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A Review of the True Meaning of Economic Growth and Variations in Rates of Economic Growth around the World

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Abstract: ***Economic growth is always considered to be one of the foremost aims for any government – an increase in the total GDP (gross domestic product) of a nation which makes it a more powerful economic power on the world stage, and so on. However, achieving substantial economic growth does not necessarily mean that the benefits that come with it have trickled down throughout the entire population of the nation. Further, the rapid economic growth rates of certain Asian nations are often quoted whenever this topic is broached, while the economic growth of many under-developed nations seems to be stunted. This paper presents a lens through which economic growth can be looked at in its entirety, and not simply as a rise in GDP. The differing rates of economic growth in different parts of the world have also been explored within the scope of the paper.***

Keywords: Economic Growth, Rates of Economic Growth, Macroeconomics, Economics

"Economic growth doesn't mean anything unless it is inclusive growth." The standard definition for growth of any kind is an increase in size. Similarly, economic growth is generally defined as a sustained increase in the overall output of goods and services of a nation. This means that it refers to only long-run growth and not the short-run growth observed in the form of fluctuations in the business cycle. Although growth can be calculated based on the rise in the nominal GDP (gross domestic product), it is more accurate to calculate it in terms of rise in real GDP, i.e., GDP calculated after taking inflation into account.

The usual understanding is that when a nation's net output increases, it causes employment to increase, workers receive higher wages, and a greater quality and quantity of goods and services are made available to all consumers. However, this is not always the case. In many countries, the growth in GDP is primarily enjoyed by a small section of the country, usually the high-income groups who control a disproportionately large portion of the country's net wealth. Further, a country with a large net GDP does not necessarily indicate that the people of that country enjoy a large per capita income and good standards of living. A nation like India may have a large nominal GDP close to 3 trillion dollars, but a per capita GDP of just over 2000 dollars. On the other hand, a country like Switzerland has a net GDP of 700 billion dollars, but a much higher per capita GDP of over 80,000 dollars.

So, a true measure of economic growth would be the growth in the per capita GDP of a nation and the increase in output should be equitably distributed amongst the various income groups and not just enjoyed by the well-capitalised consumers. Essentially, for economic growth to positively impact the standards of living of the people in a country, the country's GDP growth rate should be higher than its population growth rate.

Short-term economic growth is generally observed due to short-term increases in the aggregate demand, caused by a rise in consumption, investment, government spending or net exports. Sometimes, this causes an economy to produce at a level beyond its full-employment level, which can result in high inflation and is ultimately an insufficient form of growth. A rise in aggregate demand alone cannot stimulate long term growth but instead an increase in long-run aggregate supply (a rise in the full-employment level of output) is the usual path to sustained growth in the net output of a nation.

The primary factor which influences a growth in output is productivity (output per unit input). It is this increase in the productivity (shown by an outward shift of the production possibilities curve) of a nation's workers that tends to lead to a rise in per capita income and standards of living. Productivity grows primarily due to increases in physical and human capital. Greater levels of investment in physical capital (for example, in the upgradation of technology or in purchase of more machinery) tend to increase productivity. Increased government spending to facilitate easier access to education and healthcare can help improve the level of human capital and increase productivity. This is especially true for lower income groups who might not have access to sufficient levels of these amenities otherwise.

Economic growth, especially if facilitated by unsustainable practices, can have multiple externalities, along with potential structural unemployment. Structural unemployment can be solved to some extent by more training and upskilling of workers. Greater industrialization and larger output generation can negatively affect the environment by polluting the air, water, and land and cause resource depletion. Such effects are signs of unsustainable economic growth and can reduce the benefits reaped by an increase in GDP. Decreasing air quality and unavailability of resources will negatively affect the quality of life and standards of living in the future, and so economic growth at the expense of such externalities has only limited advantages. Adopting sustainable practices of production is essential to ensure true economic growth which can benefit stakeholders and consumers without taking a toll on the environment or causing any other form of externality.

Different parts of the world have experienced different rates of economic growth. A few factors which affect this include availability of resources (factors of production), government

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policies, and trade policy. Readily available factors of production are vital for an economy to be able to produce large quantities of a good or service over time. For example, the USA was able to produce massive quantities of armaments during the Second World War due to the presence of large reserves of mineral resources as well as a strong and wide industrial base.

Government policy with regards to taxes, subsidies or any other impetus granted to domestic industries plays an important role in determining how much output the economy can yield. For example, the Cultural Revolution started by the government of Mao Zedong in China adversely impacted the economic capabilities of the country. On the other hand, the policies adopted by the Japanese government after the 1950s, such as promotion of a consumer economy and development of a new industrial policy, boosted Japan's economy to a great extent, eventually making it one of the largest economies in the world. The nature of a country's economy is another factor affecting growth. The capitalist nations such as the United States and many of its allies enjoyed greater economic growth in the decades following World War 2, as compared to the communist bloc nations such as the erstwhile Soviet Union. This can be attributed in part to the greater economic freedom and consumer choice that capitalism offers, encouraging market competition thus compelling firms to increase their productivity.

International trade policy is another area which shapes economic growth. In the post-war era, extensive trade with countries such as the United States helped the economies of countries like Germany and Japan develop, which had been in tatters after the war. The increasing number of trade agreements between nations have helped the global economy to grow, specifically fuelled by the members of such agreements. For example, the Four Asian Tigers (Hong Kong, Singapore, South Korea, and Taiwan) are all economies which grew rapidly fuelled significantly by exports. Hong Kong has extremely high ratings of economic freedom and practices absolute free trade. 99% of all imports entering Singapore are not charged by any tariffs or duties. Greater trade relations and more free trade has helped to boost the economies of many countries.

An interesting theory in relation to economic growth is the theory of convergence or the "catch-up effect". This theory says that the economies of poorer countries tend to grow at faster rates than those of richer ones, implying that over time the gap between the per capita GDP of various nations will become smaller and smaller. The Law of Diminishing Marginal Returns says that the marginal return on investment will decrease as the economy becomes more and more developed. However, although developing countries may grow faster, the lack of physical as well as human capital may impede their growth.

Economic growth is an essential macroeconomic objective of all nations. It is one of the primary aims all governments work for. But simply a growth in the nominal GDP of a nation, without accounting for any externalities, is unsustainable and will in fact harm productivity and output in the long run. There are a host of geopolitical as well as purely economic factors affecting economic growth, and nations should aim to adopt policies which will provide an impetus to the economy and facilitate long-term growth.

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