

Book: *Economics*, Parkin, Powell, and Matthews.

Economics, Hall and Lieberman (www.4shared.com)

Exam based on what's covered in lecture

Questions each week (similar to exam)

Macroeconomics

Concerned with aggregates: output at economy-wide level, unemployment, inflation.

Two Subfields:

1. Long-Run Growth
2. The Business Cycle

Today: look at measurement of economic activity

Need measure of annual output/production in an economy

Gross Domestic Product: the total market value of final goods and services produced within a country in a given period.

e.g., 1 car worth 5 and 2 tables worth 10. Then *nominal GDP* is 25

Nominal GDP in One-Good Economy

Year	Quantity	Price	Nom. GDP
1999	5	2	10
2000	5	4	20
2001	7	5	35

Only interested in production (which determines welfare)

Real GDP: measures value of final production using *constant* prices.

Base Year

Nominal GDP

Year	Quantity	Price	Nom. GDP
1999	5	2	10
2000	5	4	20
2001	7	5	35

Real GDP in 1999 Prices

Year	Quantity	Price	Real GDP
1999	5	2	10
2000	5	2	10
2001	7	2	14

Real and Nominal GDP equal in base year

Growth in real GDP is important.

Population

But more important is growth of real GDP per capita

⇒ rising living standards

Inequality

Cross-sectional data: use same prices for each country.

In general, “GDP” refers to real GDP

Gross *National* Product: value of output produced by *domestic* residents regardless of location.

In Ireland GNP is about 85% of GDP

GDP Measurement (Measure of *Production*)

Expenditure Method

$$C + I + G + X$$

$$Y = \underbrace{C + I + G + X} - M$$

Current Account: $X - M$

Subtle Point: Inventory Investment

Example: suppose you go to dentist and pay fifty euros:

- The value of production is 50.
- The value of expenditure is 50.
- The dentist's income is 50.

Production=Expenditure=Income

Issues Related to GDP Measurement

- Restaurant buys wine for 5 sells for 7. Value Added. Avoid double counting
- Black market
- Home production
- Wars etc
- Quality of National Statistics
- A labour/leisure choice?
- Because it indicates ability to pay, use GDP in debt/deficit ratios

Economic Fluctuations

Potential GDP, Y_n

Output gap, $Y - Y_n$

Proportional deviation from potential: $\frac{Y - Y_n}{Y_n}$.

An important variable for economic policy

Inflation and Output Gap

Unemployment and Output Gap

Measuring Inflation

CPI: Price index

Measure price of fixed basket of goods.

Base year.

Fixed basket: 2 apples 1 orange

CPI: Two Apples, One Orange

Yr	A.	O.	Basket Price	CPI
1	5	1	$2(4.5)+1(1)=10$	$\frac{10}{10} \times 100 = 100$
2	6	2	$2(6)+1(2)=14$	$\frac{14}{10} \times 100 = 140$
3	7	1	$2(7)+1(1)=15$	$\frac{15}{10} \times 100 = 150$

Inflation is percentage change in CPI

Hyperinflation

Deflation

Disinflation