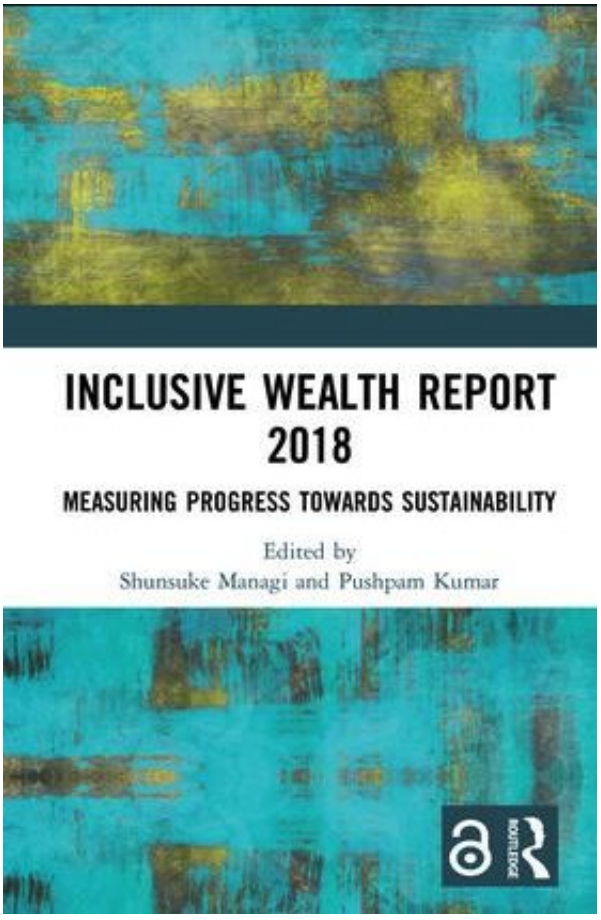
This index measures progress and sustainability better than GDP

October 10 2018, by Pushpam Kumar



An alternative to GDP, the Inclusive Wealth Index measures all assets which human well-being is based upon, including manufactured, human and natural capital.

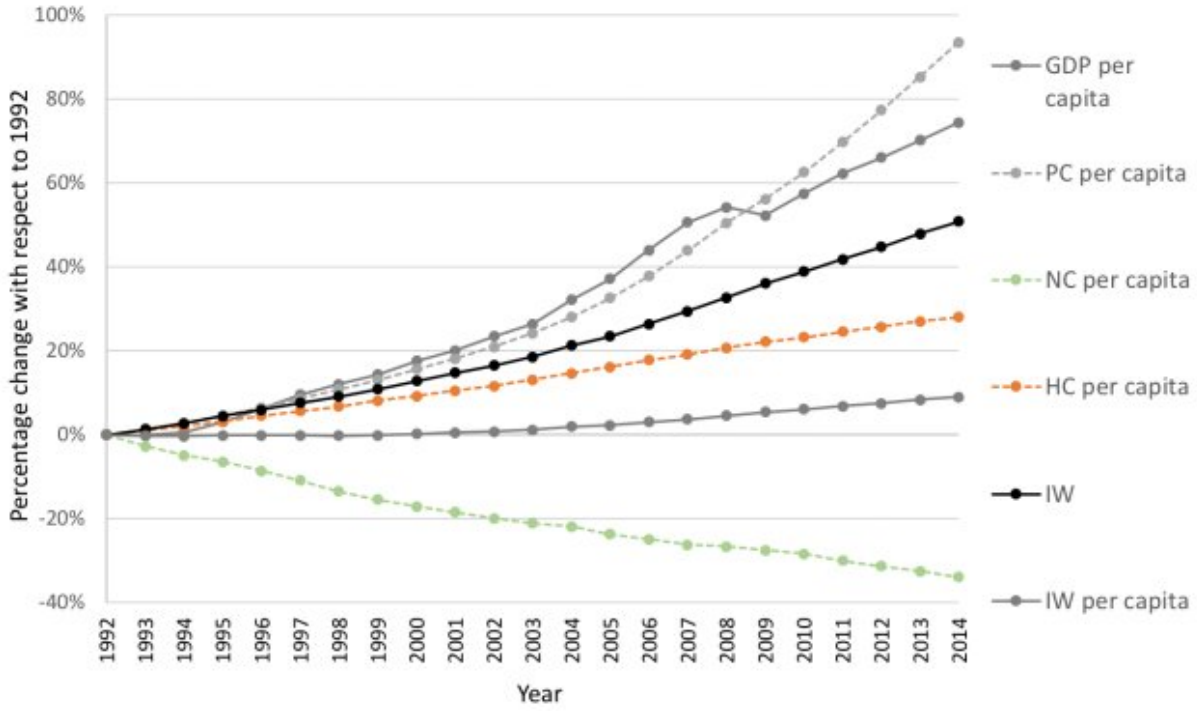
Conventionally, economists use gross domestic product (GDP) to

estimate the sustainability of the economy and the quality of societal welfare. However, this approach is not only incorrect and logically flawed, but also in gross neglect of nature's contribution to the society.

