

Chapter 6, Gross Domestic Product (GDP) and Real GDP (RGDP)

I. Gross Domestic Product

A. A Definition of GDP

1. Total market value of all final goods and services produced annually within a country's borders.
2. Concepts behind the definition
 - a. Total market value: the sum of all prices times all quantities
 - 1) We cannot add apples and oranges
 - 2) It gives us a measure of economic activity, with dollars as the yardstick.
 - b. Final G/S: we do not count "intermediate" goods; we'd be double-counting.
 - c. Goods and services: It's not just the tangible stuff.
 - d. Annually: GDP is a "flow" variable (one year), not a "stock" variable (12-31).
 - e. Within the country's borders, not BY the country
 - 1) GDP is the measure of economic activity within our borders.
 - 2) GNP, Gross National Product is the same definition, except that "by the country's citizens" substitutes for "within the country's borders". That is, with GNP we measure what our citizens do, whether here or elsewhere. With GDP, we measure what anyone working in the United States does, whether they are a U.S. citizen or a non-citizen.
 - 3) Other countries have used GDP for years. Only recently have we started using GDP instead of GNP in the United States. For us, GDP and GNP are not very different. For poorer countries, the differences can be huge.

B. GDP Omissions

1. Nonmarket activities
2. Underground activities, legal and illegal
3. Used goods
4. Financial transactions and government transfer payments
5. Leisure
6. "Bads" (pollution, crime, congestion...)

C. Computing GDP

1. Expenditures approach: $GDP = C + I + G + (X - M)$
 - a. Consumption (except residential housing): \$6257B
 - b. Investment (includes residential housing): \$1623B
 - c. Government Purchases: \$1630B
 - d. Net Exports: -\$256B
2. Income approach
 - a. Circular Flow I
 - b. Circular Flow II
 - c. National income is sum of payments to factors or production
 - 1) FOP: Labor, land, capital, entrepreneurship
 - 2) Payments: Wages, rent, interest profit
 - d. Formal definitions
 - 1) Compensation of employees: \$5332B
 - 2) Proprietors income: \$659B
 - 3) Corporate profits: \$879B
 - 4) Rental income (personal): \$146B
 - 5) Net interest: \$476B

3. Other national income measures
 - a. Net domestic product
 - b. Personal income
 - c. Disposable income
 - d. "Per capita" income (PCI, PCDI)

II. Real GDP: GDP adjusted for inflation

- A. Increases in "nominal" GDP could be increases in either prices or quantities.
 1. We're interested in what is "real", not what is just inflated prices.
 2. Adjust nominal GDP by controlling for prices
 3. $RGDP = GDP / \text{"price index"} * 100$
 4. Compare 1991 in Exhibit 5 (p. 143) with Exhibit 6 (p. 150)
- B. Economic growth is growth in RGDP
- C. Business Cycles
 1. Peak
 2. Contraction
 3. Trough
 4. Expansion
 5. From peak to peak is one business cycle.