

Economics 402

Homework #1

Due on Thursday 1/31

This assignment is based on material from Chapters 1-3 in the Mankiw textbook. However, you will also need to do some additional research to fully answer the questions. Above all, you will need to do some contemplation on your own about the questions. These are not easy questions and there are many ways to answer them. Give the best answer you can. Please type your answers.

1. Measuring Economic Activity (20 points)

To what extent does real GDP per capita provide an accurate measure of the standard of living? Is it more useful for comparing standards of living across time or across countries? To what extent does it correlate with measures of happiness and measures of political freedom? (Cite your sources. Wikipedia is not sufficient. Try to find credible academic sources.) In what way is it possible for the estimation of real GDP to *contribute* to the standard of living, not just measure it? Keep your answers to less than a page.

2. Shares (20 points)

For this question, examine the changes over time in the relative importance of consumption, investment, government, and net exports as shares of total expenditures. You will need data from the BEA website.

Go to the BEA website. Click on “Gross Domestic Product”, which is below the heading “National”. Click on “Interactive NIPA tables”. Click on “List of All NIPA Tables”. Click on the link for Table 1.1.5 Gross Domestic Product. Using the buttons near the top, select Annual instead of Quarterly and select the starting year of 1929. Then click the “Refresh Table” button. Create a table that has the percentage share of the four components of expenditures (consumption (row 2), investment (row 6), government (row 20) and net exports (row 13)) out of the total GDP (row 1) for the following years 1929, 1935, 1945, 1955, 1965, 1975, 1985, 1995, 2005. E.g., for 1929, consumption is \$77.4 billion and total GDP is \$103.6 billion. Thus, consumption’s share is 75% ($=100\% \times 77.4/103.6$). (***)Alternatively, if you are more adept at using spreadsheets, you can download Section 1 as an .xls file and plot the shares for all years from 1929-2006. Please put the years on the x-axis.)

Based on the results in your table, what can you say about how much the shares of the expenditure components change over time? Can you explain the reason for any of the larger changes? Keep your answers brief.

Second, examine changes over time in the relative importance of goods, services, and structures in total production. To do so, follow the same steps as above, but click on the link for Table 1.2.5 Gross Domestic Product by Major Type of Product instead of Table 1.1.5. (Again, you can plot the shares instead of generating a table if you are more adept at using spreadsheets.)

As before, briefly discuss how the shares change over time and what might be responsible for these changes.

Third, examine changes over time in the relative shares of different components of aggregate income in total income. To do so, follow the same steps as above, but click on the link for Table 1.12 National Income by Type of Income. In this case, only consider the shares of Compensation of Employees (row 2) (i.e., workers' share) and Corporate Profits (row 13) (i.e., capitalists' share).

As before, briefly discuss how the shares change over time and what might be responsible for these changes. Are you surprised by any of the changes (or lack of changes) in the shares? Explain.

3. *Adbusters (10 points)*

“...A man falls sick due to industrial pollution: the GDP rises... It may seem crazy to count ourselves better off the more people fall sick, but at the moment economics is crazy...” –Adbusters 2004

Why is this statement incorrect (the part about someone being sick causing GDP to rise, not the part about economics being crazy)? (Hint: think about the fallacy of composition.) Keep your answer to less than half a page.