

Funding the Future

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Published: January 12, 2026, 5:45 pm

It's the most quoted number in economics, but what is GDP really? And what's wrong with it? There are shocking flaws at the heart of how we measure our economy.

https://www.youtube.com/watch?v=eUa3u_GQVr4?si=6K-i-Vs2AKZsLqDd

This is the audio version:

https://www.podbean.com/player-v2/?i=vr4a9-18e0616-pb&from=pb6admin&share=1&download=1&rtl=0&fonts=Arial&skin=f6f6f6&font-color=auto&logo_link=episode_page&btn-skin=c73a3a

This is the transcript:

Hi, I'm Richard Murphy, and today we're talking about a big idea in political economy.

Tom is with me, and he's got the question.

Thanks, Richard. So the question today is, what is GDP, and what is wrong with it?

So, you want to start with the big ones, eh?

That seems to be one of the biggest questions that you can ask in political economy because GDP, or 'Gross Domestic Product', to give it its full name, is a measure of our national income.

The idea of GDP was created in the 1930s by a man called Simon Kuznets, and he, at

the time, saw all the problems with the measure that he had created, but our politicians have ignored these ever since.

In reality, there are three ways of calculating GDP. They're called the output approach, the income approach, and the expenditure approach. Unsurprisingly, they each come up with a different answer, and it comes down to our national statistics agencies to reconcile these into one number. But in reality, the one that most people look at is what is called the expenditure approach, and the expenditure approach adds up our total final consumer spending in the UK, the sum of business investment, and the sum of government spending (excluding transfers like pensions and benefit payments), which then get reflected instead in consumer spending, and the net exports of the country, which is simply exports minus imports. What this, then, means is that we come up with a really big number, which is supposedly our national income.

The trouble is that the expenditure in question doesn't really reflect income.

For example, in that expenditure method I've just explained, total investment is included. But the benefit of that investment comes over the years ahead.

You don't get the benefit in year one of investment; by definition, investment is made so that you get benefit over a period of time, but GDP assumes all that benefit arrives in the year when the expenditure is incurred, which is nonsense. That is not our income for the year.

At the same time, and quite bizarrely, we ignore the benefit this year of the investment expenditure that was made in earlier years.

As a consequence, the figure for national income is nothing like the figure for income that we might get, for example, in a set of financial accounts produced by a company. This fact might, by itself, explain why so many politicians who are familiar with financial accounting are so confused by the idea of GDP. The two are nothing like each other.

And then there are other problems. GDP does, for example, take no account of the value of anything. If a major oil spill created massive expenditure in the UK on a cleanup operation, that would add nothing to our well-being, but it would seriously increase GDP.

Similarly, if vast numbers of people began to get divorced in the UK, that would not add to human well-being because it would, in fact, reflect increased human stress. But the expenditure on lawyers and all the costs of breaking up households would increase GDP.

And, and I think this one is really important, the cost of treating preventable illnesses is considered to be a part of our national income, when it would've been so much better if the illnesses in question had been prevented.

In other words, GDP does not in any way reflect increases in our well-being. There's simply a total disconnect between the two, and at the same time, GDP also completely fails to take into account how the income of the country is distributed.

So, for example, if the entire financial income of the UK was owned by one person and everybody else had to live in absolute squalor within the economy, bartering to take part in any trade that they undertake, that would still be reflected as a single figure for GDP. The income of that single person would then be the GDP of the country. And if it increased, our politicians, who believe that GDP growth is the only thing that matters in the UK, would celebrate that fact. But in practice, of course, that's nonsense because everybody else will be excluded from the benefit. So that makes no sense.

We have to take distribution into account when we consider whether GDP growth is of any consequence, and we could do that very simply. We could simply actually consider whether we want to consider GDP per head of population or total GDP, but we don't, and the consequence is that GDP is what I like to call CRAp, or in other words, a Completely Rubbish Approximation to the truth.

So what could we do instead?

We could look at figures for GDP per capita, as I've just said; GDP per person, in other words. That would tell us how much better off we are as a consequence of a change in a period.

Then we could adjust for changes in income distribution arising because of investment. And that would make sense.

We could also allow for changes in income distribution, so that if we spread the income more evenly, we could reflect that fact in the data per head of population and show how the best-off have perhaps not gained as much as the worst-off, and so on. Again, this would provide us with really valuable information for policymaking, which is absent at present.

Finally, we could take out the GDP calculation or even treat them as negative income, those items that cause harm, and I've explained some of those already.

In other words, we could do much better than we are now, Tom, but we aren't, and it's time that politicians took notice.

I hope that answers the question.

If you want to write a letter to your MP on the issues raised in this blog post, there is a ChatGPT prompt to assist you in doing so, with full instructions, [here](#).

- * Murphy, R. (2024) "GDP records everything but the things that really matter." Tax Research UK. [Available here](#)
- * Murphy, R. (2024) "GDP is up, but is that good news?" Tax Research UK. [Available here](#)
- * Murphy, R. (2024) "As the July GDP data proves, nothing really changed that month." Tax Research UK. [Available here](#)
- * Murphy, R. (2024) "Economic growth? Forget it." Tax Research UK. [Available here](#)
- * Murphy, R. (2025) "Have you felt all that lovely growth?" Tax Research UK. [Available here](#)
- * Murphy, R. (2025) "Might the US be about to fall off an economic cliff?" Tax Research UK. [Available here](#)
- * Murphy, R. (2025) "Is all economic growth good?" Tax Research UK. [Available here](#)
- * Murphy, R. (2025) "GDP: what's happening?" Tax Research UK. [Available here](#)