# JAYOTI VIDYAPEETH WOMEN'S UNIVERSITY, JAIPUR

Government of Rajasthan established

## Faculty of Education and Methodology

**Faculty Name**- JV'n  Dr. Md Meraj Alam

**Program**- BA B.Ed 3$^{rd}$ Semester

**Course- Macroeconomics**

Digital session name – Investment Function – Types of Investment

**Introduction:**

In ordinary parlance, investment means to buy shares, stocks, bonds and securities which already exist in stock market. But this is not real investment because it is simply a transfer of existing assets. Hence this is called financial investment which does not affect aggregate spending. In Keynesian terminology, investment refers to real investment which adds to capital equipment.

It leads to increase in the levels of income and production by increasing the production and purchase of capital goods. Investment thus includes new plant and equipment, construction of public works like dams, roads, buildings, etc., net foreign investment, inventories and stocks and shares of new companies. In the words of Joan Robinson, "By investment is meant an addition to capital, such as occurs when a new house is built or a new factory is built. Investment means making an addition to the stock of goods in existence."

Capital, on the other hand, refers to real assets like factories, plants, equipment, and inventories of finished and semi-finished goods. It is any previously produced input that can be used in the production process to produce other goods. The amount of capital available in an economy is the stock of capital. Thus capital is a stock concept.

To be more precise, investment is the production or acquisition of real capital assets during any period of time. To illustrate, suppose the capital assets of a firm on 31 March 2004 are

Rs 100 crores and it invests at the rate of Rs 10 crores during the year 2004-05. At the end of the next year (31 March 2005), its total capital will be Rs 110 crores. Symbolically, let I be investment and K be capital in year t, then $I_t = K_t - K_{t-1}$.

Capital and investment are related to each other through net investment. Gross investment is the total amount spent on new capital assets in a year. But some capital stock wears out every year and is used up for depreciation and obsolescence. Net investment is gross investment minus depreciation and obsolescence charges for replacement investment. This is the net addition to the existing capital stock of the economy.

If gross investment equals depreciation, net investment is zero and there is no addition to the economy's capital stock. If gross investment is less than depreciation, there is disinvestment in the economy and the capital stock decreases. Thus for an increase in the real capital stock of the economy, gross investment must exceed depreciation, i.e., there should be net investment.

**Types of Investment**

### 1. Induced Investment

Real investment may be induced. Induced investment is profit or income motivated. Factors like prices, wages and interest changes which affect profits influence induced investment. Similarly demand also influences it. When income increases, consumption demand also increases and to meet this, investment increases. In the ultimate analysis, induced investment is a function of income i.e., $I = f(Y)$. It is income elastic. It increases or decreases with the rise and fall in income, as shown in figure.
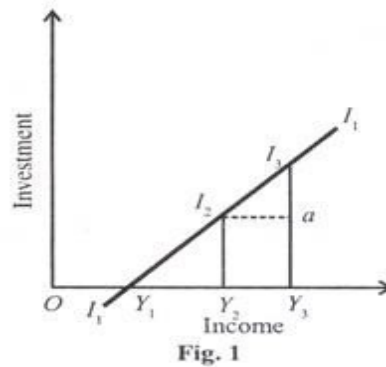
Source: Internet

I1 I1is the investment curve which shows induced investment at various levels of income. Induced investment is zero at OY1 income. When income rises to OY3 induced investment is I3Yy A fall in income to OY2 also reduces induced investment to I2Y2.

**Autonomous Investment**

Autonomous investment is independent of the level of income and is thus income inelastic. It is influenced by exogenous factors like innovations, inventions, growth of population and labour force, researches, social and legal institutions, weather changes, war, revolution, etc. But it is not influenced by changes in demand. Rather, it influences the demand. Investment in economic and social overheads whether made by the government or the private enterprise is autonomous.

Such investment includes expenditure on building, dams, roads, canals, schools, hospitals, etc. Since investment on these projects is generally associated with public policy, autonomous investment is regarded as public investment. In the long-run, private investment of all types may be autonomous because it is influenced by exogenous factors. Diagrammatically, autonomous investment is shown as a curve parallel to the horizontal axis as $I_1I'$ curve in Figure 2. It indicates that at all levels of income, the amount of investment $OI_1$ remains constant.
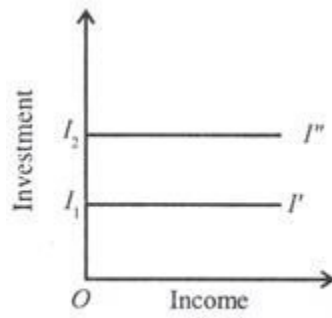
**Fig. 2**

Source: Internet

The upward shift of the curve to $I_2I''$ indicates an increased steady flow of investment at a constant rate $OI_2$ at various levels of income. However, for purposes of income determination, the autonomous investment curve is superimposed on the C curve in a 45° line diagram.