Beyond GDP: From measurement to European economic governance

A briefing paper for the Expert Conference, organised by the European Commission in co-operation with the Italian Presidency of the Council of the European Union

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Executive summary

It is widely agreed that to achieve the aims of the European Union, as set out in the Treaty of Lisbon, gross domestic product (GDP) maximisation and market efficiency cannot be the sole objectives of economic policy. The question now is how to achieve the associated changes needed to economic policy making.

One part of the answer is to develop new measures of progress ‘Beyond GDP,’ as proposed by the Stiglitz Commission. The other is to use these measures in economic governance, and this forms the agenda for this conference.

This paper summarises findings from a European Commission funded project, which identified barriers to this, and draws conclusions for action in Europe.

First, the term ‘Beyond GDP’ needs to be defined. It does not mean that environmental and social ministries or directorates general (DGs) start to use environmental and social indicators alongside economic indicators, which happens in any case. It means instead that economic ministries and DGs start to use all these indicators as part of an integrated policy process, in a way that prevents traditional economic objectives (such as GDP growth) from trumping all others.

Barriers

1. **Lack of democratic legitimacy.** The indicators being put forward have not been agreed democratically and lack public support.
2. **Lack of underpinning theory and narrative.** The indicators, unlike GDP, are not underpinned by a consistently articulated theory or ideology, summarised in a politically compelling narrative.
3. **Lack of a clear political imperative.** The economic crisis (along with barriers 1 and 2) has meant the priority has been to fix the economy in the traditional way.
4. **The need for organisational change.** An integrated approach requires working across departmental boundaries or alternatively reforming economics departments.
5. **Institutional resistance to change.** This always exists and as always reflects the fact that the power and/or success of institutions often depends on traditional objectives and models.
6. **Technical questions with indicators.** There remain disagreements about defining indicators, particularly on whether and how to create a single alternative to GDP.
7. **No widely used analytical tools for integrated and innovative economic policy making.** The tools needed are still in development. Innovation in civil services is always difficult.

The most important lesson is that all these issues will need to be addressed together. That is, action on the political, theoretical and organisational barriers (1-5) must take place alongside measures to address the technocratic barriers (6-7).

For that reason we recommend three kinds of action. None of these can succeed without the others and all of them require co-operation between politicians and officials.

1. **Build support for change** – institutions need to stimulate a broad public debate about the kind of society Europeans want, while drawing on the range of theories currently in play as to how to achieve this
2. Develop and embed better analytical tools into policy making processes
3. Improve procedures and structures so that the will for change is not diverted into rhetoric but channelled into effective action.

This paper also summarises two recent UK reports (Wellbeing and Policy by Gus O’Donnell et al and Wellbeing in four policy areas from the All-Party Parliamentary Group on Wellbeing Economics). Both these papers make recommendations for policy and process consistent with ours.

1. Background

The Treaty of Lisbon is the foundation for a ‘Beyond GDP’ approach to policy within the European Union. It says:

“The Union’s aim is to promote peace, its values and the wellbeing of its peoples... In defining and implementing its policies and activities, the Union shall take into account requirements linked to the promotion of a high level of employment, the guarantee of adequate social protection, the fight against social exclusion, and a high level of education, training and protection of human health... Environmental protection requirements must be integrated into the definition and implementation of the Union’s policies and activities, in particular with a view to promoting sustainable development.”

This is entirely consistent with the ‘Beyond GDP’ agenda to promote social justice, sustainability and wellbeing.

It is agreed that GDP maximisation and market efficiency cannot be the only objectives of economic policy if these aims are to be achieved: a broader range of intermediate objectives is needed. Growth may still be desirable, but it needs to be ‘good growth’. This is supported by the European Union’s Europe 2020 strategy and the Commission’s confirmation earlier this year that “seeking to return to the growth ‘model’ of the previous decade would be both illusory and harmful”.

So the question is: how do we achieve changes to economic policy-making that are in line with these new priorities and this strategy? One part of the answer is to create new measures of progress that reduce the predominance of GDP. This is a necessary, although obviously not sufficient, condition.

