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Most Everything Is Better Than You Think

by Richard W. Rahn

In 1914, just over a century ago, the average worker had to work about three hours to buy a bushel of wheat. Today it takes five minutes for the average American worker to buy that same bushel of wheat. The real (inflation-adjusted) price of aluminum is now about one-fifth of what it was in 1914. These ongoing, real price declines are characteristic of almost every agricultural and industrial commodity.

Improvements in a person's standard of living come from increases in real income — both earned and unearned, inflation-adjusted reductions in the price of the goods and services, and new goods and services never before available. For example, assume average inflation is two percent per year, and Jane Doe's after-tax income increases also two percent per year — that is no real increase in income.

But if the price of beef has gone up by three percent and the price of chicken has only gone up by one percent, Ms. Doe, being a typical person, will consume less beef and more chicken. By substituting the lower priced good for the higher priced good, Ms. Doe has some extra money which she uses to buy an iPhone.

The iPhone enables Ms. Doe to get a lot of "free stuff" that she used to have to pay for — such as online newspapers, all sorts of free entertainment, a better camera, an alarm clock, etc. etc. This free stuff is known as avoidable costs. So, even with a "stagnant cash income," Ms. Doe is better off because of the advances in technology. The situation for most people is even better, because real cash wages are beginning to rise again and the improvements in technology are accelerating — even though the government is having a very hard time measuring these real improvements.

Gross Domestic Product (GDP) has been used as the basic measure of national well-being for many decades. GDP is the sum of the monetary measure of the market value of all final goods and services produced in a country or region in typically one year. Economists recognize that there are many flaws with the GDP measure and related statistics, such as the measures of inflation — but how to correct these flaws is difficult and a subject of considerable debate.

Back in the 1980s, as chief economist of the U.S. Chamber of Commerce, I served on a government committee to supply recommendations on how to improve the measures of inflation. Everyone understood that the 1985 basic Chevrolet sedan was a very different vehicle from the 1965 Chevrolet, given all of the improvements that had been made — and so just comparing the price increases of the car over time did not give a true measure of inflation.

It is relatively easy to measure price inflation or deflation in basic commodities like wheat because the product has remained constant. This is not true with manufactured goods and services, many of which are changing at an increasingly rapid rate. Each year, people spend less of their income on basic commodities and more on new goods and services.

The automobile is about to go through an even more radical change as we move to self-driving and autonomous cars — which are essentially a whole new product category. Many people will no longer buy a car; instead, relying on transportation-on-demand (the autonomous car) which will reduce the overall demand for automobiles — because the existing stock will be better utilized rather than just sitting in a parking lot.

This will reduce the relative GDP number for the automobile industry, but will enable consumers to have an increase in their real disposable income, which they can spend on other goods and services. The present government economic data collection and evaluation systems are not equipped to deal with these radical changes. How does one measure the great benefits from the enormous reduction in automobile related deaths that will result from the new technologies?

The Trump administration has been undertaking a massive deregulation effort in order to get rid of regulations that are counterproductive and do not meet reasonable cost-benefit tests. This will reduce the direct regulatory expenses made by government but will cause a far larger reduction in private business and personal expenses made to support regulations.

These reductions in expenses will cause a reduction in the reported GDP number spent on those regulations. But businesses and individuals are now likely to spend those funds on much more productive activities, thus offsetting the "loss" in reported GDP from the cessation of regulation. Even though the reported immediate GDP gains might merely offset the reported GDP losses, the overall welfare of the people will be higher and the chances for greater future economic growth enhanced.

On net, the ways that GDP and inflation numbers are now collected and reported probably understate the true improvement in real per capita income experienced by most people. As we move to a world of even more rapid technological change due to increased use of artificial intelligence (AI), the real improvements most people will experience will be far greater than our present ability to measure them.

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