Date:

Urban consumer in each ~~year~~ respective country. Inflation can also be calculated with other price indexes such as produce price index or the so called GDP deflator.

Most countries try to keep inflation some where around 2-3 percent per year. That is too low to cause any problems for the businesses and households. At the same time, it is comfortably away from negative inflation i.e from deflation.

Eg8 If base year price of Basket is 20,000 and its value is 100 and if next year its value increase to 105 so the rate of change is as following.

Date:

Government:

The goods and services bought by the federal, state or local govt, it includes the military equipment, highways, and services provided by the govt workers. It excludes transfer payments such as social security or unemployment insurance benefits. This is done to avoid double countries, As it is not purchase of goods and services and they will use it for consumption.

Net Export:

The value of goods and services sold to other countries (Export) - the value of goods foreigners sells us (imports).

$$NX = Exports - Imports$$

Scanned with CamScanner

in 2013 BEA changed its mind and decided that expenditure would be treated like expenditure on a building a factory or a house. These are now added to the investment component of GDP.

Scanned with CamScanner

Date:

+ive When Exports > Imports

-ive When Imports > Exports

→ It represents the net expenditure from abroad on our goods services which provides income of domestic producers.

→ US GDP In 2007

	Billions	% of GDP	Per Capita
Y	$ 13,841	100.0	$ 45,825
C	9,734	70.3	32,228
I	2125	15.4	7037
G	2690	19.4	8905
NX	-7.8	-5.1	-2,344

→ Roles for Computing GDP

P ⇒ Price   Q ⇒ Quantity

Scanned with CamScanner

Date:

5 %

It is of 3 types.

→(1) Monthly

→(2) Quarter

→(3) Year

Solution 8

Inflation develops into a hyper inflation if it is not controlled in the initial stage itself, therefor it becomes crucial for the govt to undertake various steps to control inflation

→ Basic Cases of inflation are excess money supply in economy and excess Purchasing Power in the hands of the public, if both there factors

Scanned with CamScanner

Date:

new plant and equipments by firms i.e machines tools etc. It is called capital equipment.

* Residential fixed :

Purchase of new houses, factories, office, building by the land loards it is called structures.

* Inventory Fixed :

Inventries fixed (Goods produceds but not sold yet.

→ Company produces an item instead of selling it adds it into the inventory. The company has assumed to have purchased it for itself, thus it is a part of campanies inventory.

→ If it sells it out the investment will be negative.

Scanned with CamScanner

Date:

→ Unemployment rate:

Unemployment occures when a person who is actively searching for employment is unable to find work.

Issues in Macroeconomics

→ Inflation:

Rate of change in price. The inflation is measured by C.P.I (consumer price index).

→ CPI:

Inflation in Pakistan and other countries is calculated as a percent change in the consumer price index (CPI) from one year to the next. The CPI represents the price paid by the average

Date:

Using current Prices in its measures.

Difference :

The main difference between the real and nominal GDP is the adjustment for inflation, Since nominal GDP is calculated using current Prices it does not require any adjustments for inflation.

→ Inflation rate :

Inflation means an increase in the price of goods and services rise and decrease the value of money (Purchasing Power).

⇒ Measures how fast prices are rising.

Scanned with CamScanner

Date:

Note:

(i) **For Renters:**

Consumption includes rental payment

(ii) **For home owners:**

Consumption includes the imputed rental value of the house, but not the purchase price, or mortgage payments.

- **Investment (I):**

The total spending on goods that will be used to produce more goods in future.

Note:

Investment does not mean the purchase of financial assets like stocks and bonds.

Three types:

* **Business fixed:**

The purchase of

Chapter NO 2

Date:

The Measurement OF GDP

→ **Definition:**

The market value of final goods and services produced with in a country in a given period of time.

• **Market value:**

→ Goods are valued at their market Price

→ All goods are measured in the same value i.e Dollars in US.

→ Things that don't have market value excluded eg housework you do it for yourself.

• **Final goods:**

Intended for the end users.

Scanned with CamScanner

Date:

are brought under control.
then it is much easy to bring inflation under control.

→ There are several ways through which inflation is brought under control

(i) Monetary measures.
(ii) Fiscal measures.
(iii) Other measures.

