Don’ t Get Too Hung Up on GDP

Stephen Chung
Executive Director
Zeppelin Real Estate Analysis Limited
March 2002

This is translated from an article written in Chinese that we had contributed to the Hong Kong Economic Journal.

When economic and business news are involved, quoting of economic data is commonplace. One such frequently quoted item is the Gross Domestic Product (GDP), and investment moods seem to have some positive correlation to its relatively level i.e. when GDP growth is reported, sentiment improves, and when the GDP growth is down (or even negative), sentiment goes down with it as well. One also sees experts and academics debating over very small differences, e.g. whether the GDP growth would be 5% or 5.5% etc, despite figure-wise even a 1/2% may mean huge sums given the size of the Hong Kong economy. While admittedly the author is no economist and no expert in this area, he stills think **sometimes people may have been a bit too hung up i.e. cared too much about the GDP and its growth**. Here’ s why:

a) **In many instances, the GDP figures are “nominal”** = does a 10% GDP growth over last year really mean growth, or for that matter, mean economic satisfaction (happiness) for most? It depends. For instance, if inflation rate (to some the good old days) for that year is 15%, probably most will actually be worse off for the purchasing power is actually down (though most may be psychologically happier). Similar meanings apply if say the population of the economy expands by 12%.

b) **GDP does not take into account things that have been ‘ broken’** = for instance, say two very simple economies and both make cups. Economy A makes 1 cup per month for $10 each and thus in a year its GDP will be 12 x $10 = $120. Economy B makes the same but is always clumsy i.e. they break 3 cups each month before they finally get to use the 4^{th} one. Thus, its GDP will be 12 x 4 x $10 = $480. Economy B looks 4 times mightier than Economy A but at the end of the day they both own the same 12 cups each at $10. Tip = if you want the GDP figure to look good, one way is to make things and then break them and then make them again and then break them on and on and on.

c) **GDP alone does not tell you much about the economy’ s (market) effectiveness and (production) efficienc**y = An economy can produce a lot of the goods and services thus leading to a high GDP figure yet if these goods and services have no or insufficient takers / market for them (due to oversupply or obsolescence), its effectiveness (producing goods and services that can be sold) is reduced. Note that this is irrespective of whether the goods and services are produced (time and cost) efficiently. Likewise, an economy can be producing something that people want yet if the production process is not cost-efficient, it runs the risks of being priced out of the market or having to suffer losses, though its GDP will be higher than if it was more efficient looking from a production angle.

By and large, to gauge a bit more accurately the relative economic performance of an economy, other figures and factors may be used in conjunction. The main point here is that there is no need to get overly excited about a high / rising GDP figure or to get too depressed about a lower / decreasing GDP figure. Perhaps the GDP per capita figure may mean more, especially ones that are adjusted to some base year. At least this holds true for gauging real estate prices in Hong Kong, as both prices levels and GDP/capita have been decreasing during the recent years.

Click here to return: Simple to Read