Gross Domestic Product and Neoliberalism: Flawed Interpretations of Economic Prosperity

Each year, acclaimed economic institutions publish economic reports filled with optimism—gross domestic product (GDP) has increased, unemployment remains low, and inflation is under control. However, real-world market conditions often diverge from this theoretical prosperity. Economic growth cannot be meaningfully defined by statistics alone–namely rising production (GDP), low unemployment, and controlled inflation.

Irrational adherence to neoclassical economic theory–favoring fiscal discipline, inflationary management, and structural reform (e.g., liberalization, privatization, and deregulation)–lies on flawed assumptions: that producers and consumers act rationally, markets are inherently efficient, and production alone holistically reflects the health of an economy. To truly understand and guide economic development, we must move beyond the narrow framework of GDP and, instead, construct a multidimensional framework that incorporates behavioral theory, psychological realities, institutional strength, long-term developmental goals, and political accountability as the foundation of modern macroeconomic thinking.

GDP measures the total market value of all goods and services produced, but it excludes non-market activities such as household labor, volunteerism, and informal economies; additionally, it obscures structural and qualitative composition—such as income distribution, productional authenticity, technological advancement, financial stability, fiscal accountability, employment productivity, ideological innovation, political responsibility, educational value, research and development (R&D), social well-being, morality and gratitude, and the sustainability of growth—the very foundations for our modern democracy. By attaching equal monetary weight to all market activity, GDP's simplified short-termism obscures long-term consequences, supply-chain implications, and subjective value. Growth cannot be defined by monetary output alone, but by the broader societal and ethical impact it entails. New methods of economic thinking must be adopted to more accurately reflect growth, prosperity, and our standard of living.

Another limitation lies in GPD's single-factored dependence on market value. Given that markets are often inefficient and participants are not purely rational, prices can be distorted by externalities such as behavioral tendencies and information asymmetry. Hence, if prices are unreflective, then GDP, by extension, misrepresents the true fundamental value of production. Coupled with the law of diminishing marginal utility—positing that utility decreases as production quantity increases and markets therefore must optimally produce goods—this flaw shows that growth cannot be measured in pure volume; instead, production must be strategically managed to maximize resource efficiency while minimizing waste.

Historically, GDP emerged as a response to crises. During the Roaring Twenties, the Great Depression, and the New Deal era,nations sought a straightforward method to quantify economic performance. GDP offered a simple measurement of the scale and structure of economic activity. In the following decades, GDP assumed greater prominence—guiding the implementation of fiscal and monetary policy, New Deal reforms, and World War II production. As a result, GDP gained substantial recognition, becoming standardized through the establishment of the Bretton Woods system.

However, the neoliberal pursuit of GDP growth engendered many problems. The 1970s saw severe economic stagnation, eroding confidence in the postwar consensus of structural stability and Keynesian principles. Rather than strengthening and reforming these institutional safeguards, leaders pivoted to free market-oriented solutions such as deregulation, low interest rates, privatization, and financialization. This shift to short-termism obscured long-term structural weaknesses, leading to wage stagnation, inequality, precarious labor markets, and disempowered unions. What manifested was a pattern of recurrent economic crises, including the oil shocks, debt crises, dot-com crash, and the 2008 financial meltdown.

The neoliberal era dismantled the postwar economic vision because it fundamentally changed how policymakers understood economic success and what they were willing to sacrifice to achieve it. Instead of treating growth as the result of strong institutions—like labor protections, regulated markets, and public investment—growth itself became the primary target. This shift created pressure to remove any perceived "barriers" to output, even when those regulations and protections were critical for long-term stability. Solidified under Ronald Reagan in the U.S. and Margaret Thatcher in the U.K., and influenced by thinkers like Friedrich Hayek, Milton Friedman, and the Chicago School, neoliberalism posited that free markets are inherently efficient, and that government intervention distorts price signals and incentives. Reagan's policies—often encapsulated in the term "Reaganomics"—focused on supply-side economics, characterized by massive tax cuts for the wealthy (e.g., the 1981 Economic Recovery Tax Act), deregulation of financial and labor markets, and the privatization of public services. The theoretical claim was that reducing the burden on capital and high-income earners would increase investment, spur innovation, and eventually lead to broad-based prosperity through a "trickle down" effect. In this sense, deregulating finance, weakening labor protections, and cutting public spending appeared as rational strategies to "unleash" growth. But by removing many of these institutional safeguards, economies became more vulnerable to shocks, inequality deepened, and the feedback loop of crisis and austerity intensified. The redefinition of policy priorities—growth first, structure later—was rooted in a fundamental misunderstanding: that GDP could be engineered through speed and scale rather than through stability and equity.

