

Economics Chapter 6 – GDP and Real GDP

1. The economy should aim for price stability, low unemployment, and high and sustained economic growth
2. **Gross Domestic Product (GDP)**– the total market value of all final goods and services produced annually within a country's borders
3. **Flow Variable** – a variable that is only meaningful over a period of time. GDP is a flow variable
4. **Stock Variable** – a variable that is meaningful at a moment in time. Example: US Money supply
5. **Gross National Product (GNP)** – The total market value of all final goods and services produced annually by the citizens of a country
6. GDP measures the production of goods and services in the physical area of a country, while GNP measures the production of goods and services by the citizens of a country.
7. **Total Market Value** – the monetary value of all goods and services at today's prices
8. **Nominal GDP** – GDP at current prices
9. **Final good** – a good in the hands of its final user
10. **Intermediate good** – a good that is an input in the production of a final good
11. **Double Counting** – counting a good more than once while computing GDP
12. Only final goods are counted in the GDP because the price of the final good is based on the price of all the intermediate goods used to produce the final good. If all the intermediate goods were also counted, double counting would occur.
13. What GDP Omits – certain aspects of the market are not included in the GDP
 - a. **Certain non-market goods and services** - If a family hires someone to mow the lawn, the salary paid to the gardener is included in the GDP. However, if the family does it themselves, then the “price” of the service is not included in the GDP.
 - b. **Underground Activities, both legal and illegal** – unreported exchanges that take place outside the normal recorded market channels, including the sales of illegal goods. They are not counted because there is no record of them taking place. Also, some cash transactions that are unreported are left out.
 - c. **Sales of Used Goods** – sales for used goods aren't counted because the good was already counted into the GDP when it was sold new.
 - d. **Financial Transactions** – the trading of stocks and bonds are not counted in GDP because it does not represent the production of new assets, only the trading of assets.
 - e. **Government Transfer Payments** – a payment to a person that is not made in return for goods and services currently supplied. Examples: welfare, social security, etc.
 - f. **Leisure** – leisure isn't counted because it is too difficult to quantify. If an individual takes a week off, his salary during that week isn't counted into the GDP.
 - g. **Bads Generated in the production of goods** – Production of goods often have side effects, such as pollution. The GDP only counts the price of the good, but does not factor out any harmful side effects that may accompany it.
14. A high GDP doesn't necessarily result in a high standard of living. Some Middle East nations have a very high GDP due to oil production, but a very low standard of living, since most of the income from the oil is going to foreign investors.
15. **Per Capita GDP** – the result of dividing a country's GDP by the population of the country.
16. The GDP is computed by the Bureau of Economic Analysis (BEA)
17. **Consumption** – the sum of spending on durable goods, non-durable goods, and services
18. **Investment** – the sum of all purchases of newly produced capital goods, changes in business inventories, and purchases of new residential housing
19. **Inventory Investment** – changes in the stock of unsold goods
20. **Fixed Investment** – business purchases of capital goods, such as machinery and factories, and purchases of new residential housing
21. **Government purchases** – includes federal, state, and local government purchases of goods and services and gross investment in highways, bridges, etc.
22. **Imports** – total domestic spending on foreign goods
23. **Exports** – total foreign spending on domestic goods
24. **Net Exports** – exports minus imports
25. **The Expenditure Approach** – GDP is the sum of all the purchases of final goods and services made up by the household, business, government, and foreign sectors of the economy. Anything that is produced and isn't sold is “purchased” by the manufacturer.