To this end, in 2008 President Sarkozy set up the Commission on the Measurement of Economic Performance and Social Progress (or the ‘Stiglitz Commission’) which made its recommendations in 2009. It recommended the following changes:

**Shift the emphasis of measurement from economic output to wellbeing.** This means assessing material living standards by measuring household income and consumption, rather than

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production. There should be more of a focus on wealth distribution, and stocks of capital (financial, natural, human and social), and income measures should include non-market activities.

**Measure the objective and subjective dimensions of wellbeing along with material living standards.** These include health, education, personal activities and environmental conditions as well as social connections, political voice and security. They should take account of wellbeing inequalities, assess the connections between the various domains, and inform policy.

**Develop a ‘dashboard’ of sustainability indicators.** Monetary indicators should only be one element of this dashboard, which should also assess the state of natural capital and indicate how close we are to environmental danger. The Commission argued that wellbeing and sustainability are distinct concepts and that attempts to combine them into a single indicator could cause confusion.

In 2009 the European Commission took this work further by publishing *GDP and beyond: Measuring progress in a changing world.*

So, what else is necessary for these indicators to form an effective part of economic governance?

The debate continues. The question is being addressed at ‘Moving beyond GDP in European economic governance’ on 10 October. The conference is considering how measures of inequality, sustainability and social impacts can be better taken into account.

This paper summarises key findings from BRAINPOoL, a project funded by the European Commission under the FP7 Programme, which also addressed this question. It reports on more recent work in the UK and draws conclusions for Europe, that are based on but go beyond these various projects.

2. Beyond GDP defined

The BRAINPOoL project found there was considerable confusion about what ‘Beyond GDP’ really meant. Some statisticians identified ‘Beyond GDP’ with social and environmental indicators (perhaps influenced by the structure of the Stiglitz Commission report). They then pointed out that these indicators are already used in social and environmental policy, and it is therefore pointless to ask what is needed for them to be used in policy making. It became necessary to refine the question and ask how they could be used in *economic* policy making.

Some of those interviewed then suggested this was an illegitimate step. They accepted that there might be trade-offs between environmental, social and economic objectives as traditionally measured, but believed these can and should be resolved at the political level through negotiation.

The argument against this makes the basic case for ‘Beyond GDP’: that is, that in such negotiations traditionally measured economic objectives trump other ones. For many different reasons, there is a bias in policy making towards prioritising GDP growth and efficient markets. It is precisely to correct

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this bias that we need new indicators for economic governance. If anything this need is even greater at European Union than national level.

So, the debate is not about the use of ‘Beyond GDP’ indicators in parallel with traditional economic indicators (as described by the chart below).

Instead it is about their use as part of an integrated economic policy process.

This would allow policy makers in an individual ministry at national level, or directorate general at European level, to aim for good growth...

...as opposed to bad growth.
This would enable them, now and in the future, to more effectively "contribute to raising the economic welfare of the citizens in the European Union".4

‘Beyond GDP’ indicators can be used at two points in this model:

- as ultimate outcome measures, (of wellbeing now and in the future – the right hand box
- and to measure what drives these outcomes (the lower central box).

This corresponds to the double role that GDP plays in economic governance: as a proxy for welfare, and as a measure of output.

3. BRAINPOooL findings: barriers

BRAINPOooL found three groups of barriers to this kind of integrated economic policy making.5

**Political and theoretical barriers**

1. **Lack of democratic legitimacy – particularly for measuring ultimate outcomes.**  
The proposed new indicators have not been democratically agreed, especially those measuring sustainability. Even subjective wellbeing measures have not been popularly endorsed as measures of outcomes. By contrast, it is argued, GDP is broadly accepted by the public as an indicator of economic success.

2. **Lack of underpinning theory and narrative.** The lack of legitimacy is partly because ‘Beyond GDP’ indicators are not supported by a consistently articulated theory or ideology, let alone one summarised in a politically compelling narrative. It is not that there are no theories available – rather that they have not been linked effectively to indicators and policy.

