Economic Growth

Economic growth = an increase in National Income

From unit 2.1 you will remember that government uses national income statistics to measure economic growth. The most commonly used measure is GDP, but there are others do you remember the difference?

NOTE: *Real GDP is often referred as Real National Income on the exam!!*

Link to prior learning: If the price of goods and services rise (inflation), then this will overstate the value of GDP. That is GDP will rise, even if there hasn't actually been an increase in economic activity.

Real GDP (real national income) = nominal GDP adjusted for inflation.

Economic growth occurs when the monetary value of total income or output of a country increases, after accounting for inflation

Macroeconomic Goals

Economic growth in the national output

Growth will:

- boost firms’ revenues and profits
- boost output, incomes, jobs and living standards
- boost investments by firms in new capital and businesses
- increase tax revenues for government to finance its spending

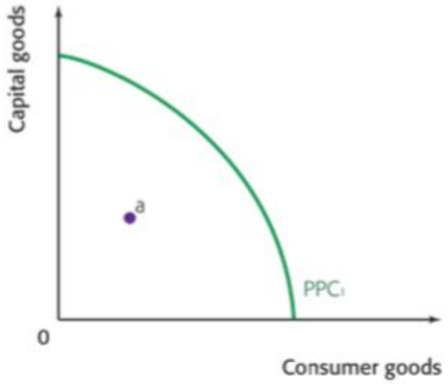
Short-term Economic Growth

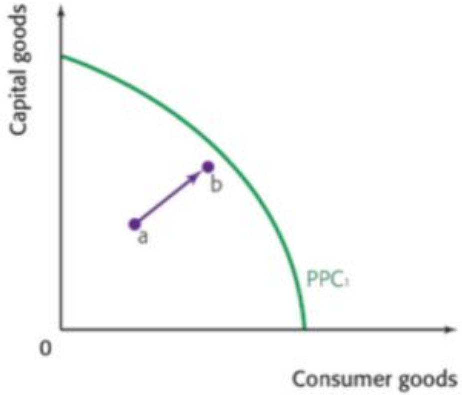
Point (a) represents actual growth and any point on the PPC would represent potential growth. At point (a) the factors of production in the economy are underemployed.

This economy does not have the factors of production to go beyond the PPC

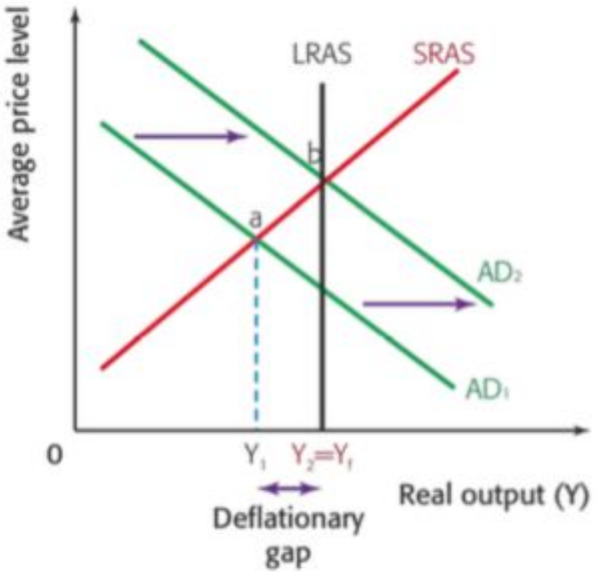
The movement of (a) to (b) shows us that actual growth has increased.

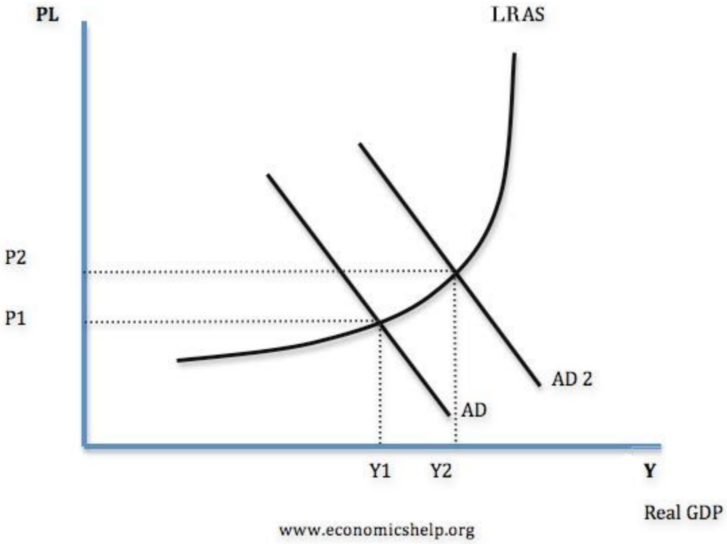
Why might this be the case?





