Macro-economics

- GDP = measure of an economy – the total market values of all final g/s produced by firms in an economy in a given period of time
  - Market value: sold in market (does not include home produced goods)
    - Public g/s = cost of provisions, although they don't have market prices
  - Final goods & services – end of production processes
  - Produced in a country during a given period: produced within borders of country, in that particular period
    - Inventories cant enter into next yr's GDP (beginning inv – end inv= included investment component)
- Real GDP Total spending = aggregate = total demand
- Measuring GDP
  - Sum of value added: revenue – cost of input = value
  - Income approach – sum of all incomes received
    - National income – total income generated from sales of g/s [labour income - wages/salaries, capital income - rent, profit, net interest]
  - Expenditure approach – sum of all final expenditures, investment, government spending & net exports
    - Aggregate expenditure= C +I +G + (X – M)
    - AE = C + I + G1 + G2 + (X – M)
  - Average of the sum of Output, Expenditure, Income
- Recession: two consecutive quarters of negative growth
  - Money GDP = face value, changes in price or output
  - Real GDP = takes into account of inflation, changes in output only
  - Real GCP per capita = takes into account both inflation and population changes
- Chain weighted GDP calculations – use weights (due to technological advances, price changes)
  - Weight – importance of production value
- GDP Is quantitative measure – only measures quantity and not quality
- Doesn't take into account of:

- Total quality of life
- Cash economy: “black market”
- Home produced, home consumed g/s (education, medical services)
- Income distribution
- Improvement of quality of goods and services (LCD/plasma TVs)
- Overseas trading relationship
- Working conditions

- $\text{G.D.P} \times \frac{\text{base year}}{\text{C.P.I}} = \text{real G.D.P}$
- $\frac{\text{Real G.D.P}}{\text{Population}} = \text{real G.D.P per capita}$
- CPI = consumer price index, measures changes in price
- $\frac{\text{Current year's G.D.P} - \text{previous year's G.D.P}}{\text{Previous year's G.D.P}} \times 100 = \text{economic growth rate}$
- Long run economic growth – process by which rising productivity increases avg standard of living
    - Determined by labour productivity & technological change
        - Increases in capital (physical, manufacture & human, knowledge) per hr worked
        - Increase ability of firm to produce given level of output with given quantity inputs
        - Concern about sustainability of growth for future generations
- Factors affecting economic growth
    - Occur in 2 ways
        - Increase in real GDP
        - Increase in real GDP per capita
        - Productivity – producing goods and services with least amount of resources

<u>Inflation</u>

- A persistent and appreciable rise in the general level of prices of g/s purchased by metropolitan households
- Applied to price increase in a period of time in a range of goods
- Affected by fast growth of economic growth
- measured by CPI – consumer price index, summaries the overall changes in prices of a large number of g/s
    - Household expenditure Survey – determines basket of g/s that represents the typical consumption of Australian family
- Does not reflect price movements outside metropolitan areas
- Not regarded as true cost of living index, does not reflect consumer preferences
- Not accounted for changes in quality of goods
- Index must have a based year (100), regimen (group)
    - Health
    - Food
    - Household equipment
    - Clothing
    - Transport
    - Alcohol
    - Recreation
    - Housing
    - Education
    - Communication
    - Financial & insurance services
- Regiment - based on sample 'basket' of g/s
- Are weighted according to how frequently its purchased
- Rate of inflation (rate of price changes) – calculated from rate of changes in CPI
- Weight x Price = expenditure
- <u>current year price</u> x 100 = CPI

base year price

- Headline inflation – CPI for a particular period
    - raw inflation figure
    - tends to get the most attention in the media
    - Included volatile CPI components, misleading the underlying inflation rate
    - E.g.: prices of fruit and vegetables, petrol
- Underlying inflation rate – “one off” factors is excluded (droughts, cyclones)
    - takes the headline inflation rate and excludes certain volatile items
    - More accurate way to measure rate of inflation
    - Excludes items that were affected by natural disasters or government taxation
- Inaccuracy of CPI;
    - Substitution bias – basket of g/s is fixed, higher prices in one good leads substitution for a cheaper good (given consumers are indifferent to the two products)
    - Quality adjustment bias – overstated inflation as quality improvements over time are difficult to adjust for