

Contribution to Beyond GDP „Virtual Indicator Expo“

<http://www.beyond-gdp.eu>

Name of the indicator/method: **The Human Development Index (HDI)**

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Why an alternative measure to Gross Domestic Product (GDP)

Gross Domestic Product (GDP), which is the standard measure of a nation's total economic activity has been a dominant measure of a country's level of development for a long time and was assumed to translate directly into improved human well being. However, while growth-oriented policies may increase a nation's total wealth, whether or not growth enhances human development depends on how that growth is generated and used. The economic growth paradigm neglects important aspects of development, such as income inequalities, unemployment, and disparities in access to public goods and services like health and education. For economic growth to enhance human development, it should provide an opportunity to enhance workers' knowledge and skills along with opportunities for their efficient use, provide better job opportunities and support greater democracy at all levels of decision-making. Thus, the growth paradigm does not capture adequately the multi-dimensionality of development.

What is the Human Development Index (HDI)?

The HDI serves as a frame of reference for both social and economic development. It is a summary measure for monitoring long-term progress in a country's average level of human development in three basic dimensions: a long and healthy life, access to knowledge and a decent standard of living. It sets a minimum and a maximum for each dimension, called goalposts, and shows where each country stands in relation to these goalposts, expressed as a value between 0 and 1.

The life expectancy component of the HDI is calculated using a minimum value for life expectancy of 25 years and maximum value of 85 years. This is because even with HIV/AIDS it is unlikely for life expectancy at birth to fall below 25 years.

The knowledge component of the HDI is measured by adult literacy rates and the combined gross enrolment ratio in primary, secondary and tertiary education, weighted to give adult literacy more importance (two-thirds). While at the national level it is unlikely for any of the knowledge indicators to assume a zero value, at disaggregated levels, it is possible for some population sub-groups to score very low on the indicators. For this reason, the lower end of the goalpost is set at 0 and the upper end at 100 per cent.

For a decent standard of living, which is measured by GDP per capita in purchasing power parity (PPP) US Dollar terms, the goalpost for minimum income is \$100 (PPP) and the maximum is \$40,000 (PPP). GDP per capita is converted into PPP terms to eliminate differences in national price levels in order to make standards of living comparable across countries.

In the calculation of the HDI, a logarithm of income is used to reflect the diminishing importance of income with increasing GDP. This is premised on the belief that people do not need an infinite amount of money for a decent quality of life.

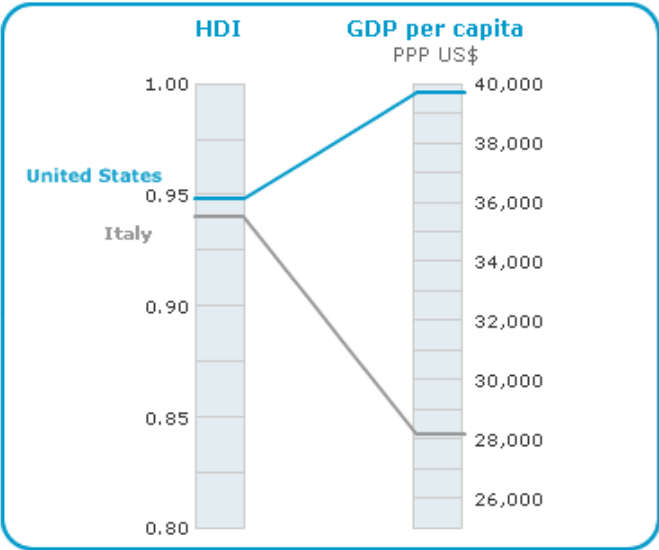
The scores for the three HDI components are then averaged in an overall index. The HDI is currently calculated for 177 countries and areas for which data are available.

While the concept of human development is much broader than this composite measure, the HDI offers a powerful alternative to GDP as a summary measure of human well-being. It provides a useful entry point into other rich information contained in the indicator tables covering a wide range of human development issues presented each year in the Human Development Reports.

What the HDI reveals

The HDI reveals that some countries do better on human development with relatively low GDPs per capita. For example, Italy’s GDP per capita is only about two-thirds of that of the United States but the two countries have similar HDI values (see Figure 1).

