6.24: Relatively Recent Economic Growth

Learning Objectives

- Explain the conditions that have allowed for modern economic growth in the last two centuries

Global Economic Growth

Every country worries about economic growth. In the United States and other high-income countries, the question is whether economic growth continues to provide the same remarkable gains in our standard of living as it did during the twentieth century. Meanwhile, can middle-income countries like South Korea, Brazil, Egypt, or Poland catch up to the higher-income countries? Or must they remain in the second tier of per capita income? Of the world's population of roughly 6.7 billion people, about 2.6 billion are scraping by on incomes that average less than $2 per day, not that different from the standard of living 2,000 years ago. Can the world's poor be lifted from their fearful poverty? As the 1995 Nobel laureate in economics, Robert E. Lucas Jr., once noted: "The consequences for human welfare involved in questions like these are simply staggering: Once one starts to think about them, it is hard to think about anything else."

Dramatic improvements in a nation's standard of living are possible. After the Korean War in the late 1950s, the Republic of Korea, often called South Korea, was one of the poorest economies in the world. Most South Koreans worked in peasant agriculture. From the 1960s to the early twenty-first century, a time period well within the lifetime and memory of many adults, the South Korean economy grew rapidly. Over these four decades, GDP per capita increased by more than 6% per year. GDP for South Korea now exceeds $30,000 in nominal terms, placing it firmly among high-income countries like Italy, New Zealand, and Israel. Measured by total GDP in 2012, South Korea is the thirteenth-largest economy in the world. For a nation of 49 million people, this transformation is extraordinary.

South Korea is a standout example, but it is not the only case of rapid and sustained economic growth. Other nations of East Asia, like Thailand and Indonesia, have seen very rapid growth as well. China has grown enormously since market-oriented economic reforms were enacted around 1980. GDP per capita in high-income economies like the United States also has grown dramatically albeit over a longer time frame. Since the Civil War, the U.S. economy has been transformed from a primarily rural and agricultural economy to an economy based on services, manufacturing, and technology.

The Relatively Recent Arrival of Economic Growth

Let's begin with a brief overview of the spectacular patterns of economic growth around the world in the last two centuries, commonly referred to as the period of **modern economic growth**. Rapid and sustained economic growth is a relatively recent experience for the human race. Before the last two centuries, although rulers, nobles, and conquerors could afford some extravagances and although economies rose above the subsistence level, the average person's standard of living had not changed much for centuries.

Progressive, powerful economic and institutional changes started to have a significant effect in the late eighteenth and early nineteenth centuries. According to the Dutch economic historian Jan Luiten van Zanden, slavery-based societies, favorable demographics, global trading routes, and standardized trading institutions that spread with different empires set the stage for the Industrial Revolution to succeed. The **Industrial Revolution** refers to the widespread use of power-driven machinery and the economic and social changes that resulted in the first half of the 1800s. Ingenious machines—the steam engine, the power loom, and the steam locomotive—performed tasks that otherwise would have taken vast numbers of workers to do. The Industrial Revolution began in Great Britain, and soon spread to the United States, Germany, and other countries.

The jobs for ordinary people working with these machines were often dirty and dangerous by modern standards, but the alternative jobs of that time in peasant agriculture and small-village industry were often dirty and dangerous, too. The new jobs of the Industrial Revolution typically offered higher pay and a chance for social mobility. A self-reinforcing cycle began: new inventions and investments generated profits, the profits provided funds for new investment and inventions, and the investments and inventions provided opportunities for further profits. Slowly, a group of national economies in Europe and North America emerged from centuries of sluggishness into a period of rapid modern growth. During the last two centuries, the average rate of growth of GDP per capita in the leading industrialized countries has averaged about 2% per year. What were times like before then? Read on for the answer.

Try It

Angus Maddison, a quantitative economic historian, led the most systematic inquiry into national incomes before 1870. His methods recently have been refined and used to compile GDP per capita estimates from year 1 C.E. to 1348. Table 1 is an important counterpoint to most of the narrative in this section. It shows that nations can decline as well as rise. The declines in income are explained by a wide array of forces, such as epidemics, natural and weather-related disasters, the inability to govern large empires, and the remarkably slow pace of technological and institutional progress. Institutions are the traditions, laws, and so on by which people in a community agree to behave and govern themselves. Such institutions include marriage, religion, education, and laws of governance. Institutional progress is the development and codification of these institutions to reinforce social order, and thus, economic growth.

