Edexcel (B) Economics A-level

Theme 3: The Global Economy

3.1 Globalisation

3.1.1 Growing economies

Notes

Growing economic power of:

- ### Asia (China and India)

Since WW2, global trade has increased significantly. The increasing number of trading blocs, the rise of emerging markets such as China and India and greater participation from previously communist nations has led to a change in the pattern of trade.

The deindustrialisation of countries such as the UK has meant the manufacturing sector has declined. This means that production of manufactured goods has shifted to other countries, such as China, whilst the UK now focuses more on services.

This has led to the industrialisation of China and India. Their share of world trade has increased and the volume of manufactured goods that they export has increased.

Between 1995 and 2005, India's share of textiles and clothing fell from 35% in 1995 to 16% in 2005. Instead, India's manufacturing sector seems to produce more engineered goods than clothing and textiles. This has resulted in UK manufacturers selling fewer manufactured goods abroad.

China and India are important for African infrastructure. They have invested in their infrastructure in exchange for natural resources.

For a long time, China has been running a trade surplus with the US. Since 2006, the US trade deficit has narrowed with China, and China has reduced their trade surplus, too. China has planned this change from export-led growth to growth fuelled by domestic consumption.

Both China's and India's share in agriculture, mining and fuel has declined. Both countries are important in the Euro area, with trade and financial relations. China is a main import source, whilst both are important for capital.

China and India have been investing in infrastructure. Examples of physical infrastructure include transport, energy, water and telecommunications. Higher supply costs delay businesses and it reduces the mobility of labour.

For example, India's poor irrigation system makes it difficult to sustain food grain production if there is low rainfall. It hurts the poorest communities and it leads to rising food prices. There are also regular power cuts. The lack of a continuous supply of electricity affects transport, communication and healthcare. It is estimated that $400 billion needs to be invested in power to meet the development goals.

The Asian Infrastructure Investment Bank (AIIB) is led by China and it funds Asian energy, transport and infrastructure. The UK is one of the founding members, along with Germany, Australia and South Korea. The UK's involvement should give British firms an opportunity to invest in fast growing economies.

Infrastructure development is a top priority for the Chinese government. From the late 1990s to 2005, 100 million Chinese people benefited from improved power and telecommunications. Employment can be boosted with improved roads, railways and airport constructions. However, some remote areas still have non-mechanised means of transport.

Some economists argue that the development gap between China and other emerging economies is due to its focus on infrastructure projects. China invested 9% of their GDP in infrastructure in the 1990s and 2000s, whilst most emerging economies only invested around 2%-5% of GDP.

China has the first and only high speed Maglev train system in the world between the city centre in Shanghai and its international airport. Some economists might argue that is it unnecessary to build more airports, since there are already almost 200 airports in China and about 80% of people live within 100km of an airport in China. There is an opportunity cost of not investing funds elsewhere.

More information on the AIIB can be found here:

http://www.bbc.co.uk/news/business-31867934
http://www.bbc.co.uk/news/business-31921011

- **Africa**

Africa has been a top recipient of Chinese aid. By the end of 2009, it received 45.7% of China's cumulative foreign aid. It is important as a policy instrument for China with engagement with Africa.

Africa's saving rate is around 17%, whilst the average for middle income countries is around 31%. This makes it more expensive for the African public and private sectors to get funds since they have higher borrowing costs. This impedes capital investment.

The population can impact the growth and development of a country. There is a link between keeping birth rates down and fighting hunger, poverty and environmental damage. Rapid population growth has complicated efforts to reduce poverty and eliminate hunger in Africa. The current population of 1.1 billion is expected to double by 2050, which is not sustainable.

Primary products are raw materials in industries such as agriculture, mining and forestry. Mining accounts for just over 60% of South Africa's exports. Their ability to pay foreign debts and for imports relies on this.

Implications of economic growth for individuals and firms

	Costs	**Benefits**
Consumers	Economic growth does not benefit everyone equally. Those on low and fixed incomes might feel worse off if there is high inflation and inequality could increase. There is likely to be higher demand-pull inflation, due to higher levels of consumer spending. Consumers could face more **shoe leather costs,** which means they have to spend more time and effort finding the best deal while prices are rising. The benefits of more consumption might not last after the first few units, due to the **law of diminishing returns,** which states that the	The average consumer income increases as more people are in employment and wages increase. Consumers feel more confident in the economy, which increases consumption and leads to higher living standards.

	utility consumers derive from consuming a good diminishes as more of the good is consumed.	
Firms	Firms could face more **menu costs** as a result of higher inflation. This means they have to keep changing their prices to meet inflation. Firms supplying inferior goods are likely to see a fall in sales.	Firms might make more profits, which might in turn increase investment. This is also driven by higher levels of business confidence. Higher levels of investment could develop new technologies to improve productivity and lower average costs in the long run. As firms grow, they can take advantages of the benefits of economies of scale. If there is more economic growth in export markets, firms might face more competition, which will make them more productive and efficient, but it will also give them more sales opportunities.
The government	Governments might increase their spending on healthcare if the consumption of demerit goods increases.	The government budget might improve, since fewer people require welfare payments and more people will be paying tax.

Current and future living standards	High levels of growth could lead to damage to the environment in the long run, due to increase negative externalities from the consumption and production of some goods and services.	As consumer incomes increase, some people might show more concern about the environment. Also, economic growth could lead to the development of technology to produce goods and services more greenly. Higher average wages mean consumers can enjoy more goods and services of a higher quality. Public services improve, since governments have higher tax revenues, so they can afford to spend on improving services. This could increase life expectancy and education levels.

Rising incomes

Rising incomes could lift individuals out of poverty, particularly in developing countries. In China, it is estimated that half a billion people have been lifted out of poverty due to the average 10% growth rate. However, increases in income might not be evenly distributed across a population, and there could be rising inequality as a result.

Conversion of nominal to real values

Real values are adjusted for inflation. For example, real GDP is the value of GDP adjusted for inflation. For example, if the economy grew by 4% since last year, but inflation was 2%, real economic growth was 2%.

Nominal values are not adjusted for inflation. Real GDP is the value of GDP without being adjusted for inflation. In the above example, nominal economic growth is 4%. This is misleading, because it can make GDP appear higher than it really is.

Real and nominal values are applied to data using constant and current prices. Constant prices consider inflation, whilst current prices do not.

Calculating and interpreting index numbers

Index numbers are used to make comparisons between years, and to measure the magnitude of change over time. A **base year** is used and is then compared to other years. For example, if the year 2015 is the base year, the value given to it is 100. If inflation has risen by 5% between 2015 and 2018, the index number for 2018 will be 105.