

Answer on Question#39193 – Economics - Macroeconomics

Assignment

The Potential Growth line from the Business Cycle shows a slow and steady increase in Real GDP. Why do economists prefer to measure Economic Growth in "Real" terms instead of "Nominal" terms? Why is a slow and steady growth rate preferred to a faster growth rate?

Solution

Economist compute real GDP because different regions have varying price levels. Economists also use real GDP rather than nominal GDP to gauge economic well-being because real GDP is not affected by changes in prices, so it reflects only changes in the amounts being produced. If nominal GDP rises, you do not know if that is because of increased production or higher prices.

The ideal GDP growth rate is one that enable the economy to grow at a healthy rate. If growth is too fast, the economy risks inflation. To grow, an economy also requires more natural capital, including soil, water, minerals, timber, other raw materials, and energy sources. When the economy grows too fast or gets too much, this natural capital is deleted, or “liquidated”.