→ Monetary measures:

These measures are adopted by the central bank of the country, State Bank of Pakistan in case of Pakistan to control the money supply

→ It includes increase in bank rates
→ Sale of Govt. Securities in open market.
→ And increase in Cash Reserve Ratio

→ Fiscal measures:

Fiscal measures are adopted by the govt to

Date:

Macroeconomics:

Macroeconomics deals with the study of economy at a national level means Macroeconomics deals with the economy as a whole.

Three especially important variables:

→ **Real GDP:** (Gross domestic Product)

Real GDP is an inflation adjusted measure that reflects the value of all goods and services produced by an economy in a given year.

→ **Nominal GDP:**

Nominal GDP is a macroeconomics assessment of the value of goods and services

Date:

affect the changes in purchasing power with the public, they include

→ Government expenditures

→ Taxation

→ Public Borrowing

→ Debt management

→ Over valution

→ **Inflation is increased or decreased by.**

→ Produce more currency.

→ Interest rate ↑ people will borrow less then demand is decreased vice virsa

→ Govt sells bonds to take money from the people, this is called open market operation

→ Increase or decrease reserve ratio

Scanned with CamScanner

Date:

. Goods and Services:

Includes tengible goods like Bikes, cars, and intengible (dry cleaning, Conserts etc).

. Produced:

It includes currently produced goods not goods purchased in past.

→ If a car is produced in a year and it is not sold yet, it is counted as sold to the owner.

. With in a country:

Within borders, weather done by its own citizens or by foriegners located there

. Given Period of time:

Usually a year or a quater.

Scanned with CamScanner

Date:

Long run economic growth:

Long run economic growth is defined as the sustained rise in the quantity of goods and services that an economy produces. Long run economic growth is directly impacted by the GDP.

- → Current in Pakistan is 3.2%
- → Lowest in the region.
- → 7% highest in the musharaf's era.

→ Unemployment 6% to 7% in Pakistan.

→ It seems low because in Pakistan if one is earning 100 rupees he is also called employed.

→ Disguised employment:

All brothers working in one garden are also called employed.

Date:

income accounts identity.

• Consumption :

Consumption consists of goods and services bought by household, it is divided into three sub categories i.e It does not include the Purchases of new houses.

(a) Non durable goods :

Goods that lasts only a short time such as food and clothing.

(b) Durable goods :

Goods that lasts a long time such as Cars, TV, etc.

(c) Services :

Work done for consumers by individuals and firms Such as haircut, doctor visits, School fees etc.

Scanned with CamScanner

Date:

The components of GDP:

Recall ⇒ GDP is total spending expenditure method.

Four Components:

- Consumption (C)
- Investment (I)
- Government Purchases (G)
- Net exports (NX).

Thus let y stands for GDP.

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

GDP is the Sum of them each dollar of GDP falls into one of ~~these~~ these categories. This equation is called nation

Date:

Types of inflation:

→ Cost Push inflation:

Cost push inflation is inflation caused by an increase in prices of inputs like labour, raw material etc. The increased price of the factors of Production leads to a decreased supply of these goods. (Decreased aggregate Supply)

→ Demand-Pull inflation:

Demand pull inflation results when prices rise because aggregate demand in an economy is greater than aggregate supply.

(~~Decreased aggregate~~)

Scanned with CamScanner

DATE: / /

, is a measure of the inflation. It is the ratio of the value of goods and services an economy produces in a particular year at current prices to that of the prices that prevailed during the base year.

(Deflator usually means take inflation out of).

" It is the measure of overall level of prices.

GDP deflator = $100 \times \frac{\text{Nominal GDP}}{\text{Real GDP}}$

→ Criticism by Robert Kennedy about GDP:

→ It does not includes

(i) Health.

(ii) Education.

Scanned with CamScanner

DATE: / /

(iii) Beauty of Poetry.
(iv) Marriages strength etc.
(v) Quality of Environment.
(vi) Leisure time.
(vii) Non Market activity.
(viii) Child care etc.

→ Why do we care about GDP?

→ Having large GDP enables a country to afford better Schools, cleaner environment, health care etc.

→ Many indicators of the quality of life are correlated with the GDP, examples :

(i) Life expectancy.
(ii) Literacy.
(iii) Internet usage

Scanned with CamScanner

Date:

→ Economic Growth :

Economic growth is an increase in real GDP (Goods and services) of a nation over a period of time. Which means an increase in the output of a country from one period of time to an other period of time

→ Economic Development :

Economic development refers to a progress and social well-being of a country. Which includes improved living standard of the people, Schools, Hospitals etc.

