

Non specific topics

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GDP National Income Accounting Question Discuss what is, and what is not, included in calculating GDP. The Gross Domestic Product(GDP) is a measure of the total income in the economy. The GDP of a specific country is the market value, in total, of all products in a given fiscal year, usually a year. The expenditure method is the most common approach to calculate the GDP. GDP, using this approach is equal to Investments + Consumption + (Exports - Imports) + Government spending. So,

$$\text{GDP} = C + I + G + (X - M)$$

The term gross means capital stock depreciation is not included. In the equation, export minus imports is attained by the cumulative exports being adjusted by the subtraction of the expenditure that is not domestic. Then all the exports in the domestic area are added.

Question 2: Why does investment spending not equal saving in the circular flow?

It is a fact that income equals to spending or savings is equal to investments. This, however, does not imply that at all times there is enough spending such that all of the economies' resources are fully employed. Even in fulltime employment, where employment is the investment spending there is still more room for extra investments in the economy.

Question 3: Why do total leakages and total injections have to be equal?

In an injections-leakage model, on one side there are injections. These injections will include non-consumption expenditures on an aggregate production. Investment, expenditures, exports, and government purchases are the three injections. They are known as injections since they are inputted/ 'injected' to the circular flow of production, consumption, and

income (Bade, & Michael, 2002). The other half of the model is the leakages. They are non-consumption uses coming from income production generates'. The leakages are imports, savings, and taxes. They are taken out of the circular flow hence the term leakages. Equilibrium in this model will be dependent on the balance existing between injections towards the core of the circular flow and leakages. If they are equal, the core circular flow's volume will not change. When this two are equal, equilibrium exists.

Question 4: Discuss the limitations of national income accounting.

In the measuring of national income, there is a need to understand some limitations that will come with it. National income accounting will not measure the social welfare but the domestic economic performance. However, there is need for there to be a strong relationship between the two. National income measure will understate transactions in social welfare- non - market. In national income measures, there is no accounting of changes in the quality of product and increase in variables like work satisfaction (McEachern, 2012). It has also been suggested that per capita income is a superior measure of standards of living compared to the total national income

Question 5: Why does the consumer price index exaggerate the inflation rate?

In calculating the inflation rate, a number of reasons make the Consumer Price Index (CPI) exaggerate the inflation rate. The index, originates from the Bureau of Labor Statistics (BLS). BLS does not incorporate the products that are new in its sample as fast as it should have. Additionally, the index does not do enough adjustments for substitutions. For example if the price of beef

goes up, the population will probably switch to chicken. This, however, will not be reflected by the CPI. This is because it retains the base year's spending patterns. However, substitution may at times be made grudgingly hence retaining a fixed basket may be an intuitive point. The bureau of labor statistics under-adjust when it comes to quality improvements. These improvements are in concept similar to price decrease.

References

Bade, R. & Michael, P. (2002). Foundations of Microeconomics Boston, MA: Addison-Wesley

McEachern, W. A. (2012). ECON Macro 3 (3rd ed.). Mason, OH: South-Western