What is GDP? [The Impact of Demand and Investment on GDP]

Gross Domestic Product (GDP) is the main measure of economic growth, showing whether the economy is in a boom or a **recession**. Central banks use this concept to set **monetary policies**.

Moreover, traders can use **GDP** and its calculation method to assess and identify whether the economy is experiencing a boom or recession.

This concept is also applied in **economic inflation** analysis, **labor markets**, **monetary policies**, and **financial markets**.



Gross Domestic Product represents all goods produced within a specific time period in a country

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What is GDP?

Gross Domestic Product (GDP) is the total value of **all final goods** and **services produced** in a countrythin a specific time frame.

GDP is one of the most important **production indicators** and a key measure of **economic growth**.

Key Points in Calculating GDP

Certain goods (including housework, charitable services, and illegal goods) are not included in GDP calculations. Only the value of **final goods** is considered in GDP.

Calculation of Final Goods Value

To prevent double-counting, only the value of final goods is included in GDP calculations.

For example, if the price of flour is counted separately in **GDP** when making bread, and then the price of the bread (the final product) is included again, **the value of flour is counted twice**.

This repetition leads to a decrease in the accuracy of the statistics.

Importance of Borders in GDP

Borders matter in GDP; only goods produced within the country are included. For instance, consider Apple, an American company.

If Apple produces a product in **China**, the value of the product produced will be counted in **China's GDP**!

Exclusion of Certain Productions in GDP

Goods produced and **traded illegally** (such as drugs), **second-hand goods**, **securities**, and **housework** or charitable activities are not included in GDP.

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What is GNP and How Does it Differ from GDP?

Gross National Product (GNP) includes the total value of goods produced by companies owned by the citizens of a country.

For example, if Nike produces goods in **China**, the final value of the products will be included in the **U.S. GNP**.

Similarly, investments made by citizens outside the country will be included in the **GNP**. The formula for calculating GNP is shown below:



GNP equals the sum of national production abroad and GDP, minus foreign production within the country

Difference in Concept

The primary difference between **GDP** and **GNP** lies in the goods included in their calculations. In GDP, **borders matter**, and only goods produced within the country are considered, regardless of nationality.

However, nationality is important in **GNP**, and **all national goods**, regardless of where they are produced, are considered.

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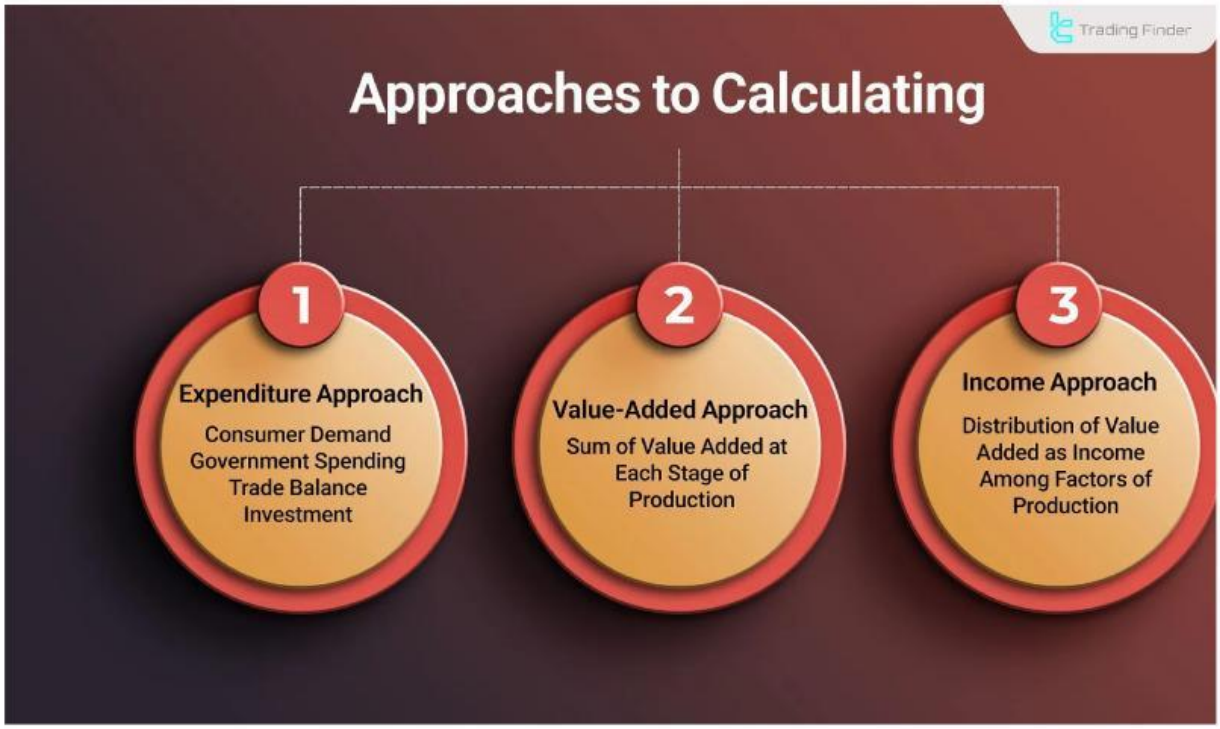
Difference in Function

GDP is mainly used to assess **economic activity** (whether in a recession or a boom), while GNP indicates the degree of dependence and profit a country gains from foreign resources.

