Economic Growth

Economic growth is one of the prime goals of every nation be small or large. Right from the beginning of the development debates, it is taken as the key driver and indicator of development. The prosperity of a nation is judged in terms of the rate of economic growth it achieves from time to time.

1.2.1 Meaning

Economic growth is the **long-term expansion of a country's productive potential.** It is the process by which a nation's wealth increases over time. Although the term is often used in discussions of short-term economic performance, in the context of economic theory, it generally refers to an increase in wealth over an extended period. An increase in the capacity of an economy to produce more goods and services, compared from one period of time to another becomes an indicator of economic growth. Economic growth is indicated through GDP or GNP per capita. Increase in *the capital stock, advances* in *technology,* and *improvement* in the *quality* and level of literacy are considered to be the *principal causes* of economic growth. In recent years, the idea of *sustainable development* has become a prime indicator of economic growth. Sustainable development focuses on *environmentally sound processes* that must be taken into *account* in growing an *economy*.

Economic growth has two meanings:

1. Firstly, and most commonly, growth is defined as an increase in the output that an economy produces over a period of time.
2. The second meaning of economic growth is an increase in production of an economy by the use of its scarce resources.

When an economy is in a position to produce more, it is termed as economic growth. The increase in production can be noted through the increase in the production of consumer goods and capital goods.

Economic growth, thus simply means an increase in the production and consumption of goods and services. Todaro and Smith define economic growth as "The steady process by which the productive capacity of the economy is increased over time to bring about rising levels of national output and income." Economic growth has been defined by Arthur Lewis as "the growth of

output per head of population”.
Economic growth is often and generally indicated by increasing real gross domestic product (GDP) or real gross national product (GNP), and it has been a primary, perennial goal of many societies and most governments. However, it should be remembered that economic growth has its limitations and sometimes blind stress on economic growth results in negative yields like degradation of environment which becomes detrimental to the lives and longevity of the people and the planet. So instead of brining economic welfare it proves disastrous for human existence.

1.2.2Characteristics of Economic Growth

There are some marked characteristics of economic growth. According to Simon Kuznet there are six characteristics of modern economic growth.
They are:

- High rates of growth of per capita incomes.
- High rates of growth of total factor productivity.
- High rates of structural transformation of the economy.
- High rates of social and ideological transformation.
- Growth of trade, specifically import of raw materials and
- Export of manufactures.

1.2.3Why countries desire economic growth?

Economic growth is the most important economic indicator of development. It simply tells us how much more the economy is producing than it did before. If the economy is producing more, businesses are more profitable, and stock prices rise,it leads to more capital investment and more employment. As more jobs are created, incomes rise. This gives consumers more money to buy more products and services, driving more economic growth. For this reason, all countries want positive economic growth.
Positive economic growth generates economic welfare. It raises the level of employment. It brings more purchasing power to the people. It betters of their consumption capacity and ensures them a better standard of living. When there is a general rise in the standard of living of the people, the country’s economy moves forward.

1.2.4 Key drivers of economic growth

There are certain driving forces of economic growth. According to Arthur Lewis, economic growth is conditioned by (1) economic activity, (2) increasing knowledge and (3) increasing capital. In other words, these three factors are labour, technical improvements and capital. Taking into consideration the aforesaid factors, the following factors can be discussed as the most important drivers of economic growth.

The most important driver of economic growth is the increase in the physical capital stock of a nation. The amount of physical stock determines the distribution pattern. Physical capital stock includes land available, natural resources, water, forest etc. In every country there is a dearth of physical

Growth in physical
capital stock
leading to increase
in per capita
income
Growth in the size of
active labor force
Growth in the quality of labor
(Growth of Human Capital)
Technological progress
and innovation leading
to increase in production
(both qualitative and
quantitative leap)
Stable system of democratic
governance, economic stability
Increase in the stock
of knowledge

capital available to the population. If the stock of physical capital can increase through the careful utilization pattern or better exploration of the natural resources, then there is a necessary increase in the stock and the number of users increase and the amount available to each user increases. This gives birth

