Principle of Macroeconomics

1) Explain difference between Absolute advantage and comparative advantage.

Absolute Advantage	Comparative Advantage
The ability to produce a good using few inputs than another producers	The ability to produce a good at a lower opportunity cost than another producer
The comparsion among produced of a good according to their productivity	Compares producer of a good according to their opportunity cost

2)

	Hours to make		Amount produced in 1 hr	
	Beer	Pizza	Beer	Pizza
Pat	4 hr	2 hr	1/4 = 0.25	1/2 = 0.5
Kris	6 hr	4 hr	1/6 = 0.167	1/4 = 0.25

a) Opportunity Cost

	1 Gallon Beer	1 pizza
Pat	0.5/0.25 = 2 pizzas	0.25/0.5 = 0.5 gallon
Kris	0.25/0.167 = 1.5 pizzas	0.167/0.25 = 0.67 beer

Pat has absolute cost advantage in making pizza as he can make 1 pizza in only 2 hour while Kris needs 4 hours

Pat has a comparative advantage in making pizza because he has lower opportunity cost of making pizza than Kris

b) Pat will trade away pizza in exchange for root beer because he has a comparative advantage in making pizzas

c) The highest price of pizza would be 2/3 = 0.67 gallons of root beer. If the price is higher than that Kris will prefer to make his own pizza.
The lowest price of pizza would be 1/2 = 0.5 gallons of root beer. If the price is lower than that then Pat will prefer to make his own root beer since O/C of making gallon of root beer would be lower than trade price.

3)

Year	Price of Milk	Quantity of Milk	Price of Honey	Quantity of Honey
2010	$1	100 quarts	$2	50 quarts
2011	$1	200	$2	100
2012	$2	200	$4	100

a) Calculating Nominal GDP

2010:- ($1 per qt. of milk x 100 quart) + ($2 per qt. of honey x 50 quart) = $200

2011: ($1 x 200) + ($2 x 100) = $400

2012: ($2 x 200) + ($4 x 100) = $800

Calculate Real GDP (base year 2010)

2010: ($1 x 100) + ($2 x 50) = $200

2011: ($1 x 200) + ($2 x 100) = $400

2012: ($1 x 200) + ($2 x 100) = $400

GDP Deflector

2010: ($200 / $200) x 100 = 100

2011: ($400 / $400) x 100 = 100

2012: ($800 / $400) x 100 = 200

b) % change in N. GDP in 2011 =

[(400 - 200)/200] x 100% = 100%

% change in N. GDP in 2012 =

[(800 - 400)/400] x 100% = 100%

% change in Real GDP

2011: [(400 - 200)/200] x 100% = 100%

2012: [(400 - 400)/400] x 100% = 0%

'1. change in GDP deflector

2011 : [(100 - 100) / 100] × 100 = 0'!

2012 : [(200 - 100) / 100] × 100 = 100'!

Economic rise more in 2011 because in 2011 real gdp is 100'!. where as 0'!. in 2012

4) Explain nominal and real interest rate and relation.

Nominal Interest Rate - The interest rate as usually reported without a correction for the effects of inflation.

Real Interest Rate - The interest rate as corrected for the effects of inflation.

Real Interest Rate = Nominal Interest rate - Inflation rate

5)

	Tennis Ball		Golf ball		Bottles of Gatorade	
	Price	Quantity	Price	Quantity	Price	Quantity
2011	$2	100	$4	100	$1	200
2012	$2	100	$6	100	$2	200

'!. change in price

Tennis ball : (2 - 2)/2) × 100 = 0'!.

Golf ball : ((6 - 4)/4) × 100 = 50'!.

Bottle of Gatorade : ((2 - 1)/1) × 100 = 100'!.

b) Cost of market basket in year 2011
$= (2 \times 100) + (4 \times 100) + (1 \times 200) = \$800$

Cost of market basket in year 2012
$= (2 \times 100) + (6 \times 100) + (2 \times 200) = \$1200$

% change in cost of market basket from 2011 to 2012
$= [(1200 - 800)/800] \times 100 = 50\%$

Gyanaranjan Sahoo
19410121030
CSE - D