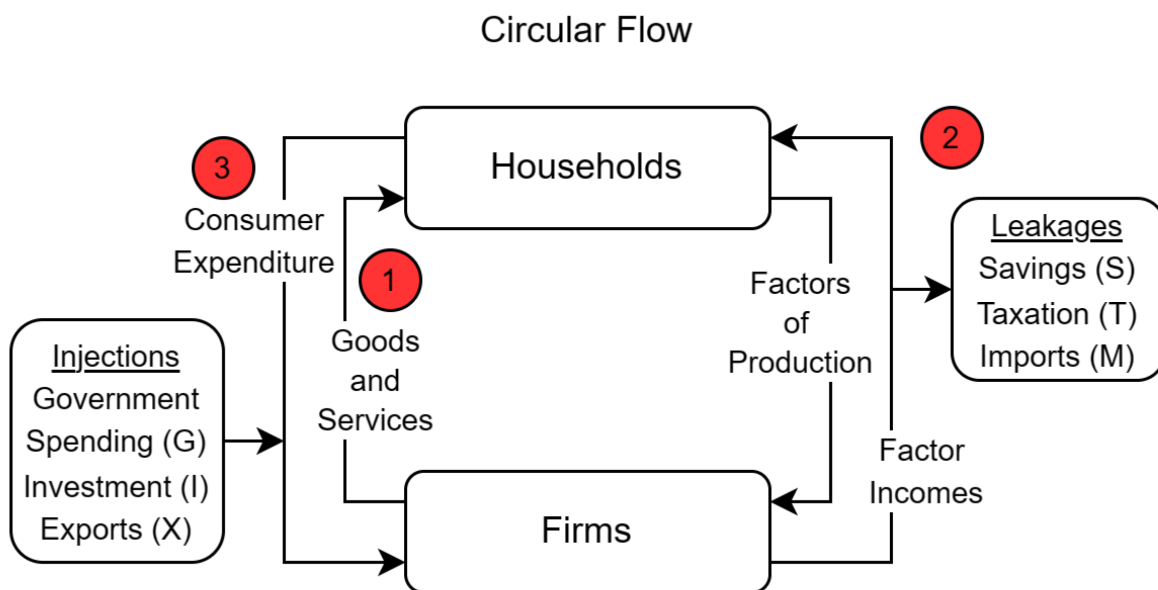
2.1.1 Economic Growth

GDP Overview

- Economic growth (actual growth) is an increase in the real value of goods and services produced in a country as measured by the annual percentage change in real national output
- Potential economic growth is an increase in the productive potential, shown by a shift in PPF
- Economic growth is a long-run increase in a country's productive capacity
- Real (nominal value accounted for inflation, used to measure changes over time) GDP is a measure of economic growth
- GDP is the total value of goods produced and services provided in a country in a given time period (output method) OR the

total expenditure on goods and services (expenditure method) OR the total income earnt in an economy (income method)



I+G+X > S+T+M Econ Growth is increasing
I+G+X < S+T+M Econ Growth is decreasing
I+G+X = S+T+M Macroeconomic Equilibrium
Outcome = Income = Expenditure

1. Output Method - Final Value of all G+S produced in an economy year
2. Income Method - All factor incomes (wages, profit, interest, rent) earnt in an economy in a year
3. Expenditure Method - C+I+G+(X-M)

- A recession is two consecutive quarters of economic growth, often leading to unemployment and a fall in living standards

GDP Real/Nominal, Value/Volume, Total/Per

Capita

- GDP per capita is GDP divided by population, used to measure living standards
- A falling but positive rate of growth indicates that real output is rising at a slower rate. Negative percentage rate of growth indicates decline
- Volume of output - number of g+s produced/provided
- Value of output - amount multiplies by price sold at
- Increase in volume does not mean an increase in value such as if prices are falling

GNI

- Gross National Income is a measure of domestic income (GDP) and net incomes from overseas

- GNI = GDP + (profits from companies operating overseas AND remittances from nationals in foreign countries) - (profits from foreign companies in the UK AND income earned by foreigners being sent abroad)

PPP's

- Purchasing power parities are used as a method of comparison of GDP between different countries
- PPP takes into account the price of a 'basket of goods', which takes into account purchasing power
- PPP exchange rate equalises purchasing power of different currencies

Comparison of Rates of Growth between Countries and Over Time

- GDP is used as a measure of standard of living which is income and quality of life (health, housing, environment, safety)

Limitations of GDP in Comparison of Living Standards between Countries and Over Time

- Differences in population (use per capita instead)
- Differences in inflation (use real GDP)
- Reliability of data
- Government spending (e.g. warfare or health)
- Income distribution
- Exchange rates
- GDP doesn't take into account self-consumed (e.g. homegrown vegetables) output other non market transactions (e.g. illegal drug sales)

- Doesn't take into account externalities such as pollution
- Doesn't take into account whether growth is sustainable or depreciation of capital

National Happiness

- Some countries may try to measure national happiness as a measure of living standards due to GDP limitations
- UK government performs personal wellbeing surveys to assess estimates of overall life satisfaction
- These surveys measure (subjectively) emotions and the extent to which people feel what they do is worthwhile
- There is a positive correlation between income and happiness to a certain income level
- Easterlin paradox - beyond a certain income level, marginal hapiness gains are

minimal

- Government needs to focus on other policies such as clean environment and income equality to improve standards of living rather than focusing purely on economic growth