↳ GROSS DOMESTIC PRODUCT (GDP):

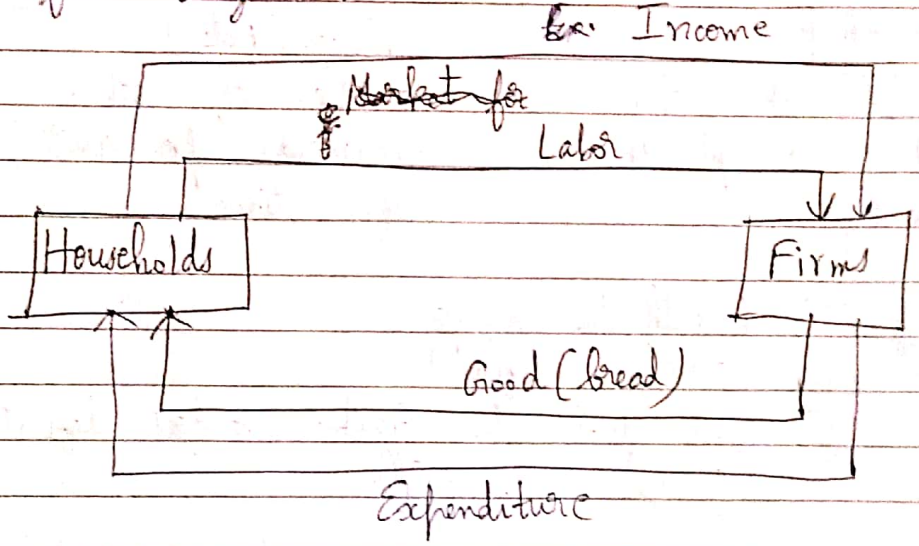
→ Total monitory value of goods & services produced by the nation in a given period of time.

→ GDP measures → values of goods & services.
→ the total income of everyone in an economy or the total expenditure on the economy's o/p of goods & services.

GDP: Income = expenditure (in an Economy)

[Income of the seller] = [Expenditure of the buyer.] → from rules of accounting.

→ GDP measures the flow of dollars in the circular flow diagram:



→ Flow of i/p & o/p.
→ Flow of dollars

Here, GDP = Total Income of firms (OR) Total expenditure by households.

Every transaction that affects expenditure also affects income & vice-versa.

Eg: If firms produce ↑ bread ⇒ ↑ expenditure ⇒ ↑ income.

Reason:

Case 1: Firms ⇒ [↑ Hired] by ↑ labour (flow)
⇒ expenditure ↑ (household) ⇒ income ↑ (firms)

Case 2: Firms ⇒ [↑ hired] by ↓ labour (flow)
⇒ expenditure ↑ ⇒ income ↑

↳ Ways to measure GDP:
- ↳ Production Method Approach.
- ↳ Income Approach
- ↳ Expenditure Approach. ☆

↳ Stock
→ Qty. of sth. at a pt. of time.

Flow (Rate)
→ Qty. of sth. measured for unit of time.

↳ Eg: ① Wealth & Saving
(stock) (flow)
② Govt debt & Govt. budget deficit
(stock) (flow)

↳ Investment
→ Spending money on new capital.

Capital (Stock)
→ factor of production

↳ EXPENDITURE APPROACH:
↳ GDP is calculated with expenditure
↳ 4 components → Net expenditure, exports

In expenditure approach, GDP = Y is:

$$Y = C + I + G + NX$$

Every dollar of GDP ∈ C, I, G, NX.

equation is an identity called as: "National Income Accounts Identity".

Consumption (C) → Goods & services bought by households.

→ Non-durable goods:
- → last for a short time.
- → Eg: Food, clothing

→ Durable goods:
- → last for long time
- → Eg: TVs, computers.

→ Services:
- → Work done for consumers by individuals and firms.
- → Eg: haircut, doctor visits.

Investment (I) → consists of goods bought for future use.

categories

→ Business fixed investment:
Purchase of new equipment by firms.

→ Residential fixed investment:
Purchase of new housing by households

↳ Inventory investment:
↑ in firms' stocks (inventory) of goods.

→ Govt. purchases (G):
↳ goods & services bought by Govt.
↳ Military equipments, highways & services provided by Govt. workers.
↳ excluded ↑ Security, welfare, transfer payments to individuals (households)
⇓
income to individuals. Here expenditure approach is used to calculate GDP. So, ignore this. → already considered C, household's expenditure.

→ Net Exports (NX):

NX = (Export) − (import)

↓ value of goods & services foreigners sell to us.

value of goods and services sold to other countries.

→ Closed economy → NX = 0
→ Open economy → NX > 0 → export > import
NX < 0 → export < import
Both export & import ≶
No export/import.

→ Closed economy → Y = C + G + I

→ Open economy → Y = C + I + G + NX.

Gross National Product (GNP): → part of GDP
Total income earned by the nation's factors of production regardless of your location.

↳ Net National Product (NNP):
Difference b/w factors payments from abroad and those to abroad.

(A) NNP = GNP − GDP
= (Factor payments from abroad) − (Factor payments to abroad)

NNP shows the total income of the nation.

↳ GDP → measures values of all final goods & services.
→ Nominal GDP → measures values of all final goods & services using CURRENT PRICES
→ Real GDP → measures values of all final goods & services using PRICES OF A BASE YEAR.
↳ = 2010 (now).

