**Economics 1 Lesson 2: Measuring Economies**

**What is an Economy?**

You can barely watch the news without hearing someone talk about “the economy” and with good reason, we have already established that economics is the way in which resources (which are limited or scarce) are shared out, so the economy is the system for sharing them. Most of the time when we say the economy we mean the economy of the country that we live in, so the UK economy. You can compare economies, which means comparing the systems of different countries, and you can study what makes one system more successful than the other at a particular point in time. The UK was once the largest (wealthiest) economy in the world, that is now the US economy with China in second.

**Measuring Economies:**

There are several different ways to measure economies, and there is not always agreement about the best way to do it. We measure economies in order to compare them, but also we measure them to compare them to themselves, in other words to see how much the economy has changed from one **quarter** to the next (a quarter being a 3 month period of the year). Mostly, we measure how wealthy that country is, and it is on that basis that we say that the US is the largest economy in the world. If we were more interested in who sells the most stuff (China) or which economy is growing the fastest (that could be Rwanda but economists don’t agree on that) then we could measure that, but generally measuring an economy means figuring out how wealthy that country is, which since wealth is not all owned by the government, or by one person, is actually quite a difficult, and usually inaccurate, thing to do.

The main method of measuring the wealth of a country is to establish the GDP of that country. This is the **Gross Domestic Product**, and is a count of all the products produced in a country. This can be calculated in a few different ways, but the most common is to add up the income of all the companies in an economy. This includes things that you might not immediately think of as products or of being produced, for example a company selling mortgages, legal firms and cleaning companies, all of which produce value even if there is no end product to take home.

Economists have come up with other more complex ways to measure economies, which do things such as include companies owned by resident of that country overseas (GNI) or which take a different approach to finding the GDP such as taking it from the income of individuals rather than companies. Despite this, GDP as measured by the income of producers, remains the most commonly used method.

A further complication is that GDP will be measured in the currency of that country’s economy, but that makes it difficult to compare. Rather than just exchange pounds, yen and euros into dollars (we always compare in dollars as the US is the biggest economy) the most accurate way to compare GDP is by seeing what that would buy you in that country (for a more interesting way of learning about this, see the **Big Mac Index** in this week’s task). This measure is known as Purchasing Power Parity or PPP, and is a way of adjusting all the GDPs so that they are in dollars and can be compared equally. Like any measure, there are so many companies, so many sets of figures, and issues with changing the currencies fairly, that most people would accept that GDP is a good guide, but not a fully accurate number.

**Economic Growth:**

One of the main reasons for measuring economies is to see how they are progressing each quarter. Over the year, politicians hope that their policies will allow the economy to grow, so that the GDP will be bigger than it was that time last year. This is not always possible, sometimes because of things that the government have done, and other times because of big shocks to the system, such as coronavirus, the 2008 banking crisis and so on. When the economy suffers negative growth (economists tend to say negative growth even though we might think that’s a silly concept and prefer to say something like decline!) for two quarters in a row, so half a year in which the economy has shrunk, then we call that a **recession**. Recessions are common and are accepted as part of the economic cycle or a normal system (so long as the system grows most of the time), though governments try to avoid them, but some recessions last a long time, or are more severe than others, so they may become famous, like the 1930s “Great Depression” or the 2008 Banking Crisis.

The idea behind always targeting economic growth is that by making the country richer overall, it will trickle down and everyone will benefit. This assumes that if a company is making more money, it will expand and take on more staff, creating work for unemployed people, or it will invest in bigger premises creating work for building firms, as well as buying more from its suppliers and so on. For example if the school decided to become bigger and take on an extra 100 pupils, it would need more teachers, more buildings and more support staff like cleaners. This would create work for people (who then spend their money in hundreds of ways), but also the school would spend money on more jotters, tables and food, all of which means spending money with other companies in the economy, which helps them to grow their business. It works the other way too, if an office in Glasgow with 1000 workers shuts down, local coffee shops sell fewer coffees, meaning they order less milk from the farmer, meaning that an office closing in Glasgow has reduced his/her income!

Not everyone accepts this “trickle down” model of economics, and some people believe that simply targeting economic growth is not good enough, as it neglects other things like tackling inequality, improving the environment or even ensuring that the people of your country are happy and have good wellbeing.

**Other Ways of Measuring Economies:**

In 1972 the King of Bhutan moved away from GDP to concentrate on Gross National Happiness, which would measure how happy his people were rather than the size of the economy, and economic growth. In recent years the idea of happiness or wellbeing being as, or even more, important than GDP has started to gain some supporters. Nicola Sturgeon joins a list of politicians who are critical of GDP, including New Zealand’s leader Jacinda Ardern who has moved her country away from using GDP.

Other potential measures include those which include environmental factors in their scoring system, so that pollution and climate change become more prominent in economic discussions, and those which look at local communities rather than whole countries. The United Nations have even created their own measure, the **Human Development Index**, which they say countries should use alongside GDP to measure how developed their country is and get an understanding of the level of access to healthcare and education among other key factors. Like anything in economics, there is huge debate and controversy over all of the possible alternatives to GDP, which remains the global gold standard for measuring economies.

**Economics 1 Task 2: Measuring Economies**

Please complete this week’s task as a word document and return it as an attachment on teams. The document title should be PUPIL NAME Economics week 2.

**Part A:**

One of the challenges of using GDP is that it has to be converted into dollars to compare it, which can completely alter the true story behind the figures. The Big Mac Index was created by the Economist Magazine as a way of comparing the reality of what a dollar would mean in each country, by comparing a product which is sold in most countries around the world. Watch the video below about the Big Mac Index and then under the heading **Big Mac Index** write a paragraph of notes about what the Index is and why it is useful.

Big Mac Index: <https://www.youtube.com/watch?v=5XdYbmova_s>

**Part B:**

GDP is not the only way to measure an economy and there are suggestions for other measures which do not focus on economic growth. Read the article below, then choose which alternative method you believe is the most effective. Under the heading **Alternative Methods to GDP** state which method you think would be the most effective out of the options in the article, and then explain in your own words why you prefer that method ahead of the others given.

Alternatives to GDP: <https://ethical.net/politics/gdp-alternatives-7-ways-to-measure-countries-wealth/>

**Part C:**

Finally, if you wish to maintain a glossary of economic terms, then the words in bold from the lesson would be a good addition to that. Once again this part of the task is voluntary, but will help you in the progress check.

**Next Time:**

In the next lesson we will begin to look at some of the biggest concepts in economics, starting with the rules of supply and demand which are important to any understanding of how economies and businesses operate.

**Further Reading:**

If you want to learn more about the alternatives to GDP beyond this week’s lesson, then Nicola Sturgeon’s TED talk is worth watching – <https://www.ted.com/talks/nicola_sturgeon_why_governments_should_prioritize_well_being?language=en>

This Forbes Magazine article on Jacinda Ardern’s move away from GDP in New Zealand also develops these points further – <https://www.forbes.com/sites/jamesellsmoor/2019/07/11/new-zealand-ditches-gdp-for-happiness-and-wellbeing/#58c88b331942>

If you’re keen to see how different countries stack up when their GDP is converted into dollars, then the CIA (yes that CIA) have a website full of data called the CIA World Factbook and you can get the GDP for any country here - <https://www.cia.gov/library/publications/the-world-factbook/fields/209.html>