SECTION 7.1 ECONOMIC GROWTH

- John Maynard Keynes once said that "in the long run we are all dead." He wanted to smooth out the business cycle, largely because of the implications that short-term cyclical fluctuations had for buyers and sellers in terms of unemployment and price instability.
- His flippant remark about the long run ignores the fact that human welfare is greatly influenced by long-term changes in a nation's capacity to produce goods and services. Emphasis on the short run of the business cycle ignores the longer term dynamic changes that affect output, leisure, real incomes, and life styles. Many would argue that in the long run, economic growth is a crucial determinant of our well-being.
- What are the determinants of long-run economic change in our ability to produce goods and services? What are some of the consequences of rapid economic change? Why are some nations rich while others are poor? Does growth in output improve our economic welfare? We need to explore these questions.
- **Economic growth** is usually measured by the annual percent change in real GDP per capita.
- Along the production possibilities curve, the economy is producing at its potential output. How much the economy will produce at its potential output, sometimes called its **natural level of output**, depends on the quantity and quality of an economy's productive factors. In addition, improved technology can increase the economy's production capabilities. Another way of saying that economic growth has shifted the production possibilities curve out is that it has increased potential output.

Exhibit 1: *Short-Run versus Long-Run Economic Growth*

Exhibit 2: *Economic Growth and the Shifting Production Possibilities Curve*

- The Rule of 70 gives an approximation of the length of time it will take for a country to double its output. To get this figure, divide 70 by the annual growth rate. A country with a growth rate of 3.5 per cent will double its output in 20 years (70/3.5) Even small differences in growth rates will have a large impact over the long term.

Exhibit 3: *Canadian Real Gross Domestic Growth per Capita*

- Over the 1989-1998 period, Canada had one of the lowest growth rates among industrial countries. However between 1999 and 2010, Canada's growth rate exceeded that of the United States and compared favourably with other industrial countries. Our growth rate must exceed that of the United States if we are to reduce the difference in our standards of living.
- The "richest" or "most developed" countries today have many times the per capita output of the "poorest" or "least developed" countries. The international differences in income, output and wealth are striking and have caused a great deal of friction between developed and less developed countries.

Exhibit 4: *Growth in Real Per Capita GDP, Selected Industrial Countries*

- ***China and India*** *have far lower levels of GDP per capita than Canada but this could change quickly. The growth rates for those countries have recently been in the range of 10% per year. This economic growth has pulled millions out of poverty.*