Thus, if a country focuses more on foreign **investment**, it will likely to have a higher **GNP** than GDP. However, if the country is dependent on foreign investment, its **GDP** will likely be higher than its GNP.

How is GDP Calculated?

Since GDP only accounts for the value of final goods and services (excluding intermediate goods), there are **three** methods for calculating GDP:



An overview of the approaches to calculating Gross Domestic Product

Expenditure Approach

Four components in the expenditure approach influence GDP. This method is the most common and widely used for calculating GDP.

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This formula is based on **classical economic** theory, which assumes that all goods produced in the economy are **consumed**.

Therefore, according to this theory, the value of produced goods can be derived from the total expenditure by consumers, the **government**, and **investments**.

In other words, four factors are considered in the GDP calculation formula:



The expenditure approach to calculating GDP includes four components: investment, net exports, consumer spending, and government spending

- **Consumer Expenditures**: The amount households spend on goods and services;
- **Government Expenditures**: The amount the government spends on public services and benefits;
- **Investment in Production**: The costs spent on capital goods and investments in production;
- **Trade Balance**: The net value of imports and exports.

Value-Added Approach

In this approach, the value added at each **production stage** is summed up. In this method, the full value of goods produced without intermediates is considered in GDP. Finally, by summing up the value added at each production stage, the price of the final product is determined.

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Income Approach

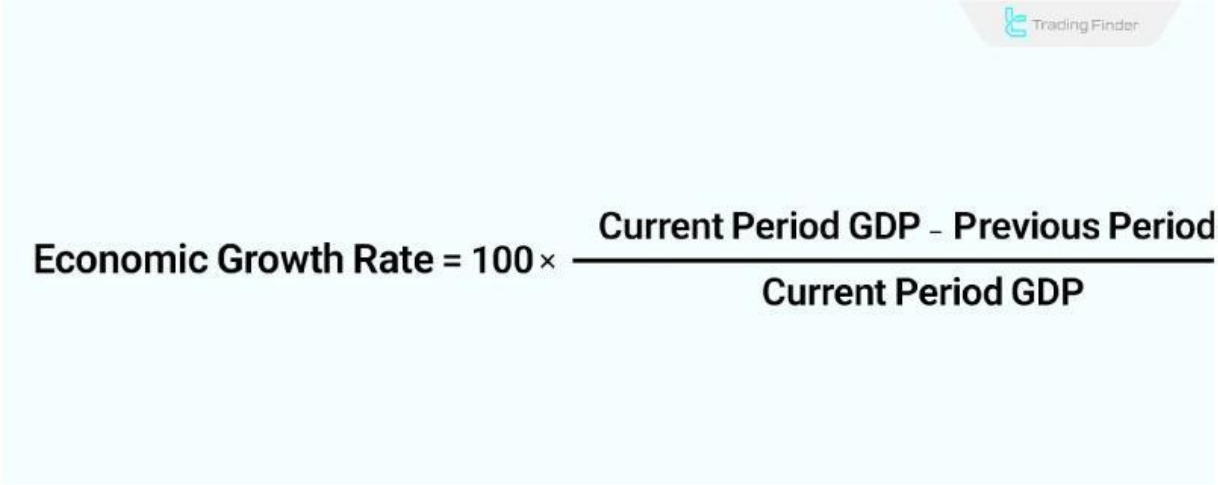
The added value of production is distributed as income among production factors. Therefore, the total income can be used to calculate the added value or the total value of **goods produced**.

Gross Domestic Income (GDI) reports can be used to track income distribution flow, identifying the sectors of the economy with the largest share of production.

What is Negative Economic Growth?

If GDP is lower in the current period compared to the previous period, the economy is experiencing negative economic growth.

The formula for calculating the economic growth rate is:



The economic growth rate (Gross Domestic Product) is calculated using this formula

According to this formula, if the GDP of the current period is less than the previous period, the **economic growth** rate will be negative.

Negative economic growth means that the total value of domestic production in the current period is **lower than** it was in the previous period.

Key points on negative economic growth:

- A decrease in economic growth is different from negative economic growth;
- According to the definition, if two consecutive quarters show negative economic growth, the economy is in a recession;

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- During negative economic growth, **market sentiment** in financial markets shifts towards risk aversion.

Importance of Real GDP

GDP calculates the total value (price) of all produced goods. Therefore, if goods become more expensive due to inflation, GDP will also increase, but this does not necessarily mean economic growth.

Central banks use Real GDP in their calculations to eliminate the effects of inflation in measuring economic growth.

Conclusion

Gross Domestic Product (GDP) is the primary measure of **economic growth** and the **health of production**, and central banks use it for decisions related to monetary policy.

In **fundamental analysis**, **Real GDP** is used to compare the countries' economic growth, as **Real GDP** eliminates the inflationary effects from the total value of goods produced.

Source:
1.our website link :
https://tradingfinder.com/education/forex/what-is-gdp/

2.all Education :
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