Sector 4: Factor Returns

Value-added, or gross domestic product, is composed of the incomes of the factors of production, which are also referred to as factor returns. In TIM, labour income (by industry) is formulated using a modified Phillips Curve as a function of the unemployment rate (Sector 3), expected inflation (Sector 5) and industry activity measures. In TIM, unlike similar models, industry value-added prices are not applied as a markup to unit labour costs. Rather, with the concept of a specific return to capital (i.e. surplus, non-labour GDP), TIM introduces unit capital costs, interest rates and other capital-related variables into the price formation process.

Sector 5: Prices

Domestic consumption prices are primarily determined in TIM as weighted combinations of industry value-added prices and foreign prices, using the input/output system. Selected export prices are determined in a similar fashion. All other trade prices are determined by exogenous foreign prices and the exchange rate.

Sector 6: Incomes

The principal component of personal income is labour income, derived in Sector 4. Corporate profits is a residual calculated after allocating other available income to government and the nonresidential sector. Most of government income is determined by direct taxes on other sector incomes and indirect taxes applied primarily to final demand.