→ Two types of Tax

→ Progressive Tax :

If the rate of

Scanned with CamScanner

DATE: / /

Eg: Pakistani have a flat in America the rent is added in GDP of america but not in GNP, because it is the factor of Payment to abroad.

→ Seasonal Adjustment:

All these ~~seasonal~~ measures exhibit a seasonal putter some of these are because of the ability of Production Eg: Building a home in winter. There for most of the economic statistics are seasonal adjust, Therefor it must be considered While Comparing.

Scanned with CamScanner

DATE: / /

→ Others measures in national income accounts.

→ GNP

Gross National Product :

Gross national Product (GNP) is an estimate of total values of all the final Goods/products and services turned out in a given period by means of Production owned by a country's residents.

GNP = GDP + factor payment from abroad — factor Payment to abroad.

→ It means the total income earned by the nationals.

Date:

tax increases with the increase in the level of income, this kind of tax will be known as progressive tax. for example 5% tax for the income below 200000, 7% ~~tax~~ tax for the income b/w 2-3 lac
9% tax for the income ~~below~~ more 300000.

→ Regressive Tax :

A regressive tax is a tax applied uniformly, taking a larger percentage of income from low-income earners than from high-income earners. It is in opposition to a progressive tax.

Scanned with CamScanner

Date:

$$\text{Growth} = \frac{8250 - 6000}{6000} \times 100$$

$$\frac{2250}{6000} \times 100$$

$$\text{Growth} = 37.5$$

→ Compute Real GDP in each year using 2005 as base year, when ever we are finding Real GDP the price will be same to base year in each year, because the Real GDP is the inflation adjusted GDP.

2005 ➡ $10 \times 400 + 2 \times 1000 = 6000$ } 20%

2006 ➡ $10 \times 500 + 2 \times 1100 = 7200$

2007 ➡ $10 \times 600 + 2 \times 1200 = 8400$ } 16.7%

→ **GDP Deflator:**

The GDP deflator also called implicit price deflator

DATE: / /

zero, and the price of few oranges that remain is driven sky-high. Because oranges are no longer part of GDP, the increase in the price of Oranges does not show up in the GDP deflator, but high price do count in CPI

Scanned with CamScanner

DATE: / /

→ Does CPI Overstates Of inflation :

Few economists beleives Yes.

→ The New improved GDP :

→(i) In past the expenditure on production of Movies were treated as intermiadiate goods and the tickets sold were treated as final goods so its contribution to GDP was only the revanue of earned this year from tickets

→(ii) A popular movie is watche again and again by veiwers for many years Theref

Date:

Apple and Oranges:

They are two different items to find its contribution to GDP.

GDP = (P of Apple × Q of apple) + (P of oranges × Q of oranges)

= ($0.50 × 4) + ($1.00 × 3)

GDP = $5.00

→ Computing Nominal and Real GDP

Example:

Years	Pizza P	Pizza Q	Latte P	Latte Q
2005	10	400	2	1000
2006	11	500	2.50	1100
2007	12	600	3	1200

→ Compute Nominal GDP

2005	10 × 400 + 2 × 1000	= 6,000	} 37.5%
2006	11 × 500 + 2.5 × 1100	= 8,250	} 30.9%
2007	12 × 600 + 3 × 1200	= 10,800	

Scanned with CamScanner

DATE: / /

DIFFERENCE B/W CPI AND GDP DEFLATOR:-

CPI	GDP DEFLATOR:-
• Measures the price of only the goods and services bought by Consumer	• Measures the Price of all goods and services Produced.
• Includes the imported goods.	• Includes only those goods produced domestically
• Fixed basket of Goods	• Assigns Changing Weights

Example:-

Frosts destroys the nation's orange crop: the quantity of Oranges produced falls to

Scanned with CamScanner

DATE: / /

→ The Price of basket of Goods.

→ Most commonly used measure of the level of prices is the consumer price index.

→ CPI :

It turns the prices of fixed basket of goods (neccessary item including imported items into a single index.

Ex :

CPI = (5 × CP of apples) + (2 × CP of oranges)

(5 × 2009 "P" of "a") + (2 × 2009 "P" of oranges)

Base year 2009.

→ There is one more which is called PPI.