

ECON 202  
INTERMEDIATE MACROECONOMICS  
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19 February 2007

**Key to Exercise 01**  
**Some Concepts and the Measurement**

1. (Abel and Bernanke, 2005) Here are some macroeconomic data for the country of PotatoeLand for the years 2002 and 2003:

	2002	2003
Output	<b>12,000 tons of potatoes</b>	<b>14,300 tons of potatoes</b>
Employment	<b>1,000 workers</b>	<b>1,100 workers</b>
Unemployed	<b>100 workers</b>	<b>50 workers</b>
Total Labor force	<b>1,100 workers</b>	<b>1,150 workers</b>
Prices	<b>2 dollars per ton</b>	<b>2.5 dollars per ton</b>

As the data suggest, PotatoeLand produces only potatoes, and its monetary units is the dollars. Calculate each of the following macroeconomic variables, being sure to give units.

a. Average labor productivity in 2002 and 2003.

12, 13

b. The growth rate of average labor productivity between 2002 and 2003.

8.33%

c. The unemployment rate in 2002 and 2003.

9%, 4.3%

d. The inflation rate between 2002 and 2003.

25%

2. (Williamson, 2005) Consider the following data on real GDP per capita in the United States:

Year	Real GDP per capita (1996 Dollars)
1950	<b>11,205</b>
1960	<b>13,339</b>
1970	<b>17,718</b>
1980	<b>21,904</b>
1990	<b>27,100</b>
1995	<b>28,747</b>
1996	<b>29,520</b>
1997	<b>30,519</b>
1998	<b>31,478</b>
1999	<b>32,238</b>
2000	<b>32,748</b>
2001	<b>32,375</b>
2002	<b>32,713</b>

a. Calculate the percentage growth rates in real GDP per capita in each of the years 1996 through 2002, from the previous year.

Year	Real GDP per capita (1996 Dollars)	
1996	29,520	
1997	30,519	3.4%
1998	31,478	3.1%
1999	32,238	2.4%
2000	32,748	1.6%
2001	32,375	-1.1%
2002	32,713	1.0%

b. Now, instead of calculating the annual percentage growth rates in the years 1996 through 2002 directly, use as an approximation  $100x(\ln y_t - \ln y_{t-1})$ , where  $y_t$  is real per capita GDP in year  $t$ . How close does this approximation come to the actual growth rates you calculated in part (a)?

Year	Real GDP per capita (1996 Dollars)	Ln(y)	
1996	29,520	10.29	
1997	30,519	10.32	3.3%
1998	31,478	10.35	3.1%
1999	32,238	10.38	2.4%
2000	32,748	10.39	1.6%
2001	32,375	10.38	-1.1%
2002	32,713	10.39	1.0%

c. Repeat parts (a) and (b) for 1950, 1960, 1970, 1980, 1990, and 2000. In this case, how large an error do you make by approximating the growth rate by the change in natural log?

Year	Real GDP per capita (1996 Dollars)	% Growth	Ln(y)	% Growth
1950	11,205		9.32	
1960	13,339	19.0%	9.49	17.4%
1970	17,718	32.8%	9.78	28.4%
1980	21,904	23.6%	9.99	21.2%
1990	27,100	23.7%	10.20	21.3%
2000	32,748	20.8%	10.39	18.9%

The accuracy of the approximation declines.

3. (Adapted from sources on the Internet) A farmer grows a bushel of wheat and sells it to a miller for \$1. The miller turns it into flour and then sells the flour to a baker for \$3. The baker uses the flour to bake bread and sells it to an engineer for \$6. The engineer eats the bread. How does this contribute to GDP? What is the value added by each person?

Farmer	Miller	Baker	Engineer
\$1	\$2	\$3	= \$6

4. (Adapted from MIT Open University) There are an orange farm and an orange juice company in a country called Orangeland. Orangelanders live only on orange juice. In 1992, the orange farm produced 10 oranges, and sold them to the orange juice company at \$1 each. The orange juice company produced 3 bottles of orange juice, and sold them all at a unit price of \$10 plus 10% indirect tax collected by government (so the price paid was actually \$11). The orange farm paid total wages of \$6. The orange juice company paid total wages of \$10. The orange juice company also had to pay \$4 to replace the orange juice extractor that was not working properly due to its use during 1992 (depreciation). Both companies retained 50% of their profits and paid the rest of it as dividends to the households. After receiving their wage income and their dividends, the households paid a 10% direct tax on their total income to the government. The government bought one orange juice bottle. (Notice that the firms are not paying any direct taxes on their retained profits)

Answer the following questions.

a. Compute the GDP of Orangeland using the value added, expenditure, and income approaches.

Approach

Value added	$10+23 = \$33$
Expenditure	$11+22 = \$33$
Income	$16+4+6+3+4 = \$33$

b. What is NDP? What is National Income?

$$\text{NNP} = \text{GDP} - \text{Depreciation} = 33 - 4 = 29$$
$$\text{NI} = \text{NNP} - \text{Indirect Taxes} = 29 - 3 = 26$$

c. What is the total income of the government?

$$\text{Government Income} = 3 + 2.1 = 5.1$$

d. What is the disposable income?

$$\text{YD} = 26 - 2.1 = 23.9$$

Alternatively,

$$5 + 6 + 10 = 21$$

e. What is government budget deficit (or surplus)?

$$\text{Government Deficit} = 11 - 5.1 = 5.9$$

5. If nominal GDP is 8,820 and the GDP deflator is 105, then real GDP is a) 9,261; b) 8,925; c) 8,715; d) 8,400; e) 8,000.

d) 8,400

6. Assume that GDP=4,800; C=3,400; Private Domestic Savings=400; G=1,200; and NX=-120. What are disposable income, private domestic investment, and the budget deficit?

Step 1:  $Y=C+I+G+NX \rightarrow I=320$  (Private Investment)

Step 2:  $S=I+NX \rightarrow S=200$  (Total saving)

Step 3:  $S=S_{\text{public}}+S_{\text{private}} \rightarrow S_{\text{public}}=-200$  (public saving)

Step 4:  $S_{\text{public}}=\text{Tax Revenue}-G \rightarrow \text{TA}=1000$  (Tax revenue)

Step 5:  $YD=Y-\text{TA} \rightarrow YD=3800$  (Disposable income)

7. Assume that only three goods are produced in a hypothetical economy. The following table gives Output (Q) and Price (P) information concerning goods X, Y, and Z. Find out the real GDP growth in 1995 prices from 1995 to 2000 and 2000 to 2005.

	1995		2000		2005	
Good	Q	$Q_{95} * P_{95}$	Q	$Q_{00} * P_{95}$	Q	$Q_{05} * P_{95}$
X	1	\$1	2	\$2	2	\$2
Y	2	\$4	1	\$2	2	\$2
Z	3	\$1.5	6	\$3	4	\$2
GDP		\$6.5		\$7		\$6

Growth rate from 1995 to 2000 is 7.7% and growth rate from 2000 to 2005 is -14.3%.