GDP

Introduction & The Expenditure Approach

The Circular-Flow Diagram

The Circular Flow

The National Accounts

- Households earn income via the factor markets from wages, interest on bonds, dividends on stocks, and rent on land.

Income from the Factor Market

**Income received by Households**
- Wages
- Rent
- Interest
- Profit

**Factors of Production**
- Labor
- Land
- Financial Capital
- Physical Capital
The National Accounts

Via the financial markets, private savings is channeled to firms for investment spending (I).

An Expanded Circular-Flow Diagram: The Flows of Money Through the Economy

Investment Spending

- Spending on productive physical capital and changes to inventories
  - Inventories seen as contributing to the future sales of the firm
    - Spending on additional inventory adds to Investment spending
    - Drawing down inventories is counted as fall in Investment spending
Government purchases of goods and services (G) is paid for by tax receipts as well as by government borrowing.

Exports (X) generate an inflow of funds into the country from the rest of the world. Imports (IM) lead to an outflow of funds to the rest of the world. Foreigners can also buy stocks and bonds in the U.S. financial markets.
An Expanded Circular-Flow Diagram: The Flows of Money Through the Economy

GDP=C+I+G+(X-IM)

- **C**: Consumer spending
- **I**: Investment
- **G**: Government
- **X**: Exports
- **IM**: Imports

What Is GDP?

- **GDP** is the nation's expenditures on all **FINAL** goods and services produced during the year at market prices.
The Flow Not Stock

- With GDP we are measuring a Flow or a movement NOT a Stock
  - The store of wealth is a stock concept.

A Stock Concept

- How Much is a Stock Concept
- GDP is a flow concept

In Macroeconomics
- Expenditures Equals Income

Expenditure Arm
Income Arm
How GDP Is Measured?

Income (wages, salary, rent, interest, profits)

$\downarrow$

Firms

$\uparrow$

Households

Expenditures by Consumers, Investors, Government, and Net Exports

9-6

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How GDP Is Measured?

Income (wages, salary, rent, interest, profits)

$\downarrow$

Firms

$\uparrow$

Households

Same As

Expenditures by Consumers, Investors, Government, and Net Exports

9-7

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How GDP Is Measured?

Income (wages, salary, rent, interest, profits)

$\downarrow$

Firms

$\uparrow$

Households

Same As

Value of what is produced

Value of what is spent

Expenditures by Consumers, Investors, Government, and Net Exports

9-8

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How GDP Is Measured?

Income (wages, salary, rent, interest, profits)

Flow of Income Approach $ Value of what is produced

Firms

Same As

Households

Expenditures Approach $ Value of what is spent

Expenditures by Consumers, Investors, Government, and Net Exports

(GDP = C + I + G + Xn )

The Components of GDP 2000 (in $ billions)

- **Consumption**
  - Durable goods .......... $ 820
  - Nondurable goods ...... 2,010
  - Services .................. 3,929
  - Total C .................. $6,759

- **Investment**
  - Plant & Equipment ....... $ 1,361
  - Residential Housing .... 416
  - Inventory change ........ 57
  - Total I .................. $1,834

- **Government Purchases**
  - Federal .................. $ 595
  - State and Local ........... 1,146
  - Total G .................. $1,743

- **Net Exports (Xn)**
  - Exports .................. $ 1,099
  - Imports ................... 1,666
  - Xn .......................... $ - 370

- **GDP** .................. $9,966
The Components of GDP, 2000 (in Billions)

- Consumption
  - Durable goods .......... $320
  - Nondurable goods ...... 2,010
  - Services ............... 3,929
  - Total C .................. $6,759

- Investment
  - Plant & Equipment ...... $1,361
  - Residential Housing ... 416
  - Inventory change ....... 57
  - Total I .................. $1,834

- Government Purchases
  - Federal .................. $595
  - State and Local ........ 1,148
  - Total G .................. $1,743

- Net Exports (Xn)
  - Exports .................. $1,099
  - Imports .................. 1,466
  - Xn ........................ $ - 370
  - GDP ..................... $9,966

GDP = C + I + G + Xn
GDP = 6,759 + 1,834 + 1,743 + (-370)
GDP = 9,966

GDP is a flow concept

Income Arm
Expenditures Equals Income

Expenditure Arm

What’s measured on the income side?
\[
\begin{array}{ll}
\text{Income received by Households} & \text{Factors of Production} \\
- Wages & - Labor \\
- Rent & - Land \\
- Interest & - Financial Capital \\
- Profit & - Physical Capital \\
\end{array}
\]