



GDP and Indicators of Economic Wellbeing

Sound Byte

At this point in history, increasing economic activity does more harm than good, so we need to adopt new indicators of wellbeing such as the Genuine Progress Indicator.

GDP and Its Discontents

For many years, especially since World War II, nations have equated economic growth with progress. Economic growth is an increase in the production and consumption of goods and services, and is indicated by increasing Gross Domestic Product (GDP). GDP, therefore, has become the standard measure of economic progress, even though it was only intended as a macroeconomic accounting tool. Prompted by Wall Street, the Federal Reserve System, and the media, citizens generally applaud increases in GDP.

The problem with GDP is that it doesn't separate costs from benefits. It simply adds them together under the heading of economic activity. In a 1968 campaign speech, Robert F. Kennedy eloquently explained the shortcomings of using GDP to gauge progress. Is increasing GDP indicative of increasing wellbeing? It depends on whether the social costs of such an increase outweigh the benefits. GDP is a good measure of size, but at some point bigger is worse, not better.

At the individual level, economic activity is required for wellbeing, but the relationship becomes very weak after a surprisingly low per capita GDP is achieved. Beyond that, the "disutility" of production and consumption causes a net drain on health and happiness.

GDP also has nothing to say about how income and wealth are distributed among the people. Does increasing GDP indicate progress if the increasing income accrues to a very small number of people? Of course not!



Speech Excerpt by Robert F. Kennedy (1968)

Too much and for too long, we seem to have surrendered personal excellence and community value in the mere accumulation of material things. Our Gross National Product counts air pollution and cigarette advertising and ambulances to clear our highways of carnage. It counts special locks for our doors and the jails for the people who break them. It counts the destruction of the redwoods and the loss of our natural wonder in chaotic sprawl. It counts napalm and it counts nuclear warheads, and armored cars for the police to fight riots in our cities.

Yet the Gross National Product does not allow for the health of our children, the quality of their education, or the joy of their play. It does not include the beauty of our poetry or the strength of our marriages, the intelligence of our public debate or the integrity of our public officials. It measures neither our wit nor our courage, neither our wisdom nor our learning, neither our compassion nor our devotion to our country; it measures everything, in short, except that which makes life worthwhile.

Alternatives for Measuring Economic Progress

As the adage goes, “we manage what we measure.” Nations, therefore, would be wise to start measuring what they truly value. Do we value growth at all costs? Simon Kuznets, the Nobel laureate who developed GDP measurement, warned the U.S. Congress in 1934 that “The welfare of a nation can scarcely be inferred from a measurement of national income.” Let’s look at some alternatives, then...

Human Development Index (Source: United Nations Development Programme)

HDI measures a nation’s achievement in three dimensions of human development: long and healthy life (indicated by life expectancy at birth), knowledge (indicated by literacy and school enrollment rates), and decent standard of living (indicated by GDP per capita). Although the first two components of HDI address specific societal goals, the GDP component remains an inadequate proxy for wellbeing.

Genuine Progress Indicator (Source: Redefining Progress)

GPI is a refined version of the Index of Sustainable Economic Welfare developed by Herman Daly and John Cobb in the late 1980s. GPI starts with the same personal consumption data as GDP, but then makes some crucial distinctions. It adjusts for factors such as income distribution, adds factors such as the value of household and volunteer work, and subtracts factors such as the costs of crime and pollution.

Ecological Footprint (Source: Global Footprint Network)

The Ecological Footprint measures how much land and water area a human population requires to produce the resources it consumes and to absorb its wastes under prevailing technology. In the mid to late 1980s, the global Ecological Footprint surpassed the capacity of the planet.

Happy Planet Index (Source: New Economics Foundation)

HPI measures the ecological efficiency with which human wellbeing is delivered. It is calculated by multiplying indices of life satisfaction (estimated by compiling responses to international surveys) and life expectancy, and dividing that product by ecological footprint. Nations score well when they achieve high levels of satisfaction and health while impacting environmental resources lightly.

Making the Switch

A quick survey of economic and ecological news from around the world demonstrates that human economies have entered a phase of growth in which costs are mounting faster than benefits. Evidence of these costs takes the form of climate disruption, species extinctions, intense competition for natural resources, declining ecological services, widespread unemployment and poverty, and massive inequity in the distribution of wealth. The global economy and GDP of many nations have grown consistently for years, but human wellbeing and ecological health haven’t kept pace. It is time to put to rest the unfounded assumption that increasing GDP equates to economic progress.

National accounts need an overhaul, but statisticians don’t have to start from scratch. They can add to existing accounts by institutionalizing and publicizing alternative measures. Right now, these indicators are typically compiled by small nonprofit organizations, but government agencies like the U.S. Bureau of Economic Analysis could adopt them as part of their standard suite of indicators. Imagine regular reports on the Ecological Footprint, HPI, and other indicators of progress alongside those that depict income and financial returns. Policy makers and citizens will obtain a more comprehensive picture of economic progress and use more appropriate information to manage their economies for long-term prosperity.

Czech, Brian et al. 2005. Establishing Indicators for Biodiversity. *Science* 308:791-792.
Daly, Herman and J. B. Cobb Jr. 1994. *For the Common Good*. Beacon Press, Boston, Massachusetts. 534pp.

Sources

Global Footprint Network. 2009. Data and Results Website. <http://www.footprintnetwork.org>.
Landefeld, J. S. et al. 2008. Taking the Pulse of the Economy. *Journal of Economic Perspectives*, 22(2): 193-216.
Marks, N. et al. 2006. *The Happy Planet Index*. New Economics Foundation. 57pp.
Talberth, J. et al. 2006. *The Genuine Progress Indicator 2006: A Tool for Sustainable Development*. Redefining Progress.
United Nations Development Programme. 2009. Statistics Website. <http://hdr.undp.org/en/statistics/>.
Victor, P. 2008. *Managing without Growth: Slower by Design, Not Disaster*. Edward Elgar Publishing. 260pp.