Short-term economic growth can also be diagrammed as….





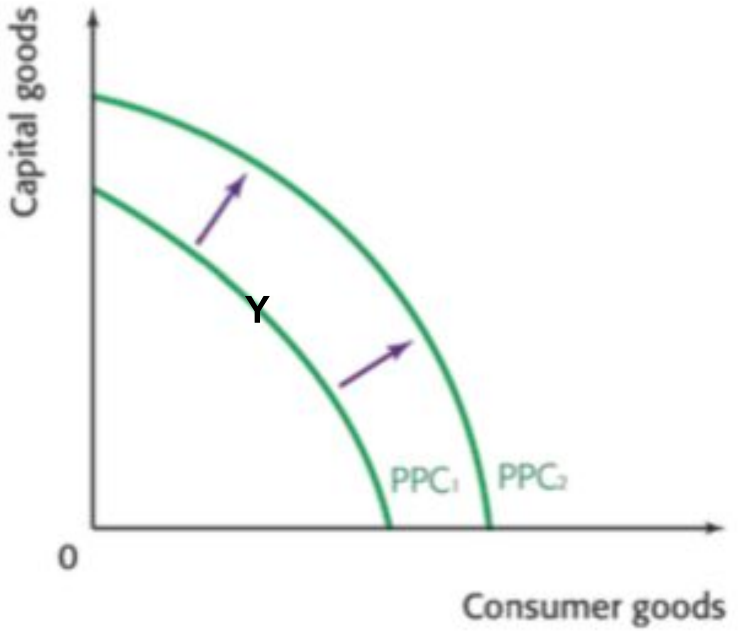
These diagrams show us that an increase in demand has led to economic growth. The increase in AD has brought about the need to employ those underemployed or unemployed resources. Furthermore firms may now be using resources more efficiently as producing more costs more. Thus moving the economy closer to the full employment of resources.

Long-term economic growth

This involves an increase in potential growth.

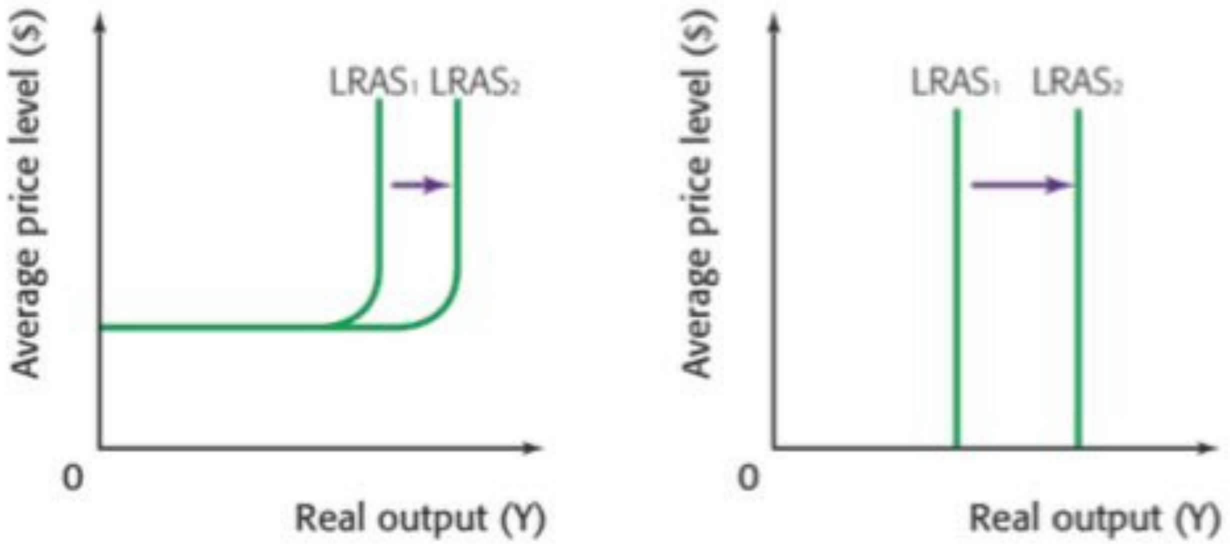
When an economy is able to produce on its PPC the opportunities for economic growth become exhausted. It doesn't mean we get to point Y, it means we can increase potential growth

Economic growth can then only be achieved by increasing in the quantity or quality of the factors of production causing an outward shift of the PPC, as shown below.



What could make this happen?

Long-term economic growth can also be diagrammed as….

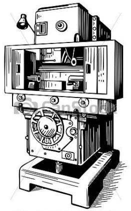


The government could implement supply-side policies to increase the potential output of the economy by bringing about an increase in the quantity of the factors of production and / or improving the quality of the factors of production.