One example of such an institution is the Magna Carta (Great Charter), which the English nobles forced King John to sign in 1215. The Magna Carta codified the principles of due process, whereby a free man could not be penalized unless his peers had made a lawful judgment against him. This concept was later adopted by the United States in its own constitution. This social order may have contributed to England's GDP per capita in 1348, which was second to that of northern Italy.

In the study of economic growth, a country's institutional framework plays a critical role. Table 1 also shows relative global equality for almost 1,300 years. After this, we begin to see significant divergence in income (not shown in table).

Table 1. GDP Per Capita Estimates in Current International Dollars from AD 1 to 1348

Year	Northern Italy	Spain	England	Holland	Byzantium	Iraq	Egypt	Japan
1	$800	$600	$600	$600	$700	$700	$700	–
730	–	–	–	–	–	$920	$730	$402
1000	–	–	–	–	$600	$820	$600	–
1150	–	–	–	–	$580	$680	$660	$520
1280	–	–	–	–	–	–	$670	$527
1300	$1,588	$864	$892	–	–	–	$610	–
1348	$1,486	$907	$919	–	–	–	–	–

(Source: Bolt and van Zanden. "The First Update of the Maddison Project. Re-Estimating Growth Before 1820." 2013)

Another fascinating and underreported fact is the high levels of income, compared to others at that time, attained by the Islamic Empire Abbasid Caliphate—which was founded in present-day Iraq in 730 C.E. At its height, the empire spanned large regions of the Middle East, North Africa, and Spain until its gradual decline over 200 years.

The Industrial Revolution led to increasing inequality among nations. Some economies took off, whereas others, like many of those in Africa or Asia, remained close to a subsistence standard of living. General calculations show that the 17 countries of the world with the most-developed economies had, on average, 2.4 times the GDP per capita of the world's poorest economies in 1870. By 1960, the most developed economies had 4.2 times the GDP per capita of the poorest economies.

However, by the middle of the twentieth century, some countries had shown that catching up was possible. Japan's economic growth expanded in the 1960s and 1970s, with a growth rate of real GDP per capita averaging 11% per year during those decades. Certain countries in Latin America experienced a boom in economic growth in the 1960s as well. In Brazil, for example, GDP per capita expanded by an average annual rate of 11.1% from 1968 to 1973. In the 1970s, some East Asian economies, including South Korea, Thailand, and Taiwan, saw rapid growth. In these countries, growth rates of 11% to 12% per year in GDP per capita were not uncommon. More recently, China, with its population of 1.3 billion people, grew at a per capita rate 9% per year from 1984 into the 2000s. India, with a population of 1.1 billion, has shown promising signs of economic growth, with growth in GDP per capita of about 4% per year during the 1990s and climbing toward 7% to 8% per year in the 2000s.

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These waves of catch-up economic growth have not reached all shores. In certain African countries like Niger, Tanzania, and Sudan, for example, GDP per capita at the start of the 2000s was still less than $300, not much higher than it was in the nineteenth century and for centuries before that. In the context of the overall situation of low-income people around the world, the good economic news from China (population: 1.3 billion) and India (population: 1.1 billion) is, nonetheless, astounding and heartening.

Economic growth in the last two centuries has made a striking change in the human condition. *Richard Easterlin*, an economist at the University of Southern California, wrote in 2000:

By many measures, a revolution in the human condition is sweeping the world. Most people today are better fed, clothed, and housed than their predecessors two centuries ago. They are healthier, live longer, and are better educated. Women's lives are less centered on reproduction and political democracy has gained a foothold. Although Western Europe and its offshoots have been the leaders of this advance, most of the less developed nations have joined in during the 20th century, with the newly emerging nations of sub-Saharan Africa the latest to participate. Although the picture is not one of universal progress, it is the greatest advance in the human condition of the world's population ever achieved in such a brief span of time.

Learning Objectives

[glossary-page][glossary-term]Industrial Revolution: [/glossary-term][glossary-definition]the widespread use of power-driven machinery and the economic and social changes that occurred in the first half of the 1800s[/glossary-definition] [glossary-term]modern economic growth: [/glossary-term][glossary-definition]the period of rapid economic growth from 1870 onward[/glossary-definition][/glossary-page]

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