THE WEALTH OF STATES: FROM GROWTH TO DEVELOPMENT

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Contents

Introduction

The vast span of human existence has been defined by poverty, with little economic growth and development. Throughout history, most people only able to earn enough income to support their basic needs, but thanks to the phenomenon in economic growth and development in the last two centuries, many countries benefit significantly by accumulating more wealth and made the residents in their territory prosperity as well.

According to the definition, wealth is the abundance of valuable financial assets or physical possessions that can be converted into a form that can be used for transactions. Moreover, a state is a territory delimited by borders and governed by the law, which is specific to it.

From this perspective, we can ask how a state can become wealthier, along with the abundance of economic growth and development?

To answer this question precisely, we will discuss economic growth based on the theory and measurement of growth in chapter one. On the other hand, we will be going through the theory of development economics in the second chapter. In the third chapter, we will present a summary and conclude our dissertation.

Chapter One: Economic Growth

Economic growth is a phenomenon of market productivity and increases in GDP, and there are theories of growth proposed by Adam Smith and John Stuart Mill and the measurement of growth presented by Simon Kuznets.

Adam Smith, considered as one of the most influential economists, argued that by letting people to freely produce and exchange whatever goods, as they please and enable the markets to be domestic and foreign competition, the self-interest of people, will promote greater prosperity and growth a lot more than with strict government regulations and interventions. In his masterpiece work, The Wealth of Nations, Smith strongly opposed the view of the mercantilist, namely zero-sum game in which one nation gain at the expense of another nation and where stocks of gold and silver in the state treasury is the primary indicator of wealth. Moreover, Smith developed the concept of a stationary state of an economy in which he believed that sooner or later, the national economy in the world will reach a final state of stationarity. Nevertheless, John Stuart Mill was argued that a stationary state could be a period of learning. He added that if it is a state that capital and population stay the same, but it is not applied to human improvement. There would still be moral and social progress while keep improving the art of living. He believed that the distribution of income would be more qualified, and everyone will be more responsible in their consumption even there is zero economic and population growth. In terms of view on the role of government in the economy, Mill favors government intervention to prevent consumers and workers from harmful products and working conditions, protect the environment, promote education, and tighten natural monopolies.

At the Bretton Woods agreements, in 1946, three measurement methods to calculate the accumulation of wealth were introduced by Simon Kuznets. The first one is the calculation of gross domestic product, which focuses on the value-added calculation. It adequately describes the industry activity of a country, especially if it is an exporting country that has a robust industrial action or it is a non-developed market and in favor of the international market because it takes in to account the added value of the whole production. In this calculation, current taxes and import taxes are included, but state expenditure is excluded from the trade balance. The second method is not common, namely the resident accounting system, which takes into consideration all of the expenses made by economic agents in society. Gross operating surplus is the third method that is focusing on income. This method is popularized among advanced economy countries by taking reference to the profit made by the financial sector and hidden the loss of their industrial activities. This way of calculating consumption is measured by social charges paid by companies, and industrial action is indicated by the import taxes.

Amartya Sen, an Indian economist, describes economic growth as one aspect of the process of economic development. So, in the next chapter, we will discuss in detail about economic development.

Chapter Two: Theory of Development Economics

Economic development is a process of growth and change that ultimately aimed to raise the living standards of people. It is accompanied by fundamental changes in the structure of an economy and consists of an increase in total and per capita income. In this theory of development economics section, the short-term and long-term development curve and the state's duty for economic development will be mentioned in the dept.

According to Simon Kuznets's theories to explain the challenges of economic development, he introduced a hypothetical graph called the environmental Kuznets curve that divides the economy into three phases. The first phase, namely pre-industrial economy in which correspondent to the calculation of wealth by taking into account value-added, when an economy's objective is to increase the product supply, reflecting the integration of a country into the international economy. In this scenario, Kuznets encourages the state to open the economy that aims to gain the advantages of trade balance and added value. The Kuznets curve implies that as a nation reached the second phase, which is called the industrialized economy, the domestic market is matured enough to support growth, and the industry is in a peak situated in the country. As a certain level of average income is achieved, environmental degradation will fall, and the rise of rapid growth and income per capital will follow. The method of calculation by expenditure will be used in this phase, so in this situation, the state needs to implement a short-term stimulus policy along with the regulation of monetary circuits to support the growth and retain capital inside the national economy. The third phase is called the post-industrial economy, which indicated that the economy had transferred its heavy reliance to the service sector from the industrial sector. In this case, we will calculate the wealth accumulation based on the income from the net profit made by financial companies. The growth rate in this stage is minimal but represents a specific development in the advanced economies. Kuznets encourages the government to implement interventionist policy have to adjudicate the economy.

Came to the state's duty for economic development, Nicholas Kaldor recommended four main goals for the state to follow in order to promote economic development, such as GDP growth, trade balance, inflation, and unemployment. He also added that the aim of full employment as an indicator of economic development. However, these four objectives are contradictory to one another, so achieving these four goals at once can be considered as impossible. For instance, in order to decrease the unemployment rate, the state needs to implement a recovery policy that will increase the demand and ultimately increase the total money supply, leading to triggering inflation. Plus, the national currency will lose its value thanks to the inflation that will endure the pain to price competitiveness on the trade balance. Moreover, inflation also causes a rapid dropped in household consumption; thus will have an impact on growth.

All in all, the state needs to make the critical move with high cautious about implementing the right policies in different phases of the economy. Plus, the state needs to remain neutral and make rational decisions to optimize the chances of achieving an inner balance of Kaldor's magic square that we mentioned earlier.

Conclusion

The growth theory in chapter one, part one which presented by John Stuart Mill is preferable than Adam Smith ideas because it is still the right approach up to date that the government intervention in some cases are very critical that only the state has the ability and authorization to take in charge effectively. On the other hand, the second main idea proposed by Simon Kuznets on how we can calculate economic growth through three different approaches is still legitimate and still seen as the tool to measure the nation's growth.

In the second chapter, the first main idea introduced by Simon Kuznets is also significantly crucial until these days because he had illustrated the different stages that a nation goes through as its economy keeps progressing from pre-industrialized economy to industrialized economy and finally to a post-industrial economy. The second main idea in this chapter mentioned by Nicholas Kaldor's magic square is remaining genuinely fundamental goals of the state to achieve economic development.

More importantly, the way that states can become wealthier, along with the abundance of economic growth and development, is first to have a dedicated government that fully engages and intervention whenever necessary to prevent corruption and calamities. Then the nation itself has to know the leading contribution indicator to the growth. By studying from the past data, it can gain insight from previous experience and can predict the main future contribution of growth. Then the state can entirely focus on the development of the economy, by first addressing the position of itself in which phase it is staying, so it can implement the right move. Thus, the state needs to be aware of the main objectives, the so-called Kaldor's magic square.

In summary, this topic has provided a concrete explanation of how a nation can measure its economic growth and how it can develop its economy that aims to make all the people live in a prosperous life in the territory. Final thoughts on this subject are that economic development encompasses more than just Kaldor's magic square. Other essential elements are also genuinely important such as the alleviation of poverty and the increase in the average levels of education, nutrition, and health condition.

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