

2.2 Limitations of GDP

Name: _____ Class: _____ Date: _____

Total: 10 marks

KEY WORDS gdp per capita 人均 • underground economy 地下经济 • externalities 外部性
• nonmarket transactions 非市场交易 • nominal gdp 名义

Objective

Build the skills to answer exam questions on **the limitations of GDP**.

You must be able to:

- explain why GDP omits **nonmarket transactions** 非市场交易
- describe how the **underground economy** 地下经济 causes GDP to understate output
- explain why GDP ignores **externalities** 外部性, resource depletion, and income distribution
- explain why **GDP per capita** 人均 GDP is better for comparing living standards

1 Worked examples

Study these first. Each one shows the method for a question type used later.

■ What GDP leaves out

- **Nonmarket** work: housework, volunteering, DIY.
- The **underground economy**: unreported and illegal activity (so GDP understates output).
- **Externalities** and resource depletion: pollution and using up nature are ignored.
- **Leisure** and the **distribution** of income: two countries with equal GDP can differ hugely in well-being.

■ GDP per capita

Dividing by population gives **GDP per capita**, a far better guide to average living standards than total GDP.

2 Practice

2.1 State two things that GDP fails to measure. [2]

2.2 State why GDP per capita is better than total GDP for comparing living standards. [1]

2.3 Explain why the underground economy causes GDP to understate output. [2]

3 Exam-style questions

3.1 GDP does **not** include [1]

- **A** restaurant meals
- **B** unpaid housework
- **C** newly built houses
- **D** exports

3.2 To compare living standards across countries, economists prefer [1]

- **A** total GDP
- **B** GDP per capita
- **C** nominal GDP
- **D** the CPI

3.3 A country has a high GDP but severe pollution and very unequal incomes.

(a) State two limitations of GDP that this illustrates. [2]

(b) Name a per-person measure that better reflects average living standards. [1]

Solutions

2.1 any two of: nonmarket production, the underground economy, externalities/pollution, leisure, income distribution.

2.2 it adjusts for population, so it reflects output **per person** rather than the size of the country.

2.3 its activity is unreported, so that output is missing from the official GDP figure.

3.1 B.

3.2 B.

3.3 (a) it ignores externalities/pollution and the distribution of income. (b) GDP per capita.