Deeper structural flaws in neoliberalism lie in its underlying theories and assumptions. A thorough examination reveals its shortcomings not just philosophically but also in practical application:

1. The Laffer Curve and the myth of self-financing tax cuts: This theory posits that there is an optimal tax rate that maximizes government revenue by increasing incentives through lower taxes. While theoretically valid at the extremes, empirical studies have shown that most tax cuts—especially those benefitting the wealthy—fail to generate sufficient economic activity to offset lost revenue. This is due to the presence of surplus value and informational gaps. In practice, supply-side tax cuts have increased deficits, widened inequality, and destabilized markets. Additional research suggests that high-income individuals exhibit inelastic labor supply behavior, meaning they are already maximizing their work hours.
2. Neoliberalism often justifies inequality through trickle-down economics—the belief that enriching capital owners and top earners leads to increased investment, job creation, and eventual benefits for lower-income groups. This assumes capital accumulation fuels productive investment rather than rent-seeking. However, from a Marxian surplus value perspective, capital owners extract more from labor than they return in wages, meaning that income tends to accumulate upward, not downward. Profits are increasingly

reinvested in financial instruments, stock buybacks, or offshore assets, not in wages or new production. For example, during the 2010s, U.S. corporations posted record profits and received substantial tax cuts; however, real wage growth remained stagnant, as capital was directed toward share repurchases and executive compensation rather than worker income. The concept of surplus value—the gap between labor output and wages paid—presents an enduring challenge to achieving equality under neoliberal systems.

3. Neoliberalism assumes market efficiency and price accuracy (in other words, that prices accurately reflect the underlying value of the product). But in the presence of externalities—cost or benefits not reflected in market prices—this assumption breaks down. Classic examples include:
    a. Pollution and environmental damage: Firms exploit natural resources to maximize revenue, thereby producing at higher-than-optimal levels because social cost isn't internalized.
    b. Education and academic enrichment: These are underprovided by the market, as their private return is often lower than the social return. Firms are disincentivized to invest, as they do not directly profit from these activities.
    c. Mental health and social manipulation: The profit potential behind the creation of social media has industrialized emotions like jealousy, comparison, and envy.

The First Fundamental Theorem of Welfare Economics (that competitive markets lead to Pareto efficiency) only holds in the absence of externalities, perfect information, and rational actors. In reality, none of these conditions are ever met due to rapidly changing market dynamics. This undermines one of the key justifications for limited government intervention.

The 2008 financial crisis demonstrated that the Efficient Market Hypothesis was dangerously flawed. Prices were artificially inflated by speculation, herding behavior, and opaque financial instruments such as subprime mortgage loans and credit default swaps. Regulators and economists assumed self-correction and minimal risk, but the result was a system-wide collapse. GDP had grown artificially through leverage and speculation but not through real value creation.

4. Another pillar of neoliberal economics is the idea of the rational, utility-maximizing individual—central to microeconomic demand theory, consumer surplus models, and cost-benefit analysis. However, behavioral economics, pioneered by Daniel Kahneman, Amos Tversky, and Richard Thaler, has shown that humans systematically deviate from rationality due to biases, heuristics, and cognitive limitations. People often demonstrate present bias by overvaluing immediate rewards over long term-benefits. They exhibit loss-aversion (feeling losses more intensely than equivalent gains), and are swayed by status quo and confirmation bias. Therefore, if consumers are not rational, market outcomes may not be welfare-maximizing. Deregulated consumer markets can actually harm individuals while contributing to GDP, allowing GDP to rise even as well-being declines.
5. Empirical studies have shown that highly unionized countries enjoy both strong worker protections and high productivity. However, the U.S. and U.K. have taken a different approach—assuming that fewer restrictions, expanded choices, lower barriers, and broad deregulation lead to flexibility, mobility, and competition. This approach was intended to reduce market frictions and wage rigidity, based on the premise of worker rationality. But

