Elasticity, GDP, GNP, and Price Indices

Econ 9: Section 3

TA: Sara Sutherland

i. Practice problem from section 2 (Jill's demand for lattes)

ii. GDP:

a. Why do we care about GDP?
   i. Measure of the "size" of the economy; Indicator of economic health; Indicator of standard of living
   ii. Total dollar value of all goods and services produced over a specific time period (usually over quarter of a year)
   iii. Calculated by adding total consumption, investment, government spending and net exports.

$$\boxed{GDP = C + I + G + \text{Net Exports (Exports-Imports)}}$$

C: Personal consumption expenditures.

I: Investment (Spent on goods to make more goods)

G: Government spending.

iii. GNP:

a. Includes GDP plus income earned by residents from overseas investments minus income earned in the domestic economy by overseas resident.
   i. 2014 highest GNP per capita: Luxembourg ($45,360)
   ii. 2014 lowest GNP per capita: Mozambique ($80)

b. GNP Formula:

$$\boxed{GNP = GDP + RI - FI}$$

RI: Income earned by residents from over seas investments

FI: income earned within the domestic economy by overseas residents.

iv. **Price Indices**

a. What are they used for?
   i. Used to assess price changes associated with cost of living.
   ii. Was _______ really cheaper back in the day?
b. A price index is a weighted average of prices of a selected "basket of goods and services relative to their prices in some baseline-year
c. What sort of goods?
   i. (examples)
d. Rate of change of prices: Inflation

REVIEW QUESTIONS

1. Macroeconomics can best be described as the:
A) analysis of how a consumer tries to spend income.
B) study of the large aggregates of the economy or the economy as a whole.
C) analysis of how firms attempt to maximize their profits.
D) study of how supply and demand determine prices in individual markets.

2. If we say that two variables are directly related, this means that:
A) the relationship between the two is purely random.
B) an increase in one variable is associated with a decrease in the other variable.
C) an increase in one variable is associated with an increase in the other variable.
D) the two graph as a down sloping line.

3. If we say that two variables are inversely related, this means that:
A) the two graph as an up-sloping line.
B) an increase in one variable is associated with a decrease in the other.
C) an increase in one variable is associated with an increase in the other.