Assessing The United Kingdom GDP Since 2008

United Kingdom has been classified as a dominant European finance centre. Furthermore, it has been categorized as the 2nd best country in the world for its financial activity (Dew, 2018). According to IMF (2018 cited in Smith, 2018), UK is placed 5th in the group of world's biggest economies with the Nominal GDP value of $2.94 trillion (£2.304 trillion). Macroeconomics is a very important branch in Economics that studies economies like UK's as a system. Tragakes (2012, p.547) gives a detailed definition of macroeconomics as "the branch of economics that examines the economy as a whole by use of aggregates, which are wholes or collections of many individual units, such as the sum of consumer behaviours, total income and output of the entire economy as well as total employment and the general price level." Macroeconomics is further used to evaluate the success and failure of the policy implemented by the government. Moreover, macroeconomics is used to study about the relationship between different economies (Riley, n.d.).

Pettinger (2017) states that "Gross Domestic Product (GDP) measures the national output/national income of an economy; this is a measure of the volume of goods and services produced in a given year". Foreign direct investment and output of foreign owned businesses that are based and located in a nation are also calculated in GDP (Riley, n.d.). Tragakes (2012, p.217) states that "the circular flow of income shows that in any given time period (say a year), the value of output produced in an economy is equal to the total income generated in producing that output, which is equal to the expenditures made to purchase that output." This model is used to show how GDP is calculated. Also, it shows how goods and services and the income generated by factors of production flow between firms, households and government (Riley, n.d.). As the name suggests, the income is flowed in and out of the economy. The income entering into the economy is known as injections. Investment, exports and government spending are injections. The money flowing out of an economy is called leakages. Savings, imports and taxes are form of leakages.

There are three methods to calculate GDP and all methods should give the same result.

Expenditure approach = Income approach = Output approach

Firstly, expenditure approach [also called aggregate demand (AD) which is explained in the next paragraph] has four components; consumption (C), government spending (G), investment (I), and net exports (exports (X) minus imports (M)) (Riley, n.d.). Expenditure approach is a summation of all spending that is used to buy final goods and services produced domestically over a certain time period. Second, income approach is the summation of all the income earned domestically by the nation from the factors of production used to produce the goods and services over a period of time (Tragakes, 2012, p.219). Transfer payments, private transfers of money and income that is not registered with tax authorities is excluded as no production of good or service takes place when these payments are given to people (Riley, n.d.). Third, in output approach the value of final goods and services produced by a nation domestically over a time period is calculated (Tragakes, 2012, pp.219).

Economic growth defined by Tragakes (2012, p.543) is, "increases in total real output produced

by an economy (real GDP) over time." All economies produce different goods and services, after a certain period of time the quantities produced by different economies change. Tragakes (2012, p.13) point out that when there is an increase in output, economic growth takes place, but when a decrease takes place, there is an economic contraction or negative economic growth. Tragakes (2012, p.552) states that "recession is an economic contraction, where there is falling real GDP (negative growth) and increasing unemployment of resources which last six months or more." UK faced a great recession which is also referred to as "the economic downturn between 2008 and 2013". There was a Global Credit Crunch that began after 2007/08 which led to a prolonged period of high unemployment level and negative economic growth (Pettinger, 2017). There are two main causes of economic growth; demand side and supply side factors.

As mentioned earlier, AD has four components; consumption (C) is all the money spent by households on goods and services. Investment (I) is the money spent by firms on investment goods. Government spending (G) is inclusive of current spending (wages and salaries) and investments on new public goods and services like roads and schools. Net exports (X-M) is the amount of money spent on importing goods and services minus the amount of money earned by exporting domestically produced goods and services (Anderton, 2015, pp.109). Hence,

$$AD=C+I+G+(X-M)$$

Tragakes (2012, pp.540) defines aggregate supply (AS) as "the total quantity of goods and services produced in an economy over a particular time period, at different price levels, ceteris paribus."

