David Youngberg
ECON 201—Montgomery College

LECTURE 20: 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.