

The impact of economic growth

Economic growth is an increase in real GDP (output), which usually raises living standards over time. However, growth can also create trade-offs .

For example in 2020 due to the covid 19 lockdown the economy shrank by 10% . This was the largest one year drop in over 300 years.

Consumers

Benefits

Higher incomes and higher living standards

Growth often increases employment (increases real GDP → increase amount of goods/services being produced → increasing derived demand for labour) and wages, so households can afford more goods and services. Over time, this can reduce absolute poverty.

Example: rapid economic growth in China (average of 9.5% a year since 1978) helped lift over 800 million households out of absolute poverty .

Better quality and wider choice

As incomes rise, demand shifts towards higher quality goods and services, such as improved healthcare, education, and technology. This also gives firms stronger incentives to innovate because more consumers can pay for new products.

More job opportunities

Higher output usually increases demand for labour, which can reduce unemployment. This improves income security and tends to support consumer spending.

Costs

Inflation reduces purchasing power

If growth is demand-led (AD rising faster than AS), it can create demand-pull inflation. This hits people on fixed incomes hardest, because their real spending power falls.

Extreme example: Zimbabwe experienced hyperinflation, showing how rapidly rising prices can destroy purchasing power. Inflation peaked at **79 billion** in 2008 .

Inequality can worsen

Growth may benefit high-skilled workers and **asset owners** more than low-skilled workers. This widens income and wealth gaps and can increase social tensions.

Written by udoecon.com

Example: the wealthiest **10% of households** now hold roughly **43% of all UK wealth**, compared to less than 1% held by the bottom 10%.

Lower non-material wellbeing

Higher output can mean longer working hours and less leisure time. Rising incomes can also increase consumption of demerit goods (such as alcohol and cigarettes), which can harm long-run wellbeing.

Firms

Benefits

Higher sales and profits

Rising household incomes often increase consumer spending, which boosts firms' revenues and profits.

Example: the rise of e-commerce increased profits for Amazon.

Economies of scale

Growth can allow firms to expand output and spread fixed costs, reducing average costs. This can improve competitiveness and profitability, especially in capital-intensive industries.

More investment and innovation

Higher expected demand encourages firms to invest in new machinery, R&D, and productivity improvements. This can raise potential output (long-run capacity) and strengthen long-run growth.

Example: Tesla investing in battery and renewable-related technology.

Costs

Greater competitive pressure

Growing markets attract new entrants, which increases competition and can squeeze profit margins.

Example: large incumbents like Microsoft and Apple face constant competitive threats as tech markets expand.

Inflation can reduce competitiveness

If domestic inflation rises faster than competitors, exports become less price-competitive. Lower exports can reduce revenue and delay investment plans.

Resource depletion and rising long-run costs

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Rapid growth can increase extraction of finite resources such as energy and minerals, which can raise input costs in the future. Environmental damage can also trigger regulation and taxes that increase firms' costs over time.

Government

Benefits

Higher tax revenues

Higher incomes and profits increase receipts from income tax, VAT, and corporation tax. This gives governments more capacity to fund public services.

Lower welfare spending (in some cases)

If growth reduces unemployment, spending on welfare benefits may fall. This can improve the government's fiscal position.

More funding for infrastructure and public services

With stronger revenues, governments can invest in transport, healthcare, education, and productivity-enhancing projects.

Costs

Inflationary pressure and policy trade-offs

Rapid growth can increase inflationary pressure, forcing policymakers to prioritise inflation control. Higher interest rates can then slow growth and raise debt-servicing costs for households and firms.

Negative externalities and environmental damage

Growth often increases pollution and congestion unless regulated.

Example: industrial expansion has contributed to pollution challenges in India.

Current and future living standards

Benefits

Higher material living standards now

Higher real GDP per capita usually improves living conditions by increasing access to goods and services. It can also support better healthcare outcomes, education access, and housing quality.

Better technology

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Growth can fund innovation and speed up adoption of cleaner or more efficient technologies. This can improve productivity and quality of life, including through greener production methods.

Costs

Unsustainable growth damages future living standards

If growth relies on heavy pollution, deforestation, and emissions, future generations may face higher climate and health costs.

Example: deforestation pressures in the Amazon rainforest reduce biodiversity and carbon absorption capacity.

Resource exhaustion

Overuse of finite resources can cause scarcity, higher prices, and lower long-run productive capacity. This can reduce future consumption possibilities, creating an opportunity cost of today's growth.