

## GDP Fetishism

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Striving to revive the world economy while simultaneously responding to the global climate crisis has raised a knotty question: Are statistics giving us the right "signals" about what to do? In our performance-oriented world, measurement issues have taken on increased importance: What we measure affects what we do.

If we have poor measures, what we strive to do (say, increase GDP) may actually contribute to a worsening of living standards. We may also be confronted with false choices, seeing trade-offs between output and environmental protection that don't exist. By

contrast, a better measure of economic performance might show that steps taken to improve the environment are good for the economy.

Eighteen months ago, French President Nicolas Sarkozy established an international [Commission on the Measurement of Economic Performance and Social Progress](#), owing to his dissatisfaction—and that of many others—with the current state of statistical information about the economy and society. On September 14, the Commission issued its long-awaited [report](#).

The big question concerns whether GDP provides a good measure of living standards. In many cases, GDP statistics *seem* to suggest that the economy is doing far better than most citizens' own perceptions. Moreover, the focus on GDP creates conflicts: Political leaders are told to maximize it, but citizens also demand that attention be paid to enhancing security, reducing air, water, and noise pollution, and so forth—all of which might lower GDP growth.

The fact that GDP may be a poor measure of well-being, or even of market activity, has, of course, long been recognized. But changes in society and the economy may have heightened the problems, at the same time that advances in economics and statistical techniques may have provided opportunities to improve our metrics.

For example, while GDP is supposed to measure the value of output of goods and services, in one key sector—government—we typically have no way of doing it, so we often measure the output simply by the inputs. If government spends more—even if inefficiently—output goes up. In the last 60 years, the share of government output in GDP has increased from 21.4 percent to 38.6 percent in the United States, from 27.6 percent to 52.7 percent in France, from 34.2 percent to 47.6 percent in the United Kingdom, and from 30.4 percent to 44.0 percent in Germany. So what was a relatively minor problem has now become a major one.

Likewise, quality improvements—say, better cars rather than just more cars—account for much of the increase in GDP nowadays. But assessing quality

improvements is difficult. Health care exemplifies this problem: Much of medicine is publicly provided, and much of the advances are in quality.

The same problems in making comparisons over time apply to comparisons across countries. The United States spends more on health care than any other country (both per capita and as a percentage of income), but gets poorer outcomes. Part of the difference between GDP per capita in the United States and some European countries may thus be a result of the way we measure things.

Another marked change in most societies is an increase in inequality. This means that there is increasing disparity between average (mean) income and the median income (that of the "typical" person, whose income lies in the middle of the distribution of all incomes). If a few bankers get much richer, average income can go up, even as most individuals' incomes are declining. So GDP per capita statistics may not reflect what is happening to most citizens.

We use market prices to value goods and services. But now, even those with the most faith in markets question reliance on market prices, as they argue against mark-to-market valuations. The pre-crisis profits of banks—one-third of all corporate profits—appear to have been a mirage.

This realization casts a new light not only on our measures of performance, but also on the inferences we make. Before the crisis, when U.S. growth (using standard GDP measures) seemed so much stronger than that of Europe, many Europeans argued that Europe should adopt U.S.-style capitalism. Of course, anyone who wanted to could have seen American households' growing indebtedness, which would have gone a long way toward correcting the false impression of success given by the GDP statistic.

Recent methodological advances have enabled us to assess better what contributes to citizens' sense of well-being, and to gather the data needed to make such assessments on a regular basis. These studies, for instance, verify and quantify what should be obvious: The loss of a job has a greater impact than can be accounted for just by the loss of income. They also demonstrate the importance of social connectedness.

Any good measure of how well we are doing must also take account of sustainability. Just as a firm needs to measure the depreciation of its capital, so, too, our national accounts need to reflect the depletion of natural resources and the degradation of our environment.

Statistical frameworks are intended to summarize what is going on in our complex society in a few easily interpretable numbers. It should have been obvious that one couldn't reduce everything to a single number, GDP. The report by the Commission on the Measurement of Economic Performance and Social Progress will, one hopes, lead to a better understanding of the uses, and abuses, of that statistic.

The report should also provide guidance for creating a broader set of indicators that more accurately capture both well-being and sustainability; and it should provide impetus for improving the ability of GDP and related statistics to assess the performance of the economy and society. Such reforms will help us direct our efforts (and resources) in ways that lead to improvement in both.

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