↳ GDP Deflator:

(A) GDP deflator = 100 × Nominal GDP / Real GDP

↳ Inflation Rate:

(A) inflation rate = % increase in overall level of prices

↳ Consumer Price Index (CPI):

CPI in the period = 100 × Cost of basket in that period / Cost of basket in base period

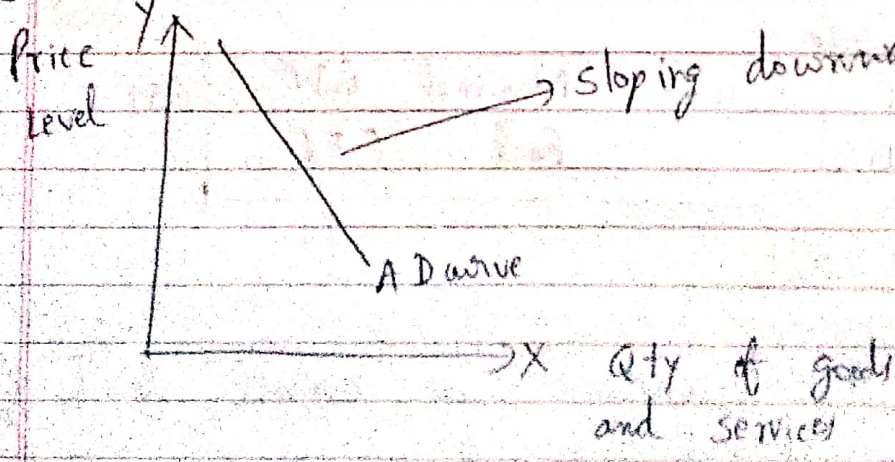
→ year-wise, mth-wise etc.,

↳ Aggregate demand:
Total demand for all final goods & services in an economy at a given time.

↳ Aggregate supply:
Total supply of all individual goods & services combined.

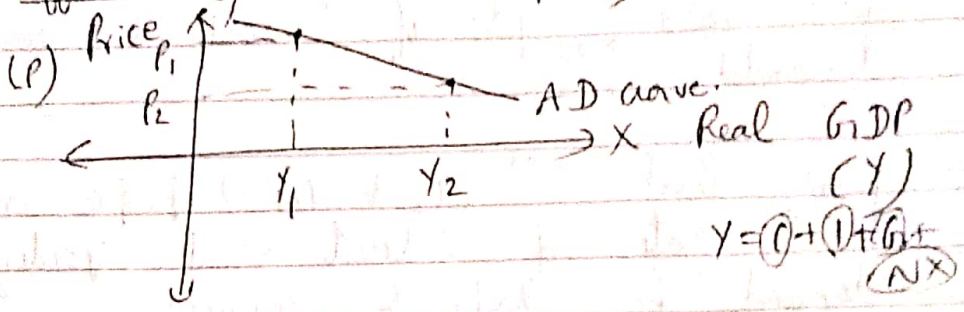
↳ Model of Aggregate demand & supply: (IS-LS Model)
↳ 2 components:
↳ X-axis: Real Qty. of all goods & services demanded measured using real GDP.
↳ Y-axis: Avg. Price Level of all goods & services as measured by GDP deflator or CPI.

→ AD curve:



• AD curve is sloping downwards because:
  - → Wealth effect (Price Level and Consumption)
  - → Interest rate effect (Price level & investment)
  - → Net exports effect. (Exchange rate effect)

① Wealth effect: (due to consumption)



① P_1 to P_2 → price-level ↓ so ⇒ real value of money ↑ so ⇒ Consumers wealthy ⇒ spend more ⇒ ↑ qty demanded.

$P_2 < P_1$

⇒ $Y_2 > Y_1$.

② P_2 to P_1 → price ↑ so ⇒ real value of money is less ⇒ Consumers are poor → spend ↓ ⇒ ↓ qty demanded.

$P_1 > P_2$

⇒ $Y_1 < Y_2$

Eg: Real Value of ~~mon~~ money.

(i) Cost of a pen = Rs. 10 and customer has Rs. 20 in his wallet then no. of pens bought = 2.

⇒ Real value of Rs. 20 = 2.

(ii) Cost of a pen = Rs. 20 and customer has Rs. 20. No. of pens bought = 1.

⇒ Real value of Rs. 20 = 1.

② Interest rate effect: (price level and investment)

→ price level ↓ ses (P_1 to P_2) ⇒ people invest ↑ money in interest-bearing assets like banks/ informal loans ⇒ lower rate of interest ⇒ ↑ loans ⇒ ↑ spending of firms to buy equipments, household to buy large durable purchases like cars ⇒ qty of goods & services demanded ↑ ses.

→ price level ↑ ses (P_2 to P_1) ⇒ people invest ↓ money ⇒ ↑ rate of interest ⇒ ↓ spending ⇒ ↓ demand for goods & services.

③ Net exports effect:

→ US: price level ↓ ses ⇒ interest rates ↓ ⇒ real exchange value of $ ↓ ies ⇒ foreign goods more expensive ⇒ import ↓. But, for foreign countries, US → dollar rate ↓ ⇒ exports ↑. (U.S. goods are cheaper. → (bcoz ↑ dollars should be supplied → value of $ ↓).

Net exports = Exports − imports
(NX) ↑ ↓

⇒ NX ↑ ⇒ demand for goods & services ↑.

↳ Externalities → +ve, −ve → refer Gregory Mankiw main T.B.

↳ CPI calc. + prob. → refer Eco C.W.