

4 Measuring the economy – Part 1

Name: _____ Class: _____ Date: _____

Vocabulary

Write each word three times.

English

Write it 3 times (English)

macroeconomics

Gross domestic
product
real

nominal

per capita

standard of living

circular flow of in-
come

Households

firms

leakages

injections

Aggregate demand

consumption

investment

Aggregate supply

price level

Recall

So far you studied single markets. Bring this with you:

- One market has its own demand, supply and price.
- A whole country has **many** markets at once.

At AS, **macroeconomics** looks at the **whole** economy together – its total output, jobs and prices.

New ideas

■ 1 Measuring the economy

Gross domestic product (GDP) is the value of all goods and services made **inside** a country in a year. Two cautions:

- **real** GDP removes the effect of rising prices, so it shows the true change in output; **nominal** GDP does not. Always compare **real** values;
- **per capita** GDP divides by the population, giving the average **per person** – better for the **standard of living**.

Micro-check. Why should you compare **real** GDP, not nominal? [1]

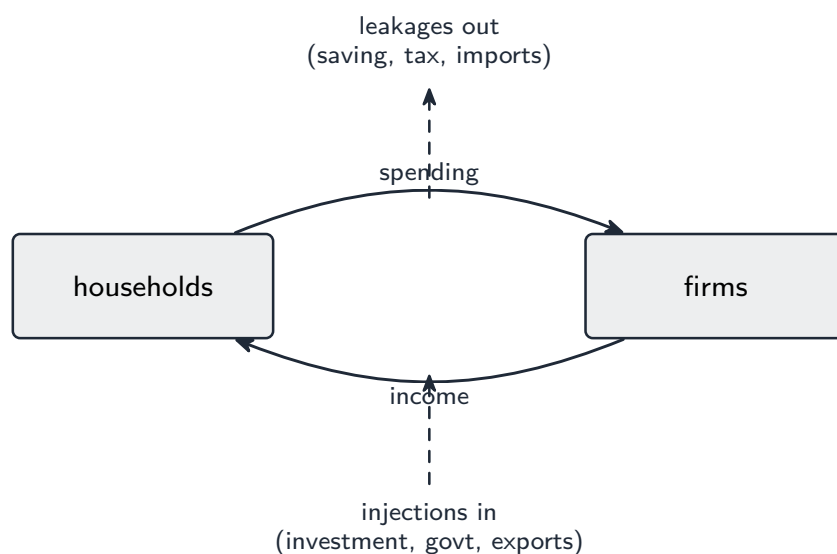
■ 2 The circular flow of income

The **circular flow of income** shows money moving round the economy.

Households supply factors of production to **firms** and get income; they spend it, and the money flows back to firms.

Money also leaves and enters the flow:

- **leakages** take money **out**: saving, taxation, and spending on imports;
- **injections** put money **in**: investment, government spending, and exports.



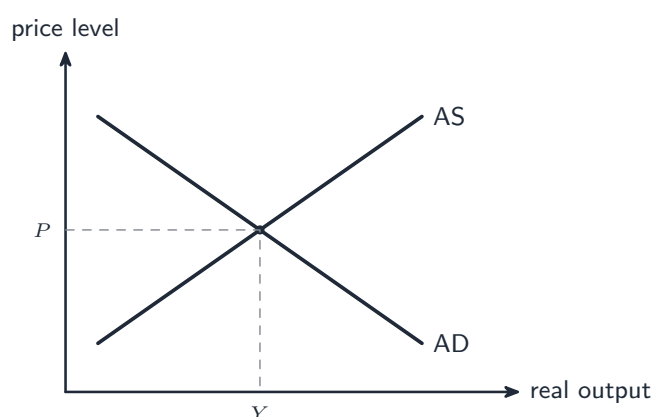
Micro-check. Is **saving** a leakage or an injection?

[1]

■ 3 Aggregate demand and supply

Aggregate demand (AD) is total spending in the economy: $AD = C + I + G + (X - M)$ – **consumption**, **investment**, government spending, and net exports. The AD curve slopes down.

Aggregate supply (AS) is total output firms will make. The economy settles where AD crosses AS, setting the **price level** and real output.



Micro-check. State the four parts of aggregate demand (AD).

[1]

Watch out: compare *real* GDP (it removes inflation), and *per-capita* GDP for living

standards. Leakages (saving, tax, imports) take money *out*; injections (investment, government spending, exports) put it *in*. $AD = C + I + G + (X - M)$.

Practice

4.1 State what **GDP** measures. [1]

4.2 Explain the difference between **real** and **nominal** GDP. [2]

4.3 State whether each is a **leakage** or an **injection**: (a) taxation, (b) investment, (c) exports. [3]

4.4 Write out the four parts of **aggregate demand**. [2]

4.5 State what AD and AS together set when they cross. [1]

4.6 Challenge. A country's nominal GDP rose by 8% but inflation was 6%. Roughly what was the real growth, and why does the difference matter? [2]
