Gross domestic product

Economics

Economy and politics are strongly related because politicians need to make decisions that would affect the people. Economy, on the other hand, describes the status of the people in a certain country. Therefore, economical measurement tools are heavily used by politicians for decision making. These tools would also work like alerts for a change in the economy status that would help in conducting proactive decisions. GDP is a strong example of such tools.

Moreover, for any investor or creditor, it is important to know the economical status of the party that he is going to credit or invest his money with, and the environment that he will put his money in. For the first case, financial statements are used to reflect the economical status of the company. However, when it comes to measure the financial and economical status of the environment, such as a country, a region or even a nation, the role of economical status measurement tools or indicators shows its importance. One of the most important and correct tools is GDP.

In the following papers we will take a tour in the world of GDP where we will define GDP. Then we will show the two ways in which we can measure GDP in a certain country. Finally we will show the shortfalls of measuring industrialized countries' GDP in oppose of developing countries' GDP and we will demonstrate this using two example countries, Germany as an Industrialized country vs. Saudi Arabia as a developing country.

What is GDP?

Gross Domestic Products, or GDP, is defined by economics as " the total market value of all final goods and services produced in a country in a given time period”. We will stop at important parts of the definition to clarify the meaning of GDP.

Gross means before subtracting the depreciation of capital. The opposite of “ gross” is net, which means after subtracting the depreciation of capital. This word is important as it means that for the our calculation we are looking for the gross amount not the net amount of either expenditure or income.

One key phrase in the definition is " final goods", which means the goods that are consumed by the end user, wither the end user is a person or an organization, and does not require any further processing. GDP of a certain country can be thought of as the size of its economy.

Another key phrase in the definition is “ produced in a country”. GDP will only consider the goods and services produced inside the country. It will not consider any goods or services produced outside the country boarders even if it is owned by one of its citizens. For example, even though Toyota is a Japanese corporation, its products are calculated in the U. S. GDP because Toyota cars are produced in the U. S.

GDP is calculated quarterly. Each quarter's GDP is compared against the previous quarter’s GDP. If there is a positive difference, it means that the economy has enhanced over the past three months. If the difference is negative, it is considered as an alarm that the economy is facing troubles and needs to be taking care of. If the difference is zero, then that would mean that the economy was stable during the past three months. Three consecutive decreases in the quarterly GDP would indicate a possibility of a recession period that a country would enter. It is not always good to have a high GDP because it might be an indicator of inflation which can be solved via different means like increasing taxes rates.