

LECTURE 11: GDP II

- I. What are the biggest economies?
 - a. *GDP per capita* is GDP divided by the number of people in the economy (“per capita” is Latin for “for each head”)
 - i. This is useful to determine how wealthy an average person is in a country, or the average income.
 - ii. For example, the U.S.’s GDP per capita is about \$50,000 while Mexico is about \$16,000;¹ this gives a good idea why so many people in Mexico wish to come to the U.S.
- II. Two equations
 - a. There are two ways to break down GDP to help us understand what it includes.
 - b. The first is the *spending* approach. What did people spend their money on?

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

- i. Where Y is GDP;
 - ii. C is consumption (like when you buy an ice cream bar);
 - iii. I is investment (like when you buy an ice cream maker);
 - iv. G is government spending (like when the government buys you ice cream);
 - v. NX is exports – imports: exporting ice cream increases GDP and importing ice cream decreases it (because it wasn’t produced in the U.S.).
- c. Another way to think about GDP is the *income* approach. How did people get their money?

$$Y = wages + rent + interest + profit$$

- i. Where Y is still GDP;
- ii. Wages are all the salaries of everyone in a country;
- iii. Rent includes all the money people get from physical assets;

¹ 2012 data, from CIA World Fact Book. These data are adjusted for purchasing power (i.e. the price level in a country). Without adjusting for purchasing power, Mexico is closer to \$10,000 per person. The United States is about the same: \$49,000.

- iv. Interest is everyone's income from keeping money in a bank;
- v. Profit is the money business owners keep after they receive revenue and pay their costs.