A higher AD and higher economic growth are achieved by a rise in consumption, investment, government spending or exports (Pettinger, 2017). AD is affected by many factors. Firstly, the lower the interest rates are, the cheaper the borrowing is and it encourages firms to invest and consumers to spend. Secondly, consumer confidence is a very important factor because the more the consumers are optimistic about their future the more they will be encouraged to borrow and spend. They will save more and spend less if they are pessimistic. Thirdly, a positive wealth affect is created when there is an increase in house prices. Consumer spending is encouraged as people have the option of re-mortgaging against the rising value of their homes. In UK, there are many homeowners, so house prices is a very important factor.

Fourthly, in 2017, there was a fall in UK's real wages. There was a decline in real incomes due to a higher inflation rate than nominal wages which led to cutting on spending, especially luxurious goods. Fifthly, exports become more competitive and imports become really expensive when Sterling Pound is devalued. This helps in increasing demand for domestically produced goods and services. In short term growth is boosted even if depreciation could cause inflation. Lastly, banking sector can be dominating when determining the areas of investment and growth, which was proved in the 2008 credit crunch (Pettinger, 2017).

In the long run, determination of economic growth is determined by the factors that affect the growth of LRAS (long run aggregate supply). An increase in AD will be inflationary if there is no increase in LRAS. Figure 6 shows the LRAS curve. LRAS can be influenced by the following factors; firstly, investment in infrastructure like roads helps firms with cost cutting and expand production. Without proper infrastructure, it would be hard for firms to compete internationally. Developing economies lack due to poor infrastructure. Secondly, productivity of workers

(education, training and motivation) is known as human capital, the higher the productivity of worker, the more the efficiency in production process. Thirdly, for higher economic growth, an economy should be up-to-date with the new technology. Lastly, if labour market is flexible, firms will find it easy to employee workers, which will help in expansion (Pettinger, 2017).

The size of UK economy got bigger every quarter but in April to June 2008 it started to fall. The economy kept shrinking for five consecutive quarters. Between the first quarter of 2008 and second quarter of 2009 the economy fell by over 6%. It took 5 years for the GDP to recover and now the economy is 11% bigger before the recession. Many people became unemployed since the economy was shrinking. About 2.6 million people were seeking employment by the end of 2011. Quarterly unemployment was highest since 1995, it crossed 8.4%. By the end of 2015, unemployment rate returned to its pre-downturn rate, and after this it has been falling with a minimal unemployment rate of 4.3% in the third quarter of 2017 and by the end of the year it slightly rose. Since recession, earnings have lagged behind prices of goods. (ONS, 2018, https://www.ons.gov.uk/economy/grossdomesticproductgdp/articles/the2008recession10yearson/2018-04-30). The 2008 recession was one of the major reasons of the major crisis in the UK. Figure 7 shows how recession caused a drastic change in the GDP. The main reason of the great recession was the credit crunch which was caused by the bad debts in US housing market; it did not only affect UK's economy but all economies in Europe. The main causes are; there was a decrease in bank lending due to credit crunch because of shortage of liquidity, Secondly, due to financial instability, consumers and businesses lost confidence in investment. Thirdly, there was fall in exports due to global recession. Also, there was a negative impact on wealth due to a downfall in the prices of housing market (Pettinger, 2017).

In conclusion, GDP is not a perfect measure although it is the most common method of measuring an economy's well-being, it has limitations (shown in figure 9). Furthermore, there are many other indicators like HDI (Human Development Index). Clarke (2017, https://www.itv.com/news/2017-05-11/has-the-uk-economy-actually-recovered/) reported on ITV that "last year the country was almost the fast growing economy in the G7". UK could not gain the G7 position because of the disparities within the economy like the Brexit issue. Clarke (2017, https://www.itv.com/news/2017-05-11/has-the-uk-economy-actually-recovered/) argued that "It matters even more because the Bank of England now expects slower growth this year, real pay to fall, and household incomes to fall." The politicians and people residing in UK should take precautionary measures to prevent the economy to further go down.

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