

WHAT'S IN GDP?

STUDENT HANDOUT

ACTIVITY 1: Components of GDP

Which component of GDP would each of these fit into?

1. _____ Mechanic fixes a transmission
2. _____ A business purchases computer software and a PC
3. _____ A local library purchases new audio books
4. _____ A retailer purchases tennis shoes from a manufacturer in China and sells them
5. _____ Mother purchases those tennis shoes from the retailer

Write one more example of each of the four components.

6. _____ Consumption
7. _____ Investment
8. _____ Government spending
9. _____ Net exports
10. Explain why the sale of used goods is not included in GDP. _____

ACTIVITY 2: Nominal and real GDP

You are an economist who has been asked to calculate your nation's GDP, which produces only three goods/services. Calculate nominal GDP for Year 1 and Year 2. $GDP = price \times quantity$.

Year 1 Nominal GDP				Year 2 Nominal GDP			
	Price	Quantity	GDP		Price	Quantity	GDP
Oil changes	\$15	5	\$75	Oil changes	\$18	6	\$108
Hamburgers	\$2	20	\$40	Hamburgers	\$3	25	\$75
MP3 players	\$150	3	\$450	MP3 players	\$175	5	\$875
		Total	\$565			Total	\$1,058

11. By how much has GDP increased from Year 1 to Year 2? _____

Now calculate Year 2 real GDP using Year 1 as the base year.

Year 2 Real GDP			
	Price	Quantity	GDP
Oil changes	\$15	6	\$90
Hamburgers	\$2	25	\$50
MP3 players	\$150	5	\$750
		Total	\$890

12. By how many dollars was nominal GDP overstating GDP in Year 2? _____

13. How much has real GDP increased from Year 1 to Year 2? _____

14. Why is it important to adjust nominal GDP for inflation? _____

ACTIVITY 3: Other Measures of Standard of Living

Economists often use real GDP over the long run to understand changes in a nation's economic growth. Real GDP tends to increase as a nation's standard of living improves; however, GDP does not capture some very important social measures. For example, other factors that can give insight into a population's well-being are income distribution, the literacy rate, the mortality rate, and life expectancy.

Using the Internet, investigate one of the following measures of the standard of living in a country:

- Gini Coefficient
- Human Development Index
- Human Poverty Index
- Gross National Happiness

Create a presentation for your classmates about your standard of living measure. As part of your presentation, address the following issues:

1. How is the measure calculated? That is, what factors does it include?
2. What are the advantages and disadvantages of the measure?
3. Evaluate the measure's effectiveness in determining a country's standard of living.

ACTIVITY 4: Assessment

1. Assume that a country has a closed economy that has only three goods/services. That is, there is no trade with other countries, so the economy has consumption, investment, and government spending, but no net exports. In a given year, the economy produces
 - three haircuts that cost \$10 each
 - two factory machines that cost \$100 each
 - one highway repair that costs \$500

1a. What is total GDP for this economy? _____

1b. What percent of GDP is consumption? _____

1c. What percent of GDP is investment? _____

1d. What percent of GDP is government spending? _____

2. Suppose an economy's nominal GDP increased 3 percent in 2008. Why is this information alone not enough to determine whether the economy experienced economic growth? What other information would you need?

3. Why is GDP not the best measure of standard of living? What other factors should be considered when one determines a country's standard of living relative to other countries?