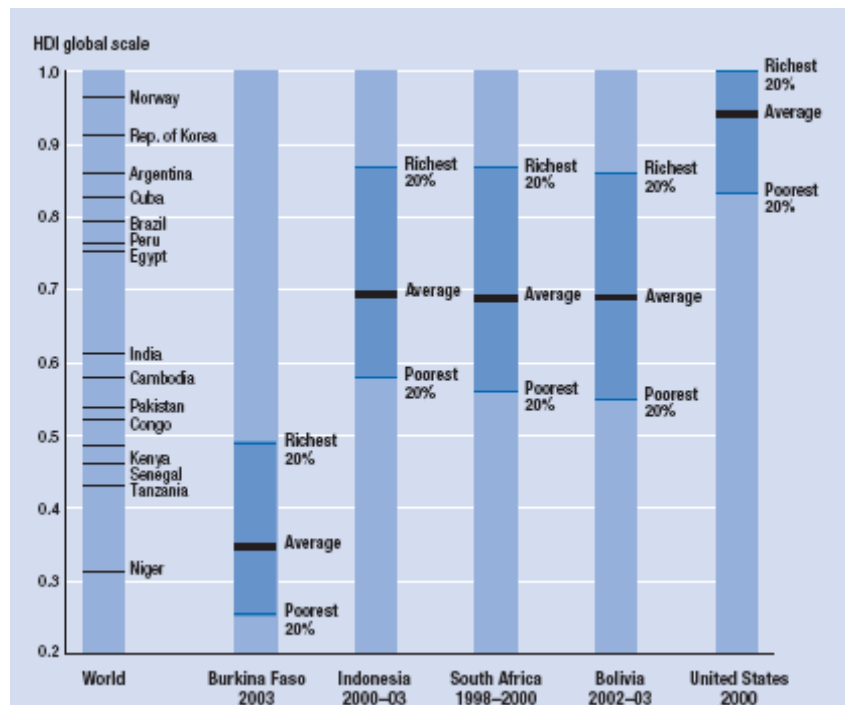
Figure 1: GDP vs. HDI; comparing Italy and USA



Source: HDRO web site <http://hdr.undp.org>

Disaggregating the HDI by income quintiles for countries for which representative data are available is also revealing. For instance, the gap between the value for the richest 20 per cent and the poorest 20 per cent of households in the United States is about 17 per cent. This is similar to the gap between average HDIs for the United States and Cuba respectively. In other words, while the richest 20 per cent in the United States would be at the top of the HDI league table, the poorest 20 per cent would be at the same human development level as people living in Cuba (see Figure 2).

Figure 2: Human development index by income groups



Source: 2006 Human Development Report

The variation in HDI value marked by unequal opportunities and capabilities calls for public policies aimed at equalizing opportunities and choices. Apart from the moral imperative to overcome extreme inequalities in income, access to education and health, inequalities pose a threat to national and global securities.

History of the human development concept

For decades, the economic growth paradigm dominated the national development discourse. However, in the 1980s unemployment levels escalated; and access to social services deteriorated in many countries including some industrialised countries while at the same time, economic production was expanding. In other words, high rates of economic growth did not automatically translate into improved human well-being. During the same period, some countries were registering improvement in human well-being with modest economic growth. These raised questions around the nature, distribution and quality of economic growth. It became clear that economic growth alone is not an adequate yardstick for a country's level of development. The need for a conceptual shift and alternative policy options that create a balance between economic growth and protection of the interest of poor and marginalised members of society became imperative.

The HDI, which was introduced in the first Human Development Report published in 1990, was a response to this demand. The idea of a composite index that measures socio-economic progress was conceived by Mahbub ul Haq a renowned economist, whose vision was to come up with one measure which is as crude as the GDP, but "not as blind to social aspects of human lives as the GNP is".

Limitations of the HDI

Like any other composite index, the HDI suffers a limitation of not capturing all the different dimensions of human development. Data availability poses a major challenge to capturing other important dimensions of human development such as political freedom, environmental sustainability and degree of people's self respect.

Secondly, the HDI is not designed to assess progress in human development over a short-term period because some of its component indicators are not responsive to short-term policy changes. Thus, the index partially measures past achievements as the components are made up of both stock and flow variables.

Future Possibilities

Since its introduction in 1990, the HDI's analytical framework, methodology and data have been subjected to rigorous scrutiny. Some of the major criticisms have led to major refinements of the methodology and component indicators but the index continues to evolve. For example, the HDI by income groups, calculated for 15 countries (13 developing and 2 developed) with data and published in the 2006 HDR, points to a need for bringing out inequalities in HDI for evidence-based planning. This is one area that the HDRO would like to extend to as many countries as data availability would allow.

Another future plan is to construct a separate HDI for women and for men to better present gender inequalities in human development. But this depends on reliable data on income for women and for men.

There are also discussions around capturing the environment dimension of human development either as part of the HDI or as a new index. However, these discussions are at a very early stage and data availability will inform any the final decision.