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5 At a superficial level there may be a lack of resources or (timely) data, or simply ignorance or confusion about the agenda. However this generally reflects low prioritisation and is a symptom of other problems. In addition, perhaps some indicators are badly designed, too complex or difficult to explain, or in some cases using inadequate data. But again, this is superficial a problem, reflecting a lack of discriminating demand. We focus here on what we think are the underlying barriers.
By contrast GDP is supported by a consistently articulated theory: markets deliver optimal outcomes except where specific market failures are identified and when they generate unacceptable inequality. It follows from this that maximising growth – while correcting market failures and conducting some redistribution – will maximise welfare.

Many economic policy makers regard this as a sound theory, and therefore regard the many aims of ‘Beyond GDP’ economic policy making as redundant or worse: ‘redundant’ to the extent that there are no policy changes implied; ‘worse’ to the extent that any policy changes that are implied may damage growth and market efficiency and, as a consequence, welfare.

3. **Lack of a clear political imperative.** The lack of legitimacy and narrative just described – along with pressure created by the economic crisis – has meant that most of the electorate appear not to want politicians to prioritise the outcomes that Beyond GDP indicators measure. Just fixing the economy (as traditionally understood) has been the priority.6

Voters understand economic competence in a very traditional way. As a result, politicians are not demanding that the relevant indicators are used – even if sometimes they call for the development of these indicators (like David Cameron and Nicolas Sarkozy) or are sympathetic, in principle, with the overall aim of creating an inclusive and sustainable economy.

**Organisational barriers**

4. **The need for organisational change.** An integrated approach to policy requires bringing to bear a range of different perspectives and working across disciplinary boundaries. This in turn requires working across departmental boundaries; alternatively, economics departments could be reformed so that they represent these different perspectives. Either of these options creates familiar organisational challenges.

5. **Institutional resistance to change.** The BRAINPOoL team encountered and heard about clear resistance to abandoning traditional objectives and models. This resistance seemed to be much deeper than the fear that, as yet, it is thought there is no better alternative. (See barrier 2). This may reflect:

   - a genuine belief in prioritising growth
   - a mistrust of those advocating change
   - the influence of established networks of advice and interest
   - or the fact that the power and/or success of certain institutions depends on the predominance of traditional objectives and informal models continuing.

**Technical barriers**

6. **There remain technical questions with indicators.** There is disagreement about the best way to measure sustainability. Some believe the adjustments to GDP (made by indicators

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6 Although of course there is demand from some section of the electorate and civil society.
such as the Index of Sustainable Economic Welfare) and derivatives (such as Germany’s National Welfare Index) lack a theoretical justification. No consensus has emerged around a single indicator of wellbeing to replace GDP as a measure of economic performance. In addition, the terms ‘sustainability’ and ‘wellbeing’ are used inconsistently and some believe the concepts behind them are unclear. Finally, all too often, indicators are developed without a clear understanding of how or whether policy makers will use them.

However, this barrier should not be overstated: work by Eurostat and others has produced powerful indicators sets.

7. There are no widely used analytical tools for integrated and innovative economic policy making. An integrated approach to economic analysis must deal with complexity and uncertainty and make use of a range of methodological approaches. This creates analytical challenges. However, models linking policy with overall wellbeing are incomplete (though work is in progress).

This contrasts with well established – although often unreliable – formal and informal models that help develop economic policy to maximise GDP and market efficiency.

Similarly, work to develop analysis of what is required to move to a sustainable economy is still in progress. Innovative policy making processes (for example, considering combinations of policies that have not been tried before) are required. And they are notoriously difficult in civil services.

Perhaps the most important lesson overall is that all these issues will need to be addressed together. That is, action on the political, theoretical and organisational barriers (1-5) must take place alongside measures to address the technocratic barriers (6-7).

It is not enough that there is technical progress among those developing statistics and policy making tools on the one hand, and a broad desire for ‘good growth’ among politicians and civil society on the other. A more focused alliance is needed between those creating pressure for change, and those creating the tools to facilitate it.

