What is Capital Formation?

Worksheet

Capital formation is the accumulation of productive assets (capital) like factories, equipment, and technology. It increases an economy's ability to produce goods and services over time.

Questions

1. What is capital formation?
A) Saving money
B) Forming a company
C) Creating productive assets
D) Earning interest

2. How does capital formation boost the economy?
A) Reduces prices
B) Increases productive capacity and output
C) Eliminates competition
D) Creates unemployment

3. Which is an example of capital formation?
A) Buying groceries
B) Building a factory
C) Watching TV
D) Renting a house

4. Why do poor countries need capital formation?
A) To consume more
B) To build productive assets and increase output
C) To reduce taxes
D) For entertainment

5. A country saves 20% of its income and invests it in new factories and equipment. How does this affect future productivity?

6. A small business takes a loan to buy new machinery. Is this capital formation?

7. A country invests heavily in technology and digital infrastructure. What long-term benefit occurs?

8. Define: What is capital formation?

9. Define: Is capital formation the same as saving?

10. Define: How does capital formation help the economy?

Answer Key

1. C) Creating productive assets — Capital formation is building productive assets that increase output.

2. B) Increases productive capacity and output — More capital → higher production → more output and growth.

3. B) Building a factory — A factory is a productive asset created through capital formation.

4. B) To build productive assets and increase output — Capital formation enables low-income countries to grow output and income over time.

5. Savings → capital formation (factories, equipment) New capital increases productive capacity Future output and GDP growth rise

6. Business borrows and buys machinery (capital asset) Machinery increases production capacity Yes, this is capital formation through business investment

7. Digital infrastructure = new capital asset Technology enables more efficient production Long-term productivity and competitiveness rise

8. The accumulation of productive assets (factories, equipment, technology) that increase production capacity.

9. No — saving is keeping money; capital formation is using savings to build productive assets.

10. It increases productive capacity, enabling more output, higher wages, and long-term growth.