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Will the Great Recession finally end our misguided obsession with gross domestic product?

by *Megan McArdle*

Misleading Indicator

HERE'S A QUESTION no one ever asks about the Great Recession: How do we even know it's happening? Daily, almost, someone releases employment figures, production estimates, consumer-confidence indexes—almost all of them bad. There's no need to wonder what's happening when information about everyone's problems constantly streams across your TV screen.

And in this dolorous statistical parade, no number is quite so central to public life as the gross domestic product. Political scientists build formulas around it to predict who will win the presidency. The stock market trembles at the approach of new quarterly figures. Other economic statistics, like budget deficits or health-care spending, are quoted as percentages of GDP. It has become the common denominator of economic well-being.

But GDP's broad dominion has long had its critics. It was never meant to be the measure of our well-being, they say, only the measure of our production—literally, the total value of the goods and services produced within the national borders in a given year. While the quest for some broader measure of progress has been going on for a while (more than a decade ago, for example, *The Atlantic* was running articles like “[If the GDP Is Up, Why Is America Down?](#)”), it may finally be gaining traction at a time when people understand, as never before, how easily GDP and well-being can diverge.

One of the leaders of a huge global effort to build a better statistical yardstick has been Enrico Giovannini, until recently the chief statistician of the Organization for Economic Cooperation and Development. Though the OECD is the global coordinator of the project, its partners represent a who's who of economic development: the World Bank, various UN programs, the African Development Bank, and the European Commission. They are looking to create more-reliable metrics for measuring change in our health, education, the environment—the many ways that human beings make themselves better off or worse off. This fall, in the wake of the OECD's third World Forum on Statistics, Knowledge, and Policy, these groups are set to move ahead on a broader, better set of indexes.

Crisis seems to be the mother of statistics. The germ of the idea that eventually became GDP emerged after World War I, when American economists who had been frustrated by the lack of reliable statistics to guide war production founded the National Bureau of Economic Research (despite its name, the NBER is a private organization). Still, not until the Great Depression did we finally get our first national income accounts, which measured the annual income of people, companies,

and the government.

It is rare for people to write about that era without taking a swipe at Herbert Hoover, but we might be kinder if we remembered just how little information he had. With no national income accounts, Hoover had to rely on fragmentary indicators such as freight-car loadings, steel production, and the gyrations of the New York Stock Exchange. There weren't even comprehensive national unemployment statistics, because Congress didn't authorize the Department of Labor to collect them until the middle of 1930. Forget Hoover's economic theory, most of which was pretty bad; the man barely had any *data*.

Beyond newspaper anecdotes and a bunch of unrelated industrial indexes, he had little way of knowing just how awful things were or, more important, exactly where intervention might be needed. It's as if someone hired you to cater a lavish formal dinner—then gave you no head count, a partial list of available ingredients, and the July 1953 issue of *Gourmet* magazine to work with.

That started to change in 1932. The legendary progressive Senator Robert La Follette introduced a resolution that directed the secretary of commerce to estimate national income for the prior three years. Unable to find anyone in the department who was up to the task, Commerce hired Simon Kuznets, who had already begun working on the problem at the NBER. He spent the next 14 years creating a system of national accounts that, with constant refinements and additions, we still use today.

It's almost impossible to overstate what a titanic achievement this was. But here's something that hints at the magnitude of the difficulties: despite his earlier work, Kuznets didn't make the first tentative presentation of his figures to Congress until 1934. By 1941, he had expanded the series backward to 1919, and all the way to 1938. Measures of output—the true forerunners of GDP—didn't follow until 1942, as war production ramped up. (Total mobilization depended on extensive statistics, which is why the Nobel Prize winner Paul Samuelson called World War II “an economist's war.”) The Great Depression and World War II created the modern world in a lot of ways. They also created one of the primary lenses through which we view it.

Unfortunately, that lens is a trifle distorted. It counts the dollar value of our output, but not the actual improvement in our lives, or even in our economic condition.

Think about a house, any of the millions that were constructed during the bubble that burst in 2008. Let's make it a nice house: four bedrooms, 3.5 baths, with an attached garage and a quarter-acre lot. During its construction, that house did its own little bit to boost GDP. Lumber was purchased and swathed in fluttering robes of Tyvek. Tiles were pressed out of clay and nailed to the roof. Pipe was laid, glass was sealed into the window slots, granite was hewn from a Vermont mountain and shipped all the way to its kitchen counters. All of this output, which swelled GDP (at least to the tune of its purchase price), has ended up in ... nothing. The house, in an exurban cul-de-sac, sits empty while bankers, borrowers, and regulators squabble. One of the estimated 2.4million excess homes on the market, its only function right now is to bankrupt its owner.

GDP does not, and cannot, reflect the waste of enormous effort, and precious natural resources, that went into building something that suddenly no one wants. Moreover, it misses many other aspects of our existence. Strip-mining a picturesque mountaintop, or clear-cutting a primeval forest, shows up in GDP only as a boost to output. Meanwhile, in India's national accounts, all of Mother Teresa's labors among the poor would have had only the most minimal possible impact. GDP can record how much money we spend on health care or education; it cannot tell us whether the services we are buying are any good.

which is mathematically impossible.

Besides, much of the progress in important areas of life is invisible to most people. You are indisputably better off having the option of getting a liver transplant if you should need one. But unless your skin actually starts turning yellow, you probably never think about it.

The OECD project's daunting task is to find better ways to handle these kinds of obstacles. One possible approach is to focus on hard indicators that we can measure in a fairly standard way. But these are scarce for some aspects of life, and even when they exist, can be tricky to interpret. Life expectancy, for example, seems pretty objective. It's a metric on which the United States does relatively poorly, causing us endless consternation. A few years ago, however, the health-care economists Robert Ohsfeldt and John Schneider recalculated the numbers after controlling for deaths from homicides and traffic accidents. Because these things tend to strike very young people, they can have an outsize impact on mortality statistics. Those deaths reflect America's crime policy and its driving habits more than the effectiveness of its health-care system. And if you remove them from the picture, say Ohsfeldt and Schneider, America jumps to the top of the life-expectancy tables. Assuming they're correct, does America have good health, or bad? Neither answer is the obviously right one. Such conundrums will vex analysts long into the future.

But of course, measurement problems also bedevil GDP, which is why the U.S. Bureau of Economic Analysis employs economists and statisticians rather than bookkeepers. Whatever the difficulties, the OECD project's leaders, like their forebears during the Great Depression, are convinced of the urgent need to get a better handle on the progress our societies are making.

That sense of urgency doesn't mean we should look for speedy results. Even though his staff had to tabulate the results without the aid of computers, Kuznets and his team produced the first national accounts more rapidly than his successors will create the newer, better set of statistics they aspire to. For all the burdens under which Kuznets labored, he had one advantage: the absence of an existing economic establishment. He did not have to convene working groups and seminars to make sure that academics around the world and the staffs of dozens of institutions felt included. Nor, once he was finished, did he have to convince governments that they should care. Giovannini describes today's next step as developing "a framework that at least lists the domains that outline what this project should look like." That's several nouns away from any sort of working model.

It doesn't help that Giovannini has left the OECD to head Italy's statistics authority. But efforts like these have always been larger than one person. When our grandchildren face their financial Waterloo, they may have Giovannini's brainchildren to help guide them through it. But we will have to muddle through with the legacy of Kuznets and the generations of economists who expanded and improved on his remarkable achievement.

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