in real labor markets, especially those with rising employer concentration, firms often exercise monopsony power in local or sector-specific markets. This allows powerful firms to artificially suppress wages below competitive levels. Additionally, job switching is constrained by real-world costs, such as geographic immobility, information asymmetry, switching costs, and health insurance ties. Workers have less bargaining power, making labor markets less mobile and flexible than theory assumes. Furthermore, “flexibility” often translates to insecurity.; The gig economy, zero-hour contracts, and other deregulated arrangements are marketed as “flexible,” but they frequently result in lost benefits, income unpredictability, weaker legal protections, and the erosion of collective bargaining rights. All of this presumes that workers are rational agents and that competitive pressure is applied to labor and wages—but in practice, competition among firms is weak and the benefits are captured at the top rather than shared with workers. As a result, deregulation has produced precarious work, stagnant wages, and widespread worker insecurity, despite rising GDP. This signals that risk is being redistributed from firms to individuals, undermining social cohesion and long-term human capital development.

Speculative bubbles, like those of the Roaring Twenties or the early 2000s, illustrate how rising GDP and economic output do not necessarily lead to greater happiness, security, or social cohesion. Throughout the 20th century, periods of rapid growth created material abundance, but they also bred complacency and overconfidence in perpetual expansion. In modern times, political fragmentation, democratic irresponsibility, and declining moral values present a serious challenge to societal stability. Growing inequality, declining social trust, and worsening mental health have taken root. Cultural shifts fueled by consumerism and social media have amplified envy, status anxiety, and toxic comparison, eroding traditional values like gratitude, community, and the dignity of work. Younger generations are growing up in societies where success is measured by visibility and wealth, rather than purpose or contribution. Economic growth, when untethered from moral and institutional foundations, can deepen social fragmentation rather than resolve it.

A growing body of scholarship and policy innovation has emerged to challenge the dominance of GDP as the primary measure of economic progress, advancing more comprehensive frameworks that reflect human well-being, equity, and ecological sustainability. Influential economists such as Amartya Sen and Martha Nussbaum have laid the philosophical and methodological groundwork through the Capability Approach, which emphasizes individuals’ real freedoms and opportunities over aggregate output. This perspective has directly shaped the United Nations Human Development Index (HDI), which incorporates income, education, and life expectancy as core dimensions of development. In response to the 2008 financial crisis, the Stiglitz-Sen-Fitoussi Commission urged governments to move "Beyond GDP," advocating for metrics that capture quality of life, inequality, and environmental sustainability. Similarly, Kate Raworth’s Doughnut Economics framework proposes a model that defines a “safe and just space for humanity,” bounded by ecological limits and social foundations. It offers a visual and policy-relevant alternative to linear growth models. On the national level, Bhutan’s Gross National Happiness (GNH) index explicitly rejects GDP as the central measure of prosperity, incorporating nine domains ranging from psychological well-being to ecological resilience. In practice, this shift has begun to influence public budgeting. For example, New Zealand’s 2019 Wellbeing Budget, introduced under Prime Minister Jacinda Ardern, prioritized mental health, child poverty reduction, and indigenous rights over conventional growth metrics. Additionally, tools like the Genuine Progress Indicator (GPI) adjust traditional economic output by accounting for social costs such as pollution, inequality, and the loss of ecosystem services. GPI has been piloted in several U.S. states. These efforts signal an important and growing recognition that GDP is an inadequate, and often misleading, proxy for societal progress.