to economic growth.
An increase in the labour force participation rate symbolizes economic growth. The challenges of growth, job creation, and inclusion are closely intertwined. Increased labour force participation creates opportunities for people, increase their economic self sufficiency and lead to a better standard of living among them. It also reduces the dependency rate. The demand for products increase and it brings transformations in the process of production. When production increases due to increased demand, the market expands and diversifies. This brings economic growth.
Along with physical capital an important factor of economic growth is productive labour force. Productive labour force is needed to make an optimal and efficient use of physical capital. Productive labour force is the outcome of an increase in the quality of human capital in the country. The human capital depends on the level of education, skill development, health of the workers, their training and ability to innovate, motivation for work etc. When a country fosters all these qualities or provides these inputs, economic growth is spearheaded, because the process of production is well anchored and very efficiently managed to yield the maximum output.
When the human capital of a country is overstressed, there is a qualitative improvement in the labour force. This brings forth tremendous innovations and transformations in the process of production. There are rapid technological progresses. The intelligent labour force provides a new face to the process of production. There is both a quantitative increase and a qualitative rise in production. This significantly contributes towards economic growth.
However economic growth is always tied to economic stability and a stable system of governance. Economic instability like recessions, depressions retard the process of economic growth. Economic stability is dependent on a prudent and stable government which plays a significant role in making economic policies, planning and programmes. A visionary government can better facilitate economic growth. Particularly, when a government remains free from rifts, challenges and threats it remains relatively stable and focuses on better investment of capital for economic growth.

Finally, the stock knowledge or knowledge capital plays a crucial role in economic growth. Of all the factors of production, knowledge capital creates the longest lasting competitive advantage for economic growth. Knowledge capital is an essential component of human capital.Stock knowledge is an intangible asset that comprises the information and skills of the individuals who serve as employees, their experience with the process of production, group work and on-the-job learning. Thus, knowledge capital refers to the know how that results from the experience, information, knowledge, learning, and skills of the labor force. Knowledge capital is not like the physical factors of production - land, labor and capital .It is based on skills that employees share with each other in order to improve efficiencies, rather than on physical items. Skills and access to knowledge provides a better work efficiency to the labor engaged in the process f production.

1.2.5Circle of Economic Growth

There is a well decided circle of economic growth. It is initiated from the point of rising consumer demand. When the consumers have higher demand, the supply sides need a strengthening by increasing the output. To increase the output, investment of capital in all its forms, physical, human, and knowledge capital becomes a need. When the quality and amount of investment increases, there is a phenomenal rise in productivity. This leads to an increase in the wages received by the people engaged in production. This increases their purchasing power and the demand side is strengthened which boosts the subsequent stages of economic process and ultimately result in economic growth by increased per capita income and GDP. The circle of economic growth can be indicated through the figure below.

1.2.6The Phases of Economic Growth

Economic growth normally has two important phases. They are the rising phase called **economic expansion** and a declining phase called **economic recession**. Economic expansion is the most desirable phase of economic growth, when the economy grows sustainably. At some point, confidence in economic growth dissipates. When economic growth becomes economic contraction, it's known as a recession. An economic depression is a recession. It is also called a down turn in the economy.

Increased
wage
Increased
Higher investment
out put
Rising
consumer
demand
Increase
in the
wage
received
Increased
wage results in
the increasing
purchasing
power
Higher
productivity
Strengthens
demand and fuels
economic growth

Rostow's Stages of Economic Growth

W.W. Rostow, the American economic historian described the transformation of countries from underdevelopment to development in terms of stages of growth. He is of the view that all countries must pass through the following stages.

1) **The traditional society;**
2) The transitional society;
3) The take- off stage;
4) The mature stage and;
5) The age of high mass consumption

The traditional societies are custom-bound and tradition-oriented. These hinder progress and generate economic backwardness. The poor countries of today are good examples of traditional society. In short, the factors which are essential for economic growth like development of new knowledge, changing practices of production, skill are missing in such societies.

In the transitional society, the conditions for take-off stage are established. During this stage, the force of customs and traditions get reduced; economic motivation rises and there are perceptible improvements in physical and social infrastructure. Once an economy attains the take–off stage, it experiences sustaining growth.

The take-off stage refers to a situation where an economy transforms itself from a predominantly agricultural to a predominantly industrial society. For an economy to attain the take-off stage, it is required to make heavy investment from its resources for industrial production and development of allied services. The take-off stage was made possible in some countries by leading sectors like railways and defence.

After the take- off stage, when the economy attains self sustaining growth, it enters the mature stage. During this stage, the government has to make some basic decisions. As there will be abundant resources and goods, it has to decide whether it has to use them for strengthening the nation into a strong and powerful state militarily or to use the resources for improving the welfare of the people.

The final stage is the age of high mass consumption. During this period, people will consume all kinds of goods especially durable goods like cars on a mass scale.

Rostow's stages of economic growth are only broadly true. All nations have not gone through the order in which he has described the stages.