4. Relevant conclusions from two UK reports

Two reports on wellbeing have been published in the UK since the BRAINPOoL report was written. Wellbeing and Policy by Gus O’Donnell et al (former Head of the UK Civil Service and Cabinet Secretary) was published in March of this year. \(^7\) Wellbeing in four policy areas, by the UK All-Party Parliamentary Group on Wellbeing Economics, was published in September. \(^8\)


\(^8\) All-Party Parliamentary Group on Well-being Economics. (11 September 2014). Well-being in four policy areas. Retrieved http://parliamentarywellbeinggroup.org.uk. This was the result of a nine-month inquiry involving five public sessions with expert witnesses. The New Economics Foundation acted as the secretariat to the inquiry.
Both reports cover some of the implications of wellbeing evidence for policy, including economic policy, and so negate the idea that ‘Beyond GDP’ is redundant. They also make recommendations for the policy process.

The O’Donnell report, Wellbeing and Policy, proposes using subjective wellbeing data in policy making – both to set broad priorities and to improve detailed ‘cost benefit analysis’ (CBA) techniques. For either purpose, policy makers need to know the relative importance of the determinants of wellbeing (such as income, health, employment, family and so on). Fortunately there is a substantial and growing body of evidence on this.

This evidence enables the report to suggest a number of priorities. In economic policy, these priorities include:

- “a stable rate of growth rather than growth that (even if higher on average) includes periods of recession”
- reducing unemployment
- and higher levels of wellbeing at work.

The report explains that wellbeing-based CBA uses the evidence on the relative importance of the determinants of wellbeing, alongside an assessment of the impact of a particular policy on these determinants. This enables the policy maker to work out “the total effect of the policy on overall life satisfaction”. Ideally, this will take account “of what economists call ‘general equilibrium’ effects” – that is to say knock on consequences, for example the way “building an airport... will change... commuting patterns”.

This is in effect a technique for estimating the value of non-market goods and services and thus side-stepping well known problems with traditional CBA. The wellbeing numbers may be far from perfect but the question is “whether these numbers are better or worse than the shadow prices and imputations that are currently used in public decision making”. They often are.

The resulting wellbeing benefit can be converted into money values to allow comparison with the cost, but this can be problematic. For many purposes it is better to use a threshold level of wellbeing benefit. In principle this can be established by identifying the positive contribution of the marginal (least valuable) existing policy (assuming a ranking of all policies across government by their wellbeing benefits and a fixed amount of public expenditure).

The Parliamentary report, Wellbeing in four policy areas, also uses evidence to recommend a number of policy priorities. In economic and labour market policy, it concludes that:

- “secure employment and the absence of recessions are more important to wellbeing than the growth rate”

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9 These are numerous. The traditional techniques used to establish shadow prices (which can be used to price unpriced goods and deal with distributional and temporal issues) are fraught with difficulty. CBA is also based on the assumption we operate as rational maximisers, which we don’t. And it ignores non-economic domains: the fact for example that we may trade-off goods for feelings, or that outcomes can be pareto optimal when income is the only factor, but sub-optimal if political economy effects or other factors are taken into account.
• “tackling poverty and inequality matters much more than increasing national income in aggregate”
• “promoting shorter and more flexible hours would help tackle the twin problems of over- and under-work”.

The Parliamentary report’s recommendations on process include that all political parties should set out their understanding of, and approach to, wellbeing in their manifestos. It recommends that the Government set out a wellbeing strategy, including:

• objectives and how it intends to achieve them
• the use of a wellbeing-based policy assessment and the development of new tools to support it
• the incorporation of a wellbeing assessment into budget allocations between and within departments
• and tools to facilitate the cross-departmental work needed to increase the wellbeing benefits of policy.

5. Implications of BRAINPOoL and other reports for the European Union and possible actions

What might these findings and recommendations mean for the European Union institutions? In this section we set out ideas to stimulate discussion. Broadly we recommend three types of action:

1. building support for change
2. developing and embedding better analytical tools
3. improving procedures and structures.

None of these will be effective without the other two. All will require co-operation between officials, politicians and advocates of change.

Building support for change

BRAINPOoL argued that ‘Beyond GDP’ indicators and concepts can only play a role in European economic governance if they have democratic legitimacy. Where will this come from?