Causes of long-term economic growth

1. Increases in productivity - (improvements in the quality of labour)

2. Advancements in technology - (improvement in the quality of capital)



3. Increase in investment - (more and better capital equipment?)
4. Improvements in infrastructure (e.g. easier to transport goods and services)
5. Increase in immigration - (increasing the quantity of labour)

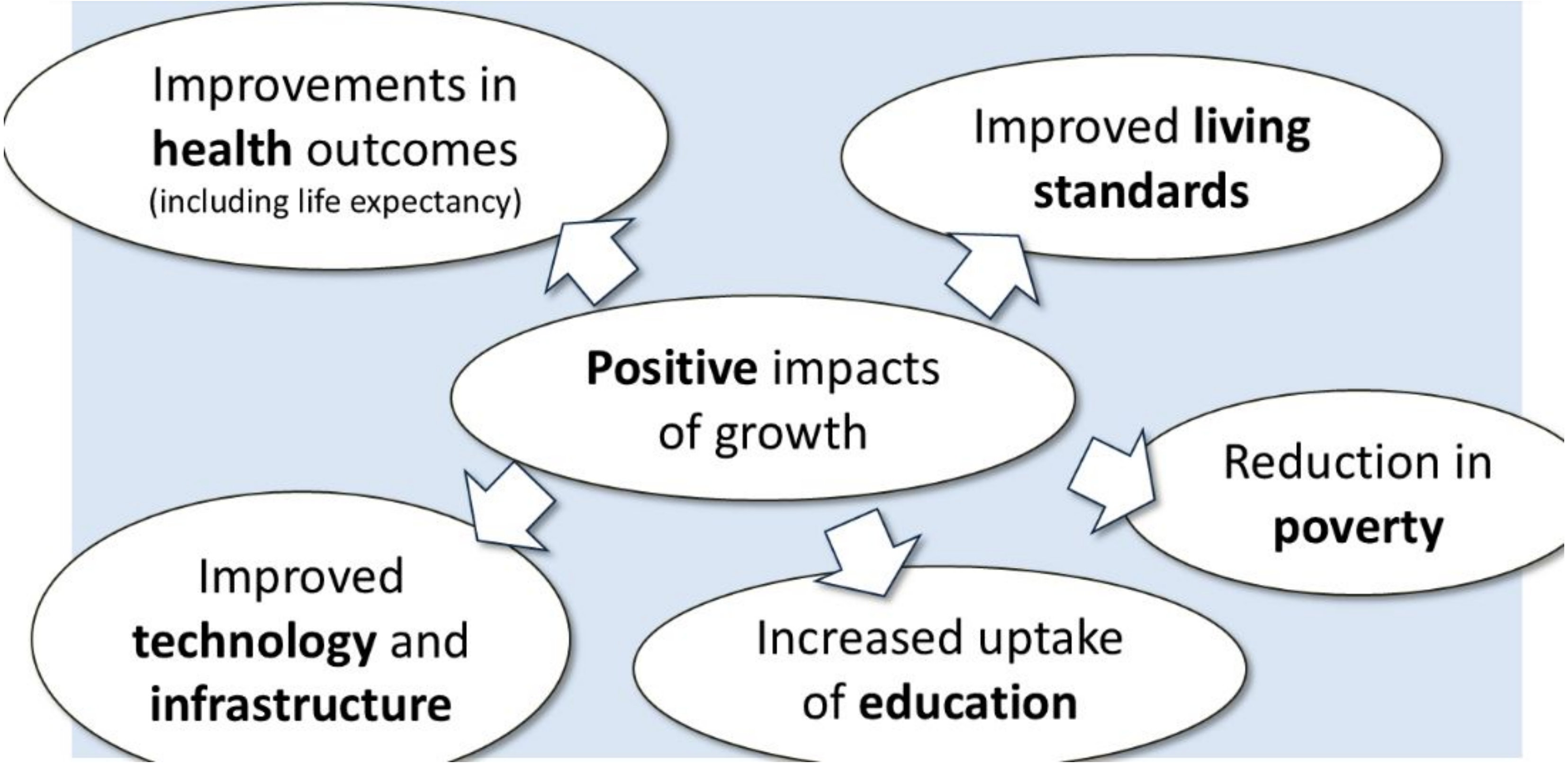
THE GOAL OF ***SUPPLY-SIDE POLICIES*** IS TO INCREASE THE POTENTIAL OUTPUT OF THE ECONOMY. USE pp.187-90 OF YOUR TEXTBOOK AND BINDER TO FIND POLICIES THAT WOULD HELP ACHIEVE POINTS 1 TO 5

Exam style questions

On the exam you may be asked questions which ask you to, “evaluate the view that increased investment is essential to economic growth or evaluate the view that improved productivity is essential to economic growth”

To answer you would diagram and explain how investment (R&D / more capital) would lead to economic growth and *alternative* methods.

Benefits of Economic Growth



Costs of Economic Growth