WEDC

MOBILE NOTE 54

Economic development indicators

Introduction

One way of measuring a country's development progress is to look at its economic indicators.

There are many different indicators used and it is useful to have an appreciation of what the terms mean.

This note gives a brief description of some of the most common economic indicators including GDP, GNP, national debt, trade balance, credit rating and wealth distribution.

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Economic development

Economic development is the increase in the amount of people in a nation's population with sustained growth from a simple, low-income economy to a modern, high-income economy. Its scope includes the process and policies by which a nation improves the economic, political, and social well-being of its people.

A number of indicators of economic growth are used and these are introduced below.

Gross Domestic Product (GDP)

Gross domestic product is a measure of economic activity in a country. It is calculated by adding the total value of a country's annual output of goods and services.

GDP = private consumption + investment + public spending + the change in inventories + (exports - imports).

Figure 1. GDP (PPP) per capita

It is usually valued at market prices; by subtracting indirect tax and adding any government subsidy, however, GDP can be calculated at factor cost. This measure more accurately reveals the income paid to factors of production.

Adding income earned by domestic residents from their investments abroad, and subtracting income paid from the country to investors abroad, gives the country's gross national product (GNP). GDP is disliked as an objective of economic policy by some because it is not a perfect measure of welfare.

It does not include aspects of the good life such as some leisure activities. Nor does it include economically valuable activities that are not paid for, such as parents teaching their children to read. But it does include some things that lower the quality of life, such as activities that damage the environment.

Gross National Product (GNP)

GNP is calculated by adding to GDP the *income* earned by residents from investments abroad, less the corresponding income sent home by foreigners who are living in the country.

National debt

National debt is the total outstanding borrowing of a country's government (usually including national and local government). It is often described as a burden, although public debt may have economic benefits. Certainly, debt incurred by one generation may become a heavy burden for later generations, especially if the money borrowed is not invested wisely.

The national debt is a total of all the money ever raised by a government that has yet to be paid off; this is very different from an annual public-sector budget deficit. In 1999, the American government celebrated a huge budget surplus, yet the country still had a national debt equal to nearly half its GDP.

Trade balance

The balance of trade (or net exports, sometimes symbolized as NX) is the difference between the monetary value of exports and imports of output in an economy over a certain period. It is the relationship between a nation's imports and exports. A positive or favorable balance of trade is known as a trade surplus if it consists of exporting more than is imported; a negative or unfavorable balance is referred to as a trade deficit or, informally, a trade gap.

The balance of trade is sometimes divided into a goods and a services balance.

Measuring the balance of trade can be problematic because of problems with recording and collecting data. As an illustration of this problem, when official data for the entire world's countries are added up, exports exceed imports by a few percent; it appears the world is running a positive balance of trade with itself. This cannot be true, because all transactions involve an equal credit or debit in the account of each nation.

The discrepancy is widely believed to be explained by transactions intended to launder money or evade taxes, smuggling and other visibility problems. However, especially for developed countries, accuracy is likely.

Credit rating

A credit rating estimates the credit worthiness of an individual, corporation, or even a country. It is an evaluation made by credit bureaus of a borrower's overall credit history. A credit rating is also known as an evaluation of a potential borrower's ability to repay debt, prepared by a credit bureau at the request of the lender. Credit ratings are calculated from financial history and current assets and liabilities. Typically, a credit rating tells a lender or investor the probability of the subject being able to pay back a loan. However, in recent years, credit ratings have also been used to adjust insurance premiums, determine employment eligibility, and establish the amount of a utility or leasing deposit.

A poor credit rating indicates a high risk of defaulting on a loan, and thus leads to high interest rates, or the refusal of a loan by the creditor.

Distribution of wealth

The *distribution of wealth* is a comparison of the wealth of various members or groups in a society. It differs from the distribution of income in that it looks at the distribution of ownership of the assets in a society, rather than then current income of members of that society.

Wealth is a person's net worth, expressed as:

Wealth = assets – liabilities

The word 'wealth' is often confused with 'income'. These two terms describe different but related things. Wealth consists of those items of economic value that an individual owns, while income is an inflow of items of economic value.

Table 1. Country risk rankings (March 2010). Least risk countries; score out of 100.

Rank	Previous	Country	Overall score
1	1	Norway	94.05
2	2	Luxembourg	92.35
3	3	Switzerland	90.65
4	4	Denmark	88.55
5	6	Finland	87.81
6	5	Sweden	86.81
7	7	Austria	86.50
8	11	Canada	86.09
9	8	The Netherlands	84.86
10	9	Australia	84.16

Source: Euromoney Country Risk, March 2010

Further information

A useful source on information on economic terms is the Economist at: www.economist.com/economics-a-to-z

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Designed and produced by WEDC

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