Our view is that it requires a process of direct public engagement, orchestrated by existing institutions. The existing democratic channels (that is, elected national governments and elected members of the European Parliament) cannot deliver what is needed on their own. On the other hand, this is not something that civil society can do on its own either.

Of course, ultimately the direction of European economic policy has to be owned by the European Council and endorsed by the member states. But something has to drive the change – something visible both to the European institutions and to the governments of the member states.
In Scotland we have recently seen the power of genuine democratic engagement about the kind of
country citizens wish to live in. The yes-no choice was the centre of a much wider debate. There was
a serious question that was worth discussing, and the public engaged and turned out to vote in
record numbers (84%).

To advance, Europe needs something similar. Can members of the Parliament and/or the new
Commission initiate something that will ask some really fundamental questions?

If so, the resulting engagement will need to be informed by evidence and designed to shape and
endorse a new narrative and a new vision of progress. (For more on narratives, see Annex 1). If the
instincts of the proponents of ‘Beyond GDP’ are right, and this agenda is popular, it will go beyond
GDP growth and an efficient single market. It will set out not only desirable and uncontroversial
goals for economic policy (such as good jobs, security, a reduction in poverty and opportunities for
children) but also priorities – that is, how to resolve some of the key trade-offs that have to be faced
in achieving these goals.

The result will not be a consensus let alone a set of policy solutions, but the process could shift the
terms of the political debate. It could strengthen the hand of those who argue for integrating a
wider range of objectives into economic policy making, and – above all – help answer the question:
“What is Europe for?”

There is a need for input into this debate. Everyone, of course, can take part, but presumably
members of the Parliament and commissioners could play a significant role. The challenge is not just
coming up with policy ideas, but selecting a few emblematic policies that are potentially popular,
represent real change, form part of a coherent framework and can be identified with ‘Beyond GDP’.

BRAINPOoL emphasised the importance of an underpinning theory. This is clearly not something for
the Commission or Parliament, but for academics and think-tanks. However it is important that
emblematic policies and theory are developed with policy makers. Theory helps policy makers
assess whether policies will work; policies help theoreticians assess whether their work is relevant.

It is not that there is no theory, as noted above, rather that it is not effectively linked to policy.
Could members of the Commission and/or Parliament set up a group to establish regular dialogue
with those working on ‘Beyond GDP’ theory?

Please note: the processes we are recommending cannot play a part in the mid-term review of the
Europe 2020 goals, because the timetable for the latter is too tight. However, they could contribute
to the next set of goals, and to creating greater political traction for such goals than is enjoyed by
Europe 2020.

**Analytical tools**

New approaches to policy analysis are required to deal more robustly with the many objectives and
the trade-offs between them. The current review of impact assessments within the Commission
represents an opportunity to embed new tools.
These may involve combining formal economics with other forms of analysis. A single numeraire, such as life satisfaction, could be developed for the evaluation of trade-offs between different dimensions of wellbeing. Or, multi-criteria screening processes could be developed to help integrate new indicators into policy development and decision making. There will be a need for other processes that are designed to stimulate innovation.

We are aware that work on such tools is on-going. No doubt the current review of impact assessments will take on board the conclusions of Gus O’Donnell and colleagues described above.

There has also been a push from some parties for impact assessments to more explicitly take into account expected costs for businesses and growth. Of course these costs ultimately have an impact on wellbeing, but it is easy to see how an impact assessment could put undue weight on this, relatively easy to quantify, determinant of wellbeing as against others. It is therefore all the more important that the kind of techniques advocated by Gus O’Donnell are introduced.

**Improving procedures and structures**

BRAINPOoL, among others, has identified the way traditional economic objectives tend to trump others, as noted in Section 2 above. Ultimately this is a political issue, which is why it is important to build support for change as just described.

However proponents of change have to ensure that the will for change, once created, is effectively channelled. It must not be diverted into ineffective statements and targets, with real action blocked by existing procedures, interests and habits of mind – all of which could be entrenched in bureaucratic structures and relationships.

In this respect, the European Commission is no different from any other bureaucracy. The general principle – that more and different people will be needed at the table when decisions are made – applies here. Bringing together diverse perspectives and challenging orthodoxies will require:

- multi-disciplinary working – incorporating insights from disciplines beyond economics
- working across silos within organisations
- increased co-operation between organisations
- and potentially re-organising.

