

## Economics, happiness and public policy

Wednesday 1:15pm – 2:55pm

### Chair: Yew-Kwang Ng

Director, Centre for Increasing Returns and Economic Organisation, Department of Economics, Monash University

### Happiness and wealth: Implications for public policy

#### Robert Cummins

School of Psychology, Deakin University

The idea that money is a proxy for happiness is deceased. In its place is a rapidly emerging understanding about the nature of the relationship between physical resources and the stable component of happiness referred to as Subjective Wellbeing (SWB). The main determinant of SWB is the genetic prescription of a 'set-point' for SWB which varies between individuals within the range of 60 – 90 points on a 0 (completely dissatisfied) to 100 (completely satisfied) scale. Thus, people normally feel positive about themselves and this positivity is maintained even in the face of mild adversity by a process called SWB homeostasis. Severe adversity, however, will defeat this system and, when that occurs, people experience the loss of positive feelings which we associate with depression. Homeostatic defence is assisted by internal and external buffers. The two major external buffers are relationships and money. In relation to the latter, the purpose of wealth, in relation to happiness, is to function as a flexible resource to assist homeostatic defence. Thus, money assists people to avoid unhappiness. My paper will outline these ideas and suggest that average population happiness could be increased by a redistribution of wealth.

### Relative income, happiness and utility: An explanation for the Easterlin paradox and other puzzles

#### Paul Frijters

School of Economics and Finance, Queensland University of Technology

The well-known Easterlin paradox points out that average happiness has remained constant over time despite sharp rises in GNP per head. At the same time, a micro literature has typically found positive correlations between individual income and individual measures of subjective well-being. This paper suggests that these two findings are consistent with the presence of relative income terms in the utility function. Income may be evaluated relative to others (social comparison) or to oneself in the past (habituation). We review the evidence on relative income from the subjective well-being literature. We also discuss the relation (or not) between happiness and utility, and discuss some non-happiness research (behavioural, experimental, neurological) related to income comparisons. We last consider how relative income in the utility function can affect economic models of behaviour in the domains of consumption, investment, economic growth, savings, taxation, labour supply, wages and migration.

### Unhappy growth

#### Ian McDonald

Department of Economics, University of Melbourne

In *The Challenge of Affluence*, Avner Offer argues that the failure of happiness to increase in recent decades even though incomes have risen is due to increases in a number of social and personal disorders, such as family breakdown, addiction, mental instability, crime and obesity. Offer puts forward a thesis to explain this failure. Offer's thesis is that people find it difficult to adjust to economic growth. Novel products can have delayed effects that cause social and personal problems. Because many people are myopic, they consume excessively and are then unpleasantly surprised. This paper develops a model of Offer's thesis and discusses how the difficulty of adjusting to new products will influence the socially optimal rate of economic growth. Various applications of the model are also discussed.

## Happiness studies: Some policy implications

### **Yew-Kwang Ng**

Director, Centre for Increasing Returns and Economic Organisation, Department of Economics, Monash University

Recent happiness studies by psychologists, sociologists, and economists have produced many interesting results. This has important implications, including: The need to improve happiness studies to make the results more reliable and interpersonally, intertemporally, and interculturally more comparable. The need to focus less on purely objective (including economic) variables and more on subjective well-being. In particular, the focus on GDP should be supplemented (if not replaced) by such more acceptable national success indicators as the environmentally responsible happy nation index. Welfare economics and cost-benefit analysis that are currently based on economic factors (which are in turn based on preferences) should be revised to be based on happiness or welfare. Public spending on areas important for welfare should be preferred over private consumption that is largely no longer important for long-term welfare at the social level. Public policy should put more emphasis (than suggested by existing economic analysis) on factors more important for happiness than economic production and consumption, including employment, environmental quality, equality, health, and safety. Above all, scientific advance in general and in brain stimulation and genetic engineering in particular may offer the real breakthroughs against the biological/psychological limitations on happiness.