Back to GDP: What is the Value-Added of Potential New Components of Welfare Measurement?

Christoph M. Schmidt and Sonja C. Kassenböhmer

We investigate the value added for political interventions by the indices suggested by the growing economic literature on „Beyond GDP". While this literature on measuring welfare suggests that GDP alone is an inadequate measure and therefore suggests exploring other determinants apart from material well-being, such as job security, crime, health, environmental factors and subjective feelings concerning one's own situation, we investigate to what extent these factors are simply correlated with GDP. Should these additional factors simply be correlated with GDP, there would be no new additional informational content. To investigate this, we use macro data from the German Federal Statistical Office combined with aggregated German SOEP data (1991-2007) on the personal work situation and subjective feelings concerning several aspects of life. We use factor analysis to show that all variables suggested by the "Beyond GDP" movement can be reduced to one main underlying background variable which is near perfectly correlated with GDP (Corr=0,99). This factor explains already 74% of the variation shared by the variables and is mainly determined by measures of life expectancy and pollution, hence objective health indicators. Together with a second underlying factor reflecting certain subjective worries about such things as world peace and the overall standard of living, 89% of the total variation shared by the variables can be explained. The latter factor is only weakly correlated with GDP, indicating that GDP cannot alone reflect the current situation of a country. However since this latter factor only reflects the current general feeling of the population which can be influenced by many events (nationally and internationally) completely outside the scope of national public policy, this latter factor seems to be of minor importance. While there are some specific benefits in using subjective measures in some economic analyses for Western countries, we show that it cannot replace, but rather at best, only augment the informational content of hard general measures of welfare such as GDP.