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nef response

Well-being and the Role of Government

In January the Institute of Economic Affairs (IEA) published a collection of essays that criticised the idea of using well-being in policymaking. In this paper we respond to the IEA's arguments and question some of the conclusions it comes to about well-being.

Introduction

In January the Institute of Economic Affairs (IEA) published *'…And the pursuit of happiness: Wellbeing and the Role of Government',* a collection of essays that criticised the idea of using well-being in policymaking[1]. This generated a substantial amount of public attention and debate about the issue, which we at **nef** welcome. However, we strongly disagree with the conclusions that the IEA reached.

The publication as a whole raises a range of interesting objections to the use of well-being to guide public policy, deserving of consideration. However, it also presents a number of arguments that over-simplify the current state of the well-being research; draw some highly speculative conclusions; and misrepresent opposing viewpoints. The following pages examine these claims and refutes them.

It also examines a broader issue, namely the IEA's deeper ideological objection to the use of well-being measures. If one believes that any government action is an intrusion into the lives of citizens, then one is unlikely to support a well-being approach. We finish by examining the implicit assumptions of the essays in the IEA report, that government should not intervene in public life.

Well-being and GDP

> *The idea put forward by the British government that economists and politicians pursue policies directed towards maximising GDP is a 'straw man'. Government has always had a multitude of different objectives and government policy would be very different today if economic growth were the single priority.*
>
> Paul Ormerod

Government has always had a range of objectives, but we would argue that much of current policy debates are biased towards one indicator, GDP growth. The BIS website, for example, currently states that "every part of

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government is focused on [growth]".[2] Ormerod himself acknowledges this, as he describes how much