We do not have detailed recommendations for bureaucratic reform in Brussels. We recommend that advocates of ‘Beyond GDP’ commission work on this, paying attention, among other things, to:

- the Rules of Procedure for the Commission
- the President’s Political Guidelines
- the structure, procedures and balance of expertise and perspectives within DG ECFIN
- the role of the Secretariat General
- and the way in which the Commission engages with civil society and business lobby groups (including conflict of interest rules and the composition of advisory and expert bodies).
Finally, we note that changes already proposed for the new College of Commissioners under President elect Jean-Claude Junker offer both a threat and an opportunity for the Beyond GDP agenda.\textsuperscript{10} A First Vice-President with a specific mandate for “Better Regulation” and a Vice-President with a specific mandate for growth both have the opportunity to advance or indeed to block measures designed to produce good, as opposed to bad, growth.\textsuperscript{11}

\textsuperscript{10}For more information, see http://ec.europa.eu/about/juncker-commission/commissioners-designate/index_en.htm

\textsuperscript{11}Titles in full: First Vice-President, in charge of Better Regulation, Inter-Institutional Relations, the Rule of Law and the Charter of Fundamental Rights; and, Vice-President for Jobs, Growth, Investment and Competitiveness
Annex 1: Narrative and theory

What do we mean by a narrative?

We mean an account of what constitutes ‘good’ and ‘bad’ and of why good things and bad things happen. In this way, a narrative can justify the programme of a government or other institution. It may make a direct promise of good things, but it will also provide voters and other stakeholders with good reasons for believing the promise.

A narrative is not the same as an economic theory, but it needs to be at least consistent with a theory. For example, Ronald Reagan had a slogan, “Cut taxes,” that formed part of a broader narrative: the world would be a better place if we could get government off people’s backs. This was consistent with neo-liberal theory, and the version of neo-classical economics underpinning it.

The most effective narratives also provide guidance to officials, simplifying assumptions that make the job easier. For example, civil servants working for the Thatcher government in the 1980s knew that the priorities were market liberalisation and cutting taxes. This made it possible to delegate tasks to relatively junior officials.

Building a new narrative

The existing growth narrative can be and has been challenged, even on its own terms, but that is not enough. A new narrative is needed. BRAINPOoL found that ‘Beyond GDP’ is not considered to be underpinned by a clear, electable narrative about the economy.

This is partly a positioning issue. In the UK at least, wellbeing has been associated with policies other than economic. This means that wellbeing is seen as a ‘nice-to-have’ rather than central to people’s lives. Sustainability has for a long time been associated in some critics’ minds with middle-class greens who are unaware of the struggles facing ordinary people. This limits political support for ‘Beyond GDP’ among those who might benefit from it the most.

However it is not just a positioning issue. It is more fundamental than that. Korean economist Ha-Joon Chang (writing in a UK context) has given one account of the challenge:

“Most Britons have come to see themselves mainly – or even solely – as consumers, rather than workers. The dominant free-market ideology has convinced them that consumption is the ultimate goal of life, and that their work is only a means to gaining the income to buy the goods and services to derive pleasure from. At the same time, the decline of the trade union movement has made many people believe that being a ‘worker’ is something of an anachronism. As a result, policies are narrowly focused on generating higher income, while any suggestion that we spend money on making jobs more secure and work less stressful, if it
is ever made, is dismissed as naive. If we are to deal with the ‘general living crisis’ we need to radically change our perspectives on what is a good life.”

One might add “and on how to deliver a good life”.

Theory can help address these fundamental challenges, that is help us define both what is a good life, and how to deliver it – and fortunately a number of potentially relevant theoretical positions already exist. These are too complex to form a popular narrative themselves but, like neo-classical economics, offer potential theoretical underpinning for a ‘Beyond GDP’ narrative.

We at the New Economics Foundation, and others, are working on how these theories might come together to form the basis of a popular and politically compelling narrative and which underpins policy. We would welcome dialogue with interested parties.

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