GDP measures the performance and level of economic activities though the market value of goods and services. This single indicator has such a profound impact on public policy and politics that even a decline in national income by half a percentage point in any quarter of the year creates political waves and generates talk about recession.

While national income provides useful information on the structure and performance of the economy, people mistakenly use it as proxy for human welfare and sustainability. The latter is not only unreliable and incorrect; it can mislead decision-makers. Nobel economists Nordhaus and Tobin were able to spot this early on. The system of national income accounting has serious flaws, but nothing is as serious as the asymmetry that arises between produced and natural capital (i.e., goods and services such as water, air, soil, biodiversity, and scenic beauty, which are critical for human existence) when using a GDP-based approach to value goods and services.

Conventional accounting systems do not adequately capture the functions and services of nature and ecosystems. The United Nations Environment-led Inclusive Wealth Index (IWI) is an alternative index to GDP and the Human Development Index. The IWI demonstrates that when produced capital, natural capital and human capital are combined, the growth rate of wealth is much slower than GDP growth for 140 countries. This indicates that traditional measures of economic growth and development may be substituting income for wealth, a practice that is dangerous as we consider how to balance economic growth with sustaining ecosystems and ecosystem services.



The latest IWI report shows that 44 out of 140 countries have suffered a decline in inclusive wealth per capita, even though GDP per capita increased in nearly all of the countries assessed. This means that these 44 countries are not on a path to sustainable development even if their economies, according to GDP, appear to be growing. Credit: Inclusive Wealth Report 2018

Economic performance and improved well-being depend on more than growth in income and GDP. Inclusive wealth includes a holistic assessment of produced capital (manufacturing output or GDP), as well as human capital and natural capital within a country. It is a multipurpose indicator capable of measuring not only traditional stocks of wealth but also those less tangible and unseen—such as educational levels, skill sets, health care, as well as environmental assets and the functioning of key ecosystem services that form the backbone of human well-being and ultimately set the parameters for sustainable development

.

The IWI is complementary to GDP and an important instrument to measure progress toward sustainable development. Its use will help build the capacities of countries to measure the full array of assets they can bring to bear on achieving sustainable development, as called for by Target 17.19 of Sustainable Development Goal (SDG) 17. It can also ensure that economic development is in fact sustainable. By tracking the evolution of stocks of produced capital, natural capital, and human capital over time, the index will help guide policymakers in their decisions relevant to sustainable development and staying within planetary boundaries.

A country's economy may appear to be doing well – its GDP may be growing – but at what cost? The IWI answers this question. To do this, the IWI tracks the progress of 140 countries that make up the lion's share of the global economy ($56.84 trillion) and population (6.89 billion people). The index accounts for each country's stock of assets – its manufactured, human and natural capital – and assesses the changing health of these assets over 25 years. It's a massive dataset that covers almost an entire generation. (Fifty countries with small economies are not included in the IWI because of the difficulty in obtaining reliable data.) The latest IWI report shows that 44 out of the 140 countries have suffered a decline in inclusive wealth per capita even though GDP per capita increased in nearly all of the countries assessed. This means that these 44 countries are not on a path to sustainable development even if their economies, according to GDP, appear to be growing. These countries are depleting their stocks of natural, human and/or produced capital at rates that will leave future generations worse off. Over all, the global per capita natural capital for 1992-2014 is on decline as shown in the figure below.

IWI is a multi-purpose, multi-target, integrated measure of sustainable

development that can help to reduce the number of global indicators needed to measure the SDGs. An increase in IWI will indicate progress towards poverty eradication (SDG 1), achieving food security while promoting sustainable agriculture (SDG 2), and supporting healthy lives and human well-being (SDG 3). An increase in IWI will also indicate sustained and inclusive economic growth (SDG 8) and sustainable consumption and production patterns (SDG 12). A decrease in IWI will indicate degradation of natural capital and failure to take steps to combat climate change and its impacts (SGD 13); failure to conserve and sustainably use the oceans, seas, and marine resources (SDG 14); and failure to protect, restore, and promote the sustainable use of terrestrial ecosystems, combat desertification, reverse land degradation, and halt biodiversity loss (SDG 15). In addition, the IWI can measure the strength of the means of implementation (e.g., policies and programs) for promoting sustainable development (SDG 17).

The key strength of the IWI is its potential to serve as a metric for sustainable development policy. By highlighting the existing productive base in a country, whether that base is used to achieve economic, social, and environmental goals, the index can help policymakers target investments and recognize the policy and resource trade-offs associated with decisions regarding sustainable development. With the advent of the SDGs, now more than ever, countries need to step up their work to strengthen environmental accounting and, consequently, become better able to use the IWI as a tool for policy change. By measuring natural wealth—an untapped and underappreciated wealth stock—we can move one crucial step closer to recognizing natural capital's contribution to and impact on achieving sustainable development.