

MORE INFO ABOUT PRIVATE INVESTMENT IN GDP

Question #4 asks what are the three main categories under **Gross Private domestic investment (I)**. The answer is not immediately obvious, so here is some additional explanation that might be helpful.

Please note that in the table, indented items are **subcategories**.

- There are two main indented items under *Gross private domestic investment*:
 - *Fixed investment* and *Change in private inventories*.
- Under *Fixed investment* there are two main indented categories:
 - *Nonresidential* and *Residential*.

Nonresidential Fixed investment is investment by businesses. This indicates how much businesses are spending on new or replacement capital equipment. It is a very important number, since it directly affects economic growth.

Residential Fixed investment is new housing. Housing is not normally included in GDP unless it represents new construction. That is, new housing is counted in GDP because it represents *current year* output. There is no particular reason to put new housing under Investment, but it is included here by convention. However, it is clear that money spent on new housing is qualitatively different from money spent on new capital equipment. If we are interested in trying to predict future economic growth, we are most interested in knowing how much businesses are spending on capital.

Changes in inventories: This figure represents finished, but unsold goods. If businesses are adding to inventories, this figure will increase. But, this is not a good sign, because it means that fewer goods are being sold than businesses expected. This could mean that businesses are concluding they have produced too much and will cut back -- produce fewer goods and possibly lay off workers.

Most of this is explained in your book, but sometimes it's hard to match up economic concepts with actual government data terminology. If you still have questions, please let me know.

Just to be really clear -- the answer to Question #4 on the GDP homework is:

- **Nonresidential fixed investment,**
- **Residential fixed investment,**
- **Changes in inventories.**

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