GDP = consumption + Investment + government purchases + Net Exports
26. **The Income Approach** – GDP is the sum of all the income in the four sectors. For every dollar a consumer spends, someone else, or a group of people, earn a dollar.
27. **Domestic Income** – the total income earned by the people and businesses within a country's borders
28. **National Income** – total income earned by US citizens and businesses, regardless of location

National Income = compensation to employees + proprietor's income + corporate profits + rental income of persons + net interest + depreciation (negative) + indirect Business Taxes + net income of foreigners

29. **Compensation of Employees** – wages and salaries paid to employees plus employer's contributions to social security and employee benefit plans and the monetary value of fringe benefits, tips, and paid vacations.
30. **Proprietor's Income** – all forms of income earned by self employed individuals and owners of unincorporated businesses.
31. **Corporate Profits** – all income earned by the stockholders of corporations. Some of the profits are paid in the form of dividends, some are kept within the firm to finance investments, others are used to pay corporate taxes
32. **Rental Income of Persons** – the income received by individuals for the use of their nonmonetary assets, including land, houses, offices, etc. It also includes returns to individuals who hold copyrights and patents, as well as an imputed value to owner occupied houses. In short, home ownership is considered a business with a "service charge" paid to the owner of the business.
33. **Net Interest** – The interest income received by US households and government minus the interest they paid out
34. **Depreciation** – the value at which capital and technology lose value over time. Net Investment = investment – depreciation
35. **Indirect Business Taxes** – sales taxes sent directly by businesses to the government
36. **Net income of foreigners** – the income made by foreigners, since they contribute to the gdp, but are not included in the US labor income (ie. Canadian basketball players)
37. **Production Approach**
 - a. Add up the value of everything produced, counting only the value added by each manufacturer.
 - b. If a company pays \$100 to buy trees, makes paper, sells for \$200, then the value added is \$100
38. **The national income doesn't equal the GDP because several factors have been left out:**
39. **Income earned from the rest of the world, income earned by the rest of the world** – both these factors need to be factored into the GDP. The income earned from the rest of the world is subtracted from the national income, then adding to the national income the income earned by the rest of the world.
40. **Indirect Business Taxes** – excise taxes, sales taxes, and property taxes. These taxes are not part of national income because they are not considered a payment to any resource. However, since they are included in purchases of goods and services, they need to be added to the GDP
41. **Capital Consumption Allowance** – The cost to replace capital goods that are used up through natural wear and tear. Also known as **depreciation**. This also must be factored into the GDP.
42. **Statistical Discrepancy** – GDP and national income are computed using different sets of data. Hence, there may be some discrepancies that must be accounted for.
43. Net Domestic Product (NDP) – the value of GDP – the capital consumption allowance
44. **Personal Income** – the amount of income that individuals actually receive. It is equal to national income minus undistributed corporate profits, social insurance taxes, and corporate profits taxes
45. **Disposable Income** – The portion of personal income that can be used for consumption or saving. It is equal to personal income – personal taxes
46. **Per Capita Macroeconomic Measurements** – Often economists like to use per capita measurements, which is the national measurement divided by the population
47. **Real GDP** – the value of the entire output produced annually within a country's borders, adjusted for price changes
48. We use a real GDP because we want to know the REASON for a rise in GDP. A rise in prices can cause a rise in GDP, so the real GDP measures the GDP after being adjusted for price, so a rise in the Real GDP usually implies a rise in production.
49. **Computing Real GDP** – multiply the quantity of the good produced in a given year by the price in the base year
Real GDP = The summation of the base year prices * current year quantities
50. **GDP Deflator** – nominal GDP/real GDP
51. **Alternate Method of Computing Real GDP** – divide GDP by the chain weighted price index *100
52. **Economic growth** – increases in real GDP
53. **Business Cycle** – recurrent swings in real GDP
54. **Peak** – real GDP is at a temporary high
55. **Contraction/recession** – a decline in real GDP. If a real GDP falls for two consecutive quarters, it is said to be in a recession
56. **Trough** – the low point in real GDP, just before it begins to turn up
57. **Recovery** – the period when Real GDP is rising. It begins at the trough and ends at the initial peak.
58. **Expansion** – increases in Real GDP beyond the recovery
59. **National Savings** – Savings = Investment + net exports.
60. **Personal Savings** – Personal Savings = Income – consumption – personal taxes