Chapter 2 Exercises

1. In the national income accounts, what is the difference between
   a. A firm's buying an auto for an executive and the firm's paying the executive additional income to buy the automobile herself?
   b. Your hiring your spouse (who takes care of the house) rather than having him or her do the work without pay?
   c. Your deciding to buy and American car rather than a German car?

2. Show from national income accounting that
   a. An increase in taxes (while transfers remain constant) must imply a change in net exports, government purchases, or the saving-investment balance.
   b. An increase in disposable personal income must imply an increase in consumption or an increase in saving.
   c. An increase in both consumption and saving must imply an increase in disposable income.

3. The following is information from the national income accounts for a hypothetical country:

GDP	$6,000
Gross investment	800
Net investment	200
Consumption	4,000
Government purchases of goods and services	1,100
Government budget surplus	30

What is
   a. NDP?
   b. Net exports?
   c. Government taxes minus transfers?

      d. Disposable personal income?

      e. Personal saving?

4. Consider an economy that consists only of those who bake bread and those who produce its ingredients. Suppose that this economy's production is as follows: 1 million loaves of bread (sold at $2 each); 1.2 million pounds of flour (sold at $1 per pound); and 100,000 pounds each of yeast, sugar, and salt (all sold at $1 per pound). The flour, yeast, sugar, and salt are sold only to bakers, who use them exclusively for the purpose of making bread.

      a. What is the value of output in this economy (i.e., nominal GDP)?

      b. How much value is added to the flour, yeast, sugar, and salt when the bakers turn them into bread?

5. Suppose a country's CPI increased from 2.1 to 2.3 in the course of 1 year. Use this fact to compute the rate of inflation for that year. Why might the CPI overstate the rate of inflation?