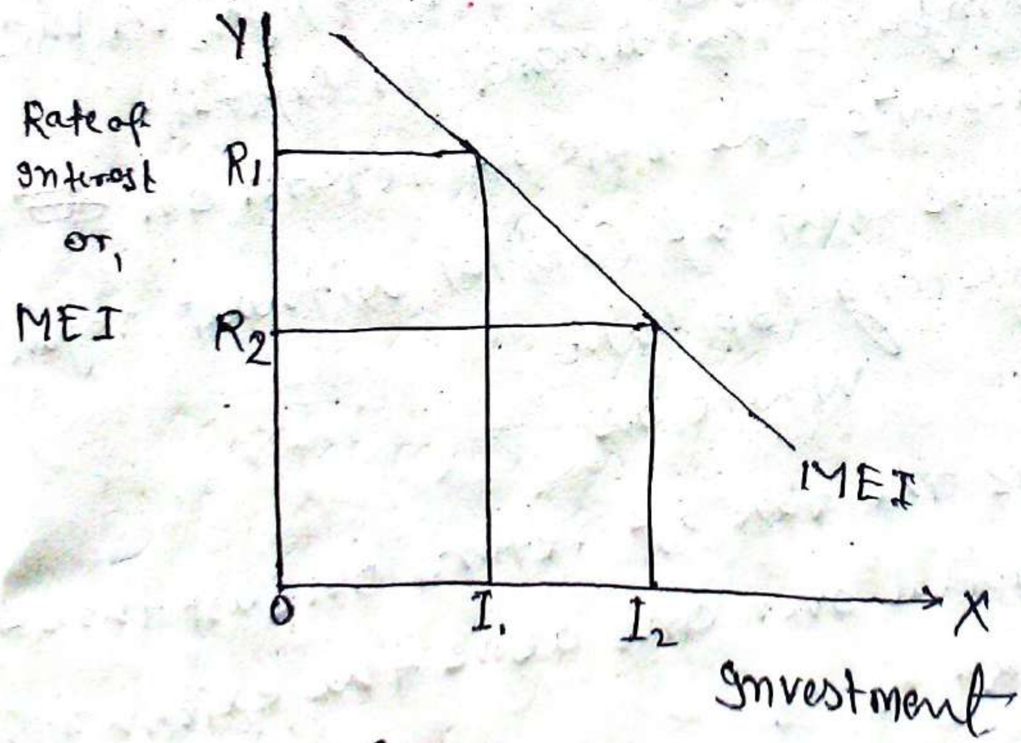

figure - MEI Curve

In the above figure, when Rate of Interest is OR_1 then the Investment is OI_1. When the Rate of Interest is decreased from OR_1 to OR_2 then ~~[illegible]~~ Investment is increased from OI_1 to OI_2.

if MEI curve has no more elastisity, The Rate of interest falls down and Result is increasing in investment will also fallsdown and vice-versa

☐ Relation between MEC (capital stock) and the MEI (Investment)

1). MEC is based on a given supply price of Capital.

where as

MEI is based on the induced change in price due to change in the demand for capital.

2) MEC represents the rate of return on all successive unit of capital without regard to ~~exis~~ existing capital.

where as

MEI shows the rate of return on just those unit of capital over and above the existing capital stock.

3) In MEC the capital stock is taken on the horizontal ~~axis~~ axis of diagram.

where as

In MEI the amount of investment is taken on the Horizontal axis of diagram.

To induce the private investment the following steps can be taken —

i) Cheap money policy

ii) Reduction in corporate taxes.

iii) Pump priming policy.

iv) Pricing Support policy. – (Stability)

v) promotion of Research

vi) Abolition of monopolistic tendencies.