If we continue to view GDP as the ultimate measure of progress, society will face a slow but certain unraveling. The warning signs are already here, yet many fail to see this trajectory due to deeply ingrained cognitive biases. Human nature favors confirmation, self-praise, and comfort in the familiar. We take abundance for granted, always striving for more, while never questioning the cost. This mindset must shift. The simplest and most urgent change we can make is to stop treating GDP as the singular yardstick of economic success. Economics, as a field of study, is too intellectually rich to be reduced to one number. We must adopt a more objective, multidimensional perspective that reflects well-being, equity, resilience, and sustainability. This can be achieved through the following approaches:

1. We must replace the model of Homo Economicus with one that recognizes humans as bounded and embedded agents, recognizing that humans are influenced by institutions, norms, identity and cognitive limits. Economic models should integrate findings from behavioral economics, sociology, and psychology. We must replace pure utility-maximization with models that reflect satisficing, habit formation, and status-seeking behavior.
2. We must critically challenge the notion that growth, measured in prices, is imperative for prosperity, employment, and welfare. Frameworks must be better optimized for sufficiency, stability, and broader societal factors, not exponential growth. Efficiency should not be the primary goal, and distribution should not be a separate “political issue.” Power relations, wealth distribution, and ownership structures should be integrated with historical, institutional, and bargaining-power-based wage models. We must stop assuming that markets “naturally” produce fair outcomes by starting to analyze who holds power, and what could be done.
3. Acknowledge co-evolution of preferences and institutions. Policies and social norms shape each other over time. Models should draw from institutional economics and complexity theory, incorporating concepts like path-dependence, hysteresis, and feedback loops. Policy should be generative and capable of reshaping norms, not just optimizing within fixed constraints.
4. Reframe the economy as embedded in society and the biosphere. We must move beyond the conventional assumption that the economy is a closed, abstract system focused on prices, outputs, and equilibrium. A new paradigm would support the economy as a subsystem of both the biosphere and society, governed by thermodynamic laws, material flows, and social cohesion. Equilibrium models must be replaced with systemic dynamics, non-linear modeling, and entropy-based accounting. We must recognize energy, time, and ecological degradation as core inputs into value, not “externalities.”
5. Reconceptualize scarcity and abundance. We must also rethink economics as not the study of allocating scarce resources but the study of the relation between resources, society, and institutions. Modern scarcity is often artificial, while abundance of care, knowledge, and relationships is undervalued. We must reconstruct economics to value reproductive labor, the commons, and informal economies.
6. Redefine intertemporal ethics. The current assumption holds that discounting the future is

rational; value is price. However, intertemporal ethics must shift. Future generations, non-human life, and slow-building social goods must be treated as real and valuable. We must challenge the use of net present value (NPV) and discounted cash flow (DCF) in public decision-making, developing models where long-term resilience and irreversibility matter more than short-term returns.

7. Promote a new economic ethic. Humans must learn to embody humility and gratitude. Life should not be viewed through the lens of consumption, competition, and comparison. Neoliberalism, with its valorization of individual success and material accumulation, has bred a culture of status anxiety and envy, leading to the gradual diminishing of morality and cultural stability. Increasing rates of depression, burnout, and social isolation must be counteracted by a shift in public perception of growth. We must accomplish this by developing an economic ethic that privileges gratitude, sufficiency, and purpose, rather than perpetual desire. Economics must be organized to enable dignity, stewardship, and meaning, not just output.
8. Engage in institutional reform. Meaningful reform requires structural and institutional thinking that strives to understand how economic outcomes emerge from deep architectures. For example, inequality is not simply a matter of redistribution, but of who owns productive assets, how markets are structured, and what social contracts underpin employment and care. To move forward, economists and policymakers must adopt a systems perspective, seeing the economy as a dynamic, embedded, and multi-layered organism. This means investing in state capacity, collective intelligence, and long-term institutions that can adapt and coordinate. Theory and policy should be weaved together into a comprehensive economic network centered around a new interdisciplinary paradigm.
9. Build a new interdisciplinary paradigm. The failures of neoliberal economics require a new ideological synthesis that draws strength from multiple schools of economic theory. From Keynesianism, we retain the insight that aggregate demand, fiscal policy, and macro coordination are essential to economic stability. From developmental economics, we learn the importance of state-led industrial policy, institution-building, and strategic planning for national progress. From the Austrian school, we acknowledge the centrality of entrepreneurial discovery, subjective value, and institutional knowledge in a dynamic and uncertain society. This new framework must integrate ecology, sociology, psychology, ethics, and history to ground economic thinking in human and societal realities. Growth must be understood not as GDP, but as a comprehensive foundation for well-being and collective resilience.