

**Due: Wednesday, January 30 In Class**

1. Identify and explain one characteristic of microeconomic markets that cannot be understood by looking at individual markets alone, and, therefore, suggests the need for macroeconomic analysis.
2. Which of the following activities have a direct effect on GDP? How much does each activity change GDP? Give a brief explanation for your answer in each case (a few words will do.)
  - a) Smith pays a carpenter \$8,000 to build a garage.
  - b) Smith purchases \$2,000 worth of materials and builds a garage herself, which adds \$8,000 to the value of her house.
  - c) Smith goes to the woods, cuts down trees, and builds a garage from logs that is worth \$8,000.
  - d) The Jones family sells its old house to the Reynolds family for \$125,000. The Joneses then buy a newly constructed house for \$180,000
  - e) Ms. Wang sells 100 shares of Microsoft common stock at a profit of \$10 per share.
  - f) Due to a price increase, Honda's sales rise by \$10 million on cars produced in Ohio.
  - g) Your grandmother wins \$10,000 in the Illinois state lottery.
  - h) Your grandmother uses her \$10,000 lottery winnings to finance a trip around the U.S.
  - i) The government pays out \$30 billion more in social security benefits as the result of a law change.
  - j) A change in government regulations forces firms to spend \$20 billion more on pollution control equipment.
3. Jane Justice, attorney at law, represents Joe Doe, who is suing his former employer for negligence because of an injury he sustained while on the job. Joe wins the case, is awarded \$3 million, and pays Jane his 1/3 share. Did this legal action bring about an increase in GDP and if so, how big was the increase? Why?
4. Explain three potential problems with using real GDP figures to measure national economic welfare.
5. In the past several decades, Japanese auto companies, like Toyota, have been producing cars in the U.S., just like traditional U.S. auto companies, such as Ford.
  - a) Suppose Toyota produces a car in the U.S., sells it in the same year to an American household for \$20,000, and earns a profit of \$3,000. The car contains parts worth \$10,000 imported from Japan. How much will GDP change due to these activities alone? Which components of GDP (C, I, G, Ex, and Im) change and by how much?
  - b) How would the effect on GDP and its components (from part a) be different if Ford produced a truck sold to an American household for \$20,000, made a profit of \$1,000, and used \$10,000 in parts imported from Canada?
  - c) Assume that Toyota is owned entirely by Japanese citizens and Ford is owned entirely by American citizens. Explain the difference between the effect of the activities described in parts a) and b) on U.S. national income.