2.1.1 Economic growth

a) Rates of change of real Gross Domestic Product (GDP) as a measure of economic growth
b) Distinction between:
    - real and nominal
    - total and per capita
    - value and volume
c) Other national income measures:
    - Gross National Income (GNI)
d) Comparison of rates of growth between countries and over time
e) Understanding of Purchasing Power Parities (PPPs) and the use of PPP-adjusted figures in international comparisons
f) The limitations of using GDP to compare living standards between countries and over time
g) National happiness:
    - UK national wellbeing
    - The relationship between real incomes and subjective happiness

- UK's macroeconomic objectives:
    1. Full employment
    2. Low, stable inflation
    3. A sustainable current account on the balance of payments
    4. Sustainable economic growth
- An increase in real GDP is used to measure economic growth and occurs when the circular flow of income expands
- Gross domestic product (GDP) is the total value of products produced in a year or total amount spent or total amount earned
- GDP (or national income)= national output = national expenditure = national income
- Expenditure method: also known as AD it is the same as C+I+G+(X-M)
- Income method: Income from jobs + profits of private sector businesses + rent income from the ownership of land. It excludes transfer payments (payments from government), private transfers of money, incomes not registered by the tax authorities, subsistence work or bartering
- Output method (value added): the total increase in the value of goods or services as a result of the production process. It excludes costs supplying the input of a good or service
- Value added= value of production – value of intermediate inputs
- Measuring growth is import for keeping track of:
    - Rate of economic growth (GDP)
    - Changes to living standards
    - Changes in income distribution
- Long-run economic growth: is an increase in a country's productive potential. Shift outwards of the PPF
- Short-run economic growth: an increase in GDP; value of national output. Movement outwards within the PPF
- A slump is a long recession

- An economic depression is a sustained economic downturn which lasts for a long period over time
- The formula for economic growth (percentage change) is: Change in GDP/ Original GDP x 100
- Potential economic growth: A measure of the increase in capacity in an economy which can be shown by a movement outwards of the PPF curve or a measure of how efficient the economy is in using its resources
- Recession: If an economy has two consecutive quarters of negative economic growth then it is in a recession
- A quarter in economics: Three consecutive months starting January, April, July or October
- The effects of a recession: There is less spending, income and output in the economy which can lead to firms closing, increased unemployment and a resulting fall in living standards
- Real: Inflation has been taken into account; real values are sometimes referred to as 'constant prices'; prices held at a level of a base year
- Nominal: not adjusted for inflation, data expressed at current prices
- Real GDP (£)= 100 x Nominal GDP/ Price index
- GDP is measured in a common currency so they can be compared to other countries
- Exchange rates mean GDP per capita can't always be accurately compared
- Difference between volume and value of output: Volume of output measures the number of items produced but if these are falling in price then value could fall even if volume rises
- GDP per capita: the total GDP divided by the population since total population can't be assumed to be constant it gives a better indicator of incomes
- Limitations of using GDP to measure economic growth:
    1. Understates the value of the shadow economy and the value of unpaid work
    2. Data often inaccurate as poor country's struggle to collect data
    3. It can be manipulated for economic gain
- Limitations of using GDP to make comparisons:
    1. The shadow economy doesn't appear in official figures
    2. Some governments provide more benefits such as benefits which improve the standards of living
    3. The extent of income inequalities
    4. Other differences in the standard of living
- index numbers are useful for making comparisons over a period of time. The first year is called the base year which is set at 100 and changes are set as numbers above or below 100
- Standards of living: A measure of the quality of life such as physical assets and consumption, happiness, lack of stress, working hours, lack of pollution and capacity of houses
- An increase in GDP is likely to improve standards of living as people can afford more goods and services or feel that their lives are better as they do not need to work as hard to achieve their requirements in life

- Rising incomes may not improve standards of living as it depends on how the extra money is distributed, whether inflation has been taken into account, the amount spent on investment and long-term socially beneficial projects and population change
- Growth depends on:
    1. How much output is self-consumed so does not appear as GDP
    2. Methods of calculation and reliability of data
    3. Relative exchange rates
    4. Type of spending by government
    5. What size of economy you start with
- Quality of life: A measure of living standards that takes into account more than just income (or GDP)
- Economic growth: A change in levels of real GDP, not GDP itself
- Purchasing power parities (PPPs): How many units of one country's currency are needed to buy exactly the same basket of goods and services as can be bought with a given amount of another country's currency
- When cost of living is high there will be a downward adjustment of price to a PPP adjusted GDP per capita
- Example of PPP: A product costing £10 and \$10 has a PPP rate of £1=\$1 since the exchange rate is £1=\$1.50 the pound is overvalued on the currency markets
- Economists say the exchange rate should reflect PPP i.e. you can buy the same amount in both country's
- Real exchange rate: takes into account changes in costs and pries
- Nominal exchange rate should adjust to the real exchange rate as more spending on UK goods and services means the supply of dollar increases which increases the demand for the pound which causes the dollar to depreciate to the PPP however this effect often doesn't happen as trade effects dominate exchange rates. Speculative flows are more important in the exchange rate value
- The Big Mac Index works out a currency's value by comparing it to the price of a Big Mac in the USA
- If the nominal exchange rate is less than the real exchange rate the pound is undervalued and buys less in the US
- Purchasing power: The real value of an amount of money in terms of what you can actually buy with it which can vary between countries.
- GNI: Gross national income measures income received by a country both domestically (GDP) and net incomes from overseas
- GDP and GNI measure output from the workers and companies of a particular nation, regardless of the country the income earners are based in
- Subjective happiness: A measure of how people feel about themselves
- National wellbeing: Surveys can measure subjective happiness, such as security and social interactions, alongside the traditional measures such as real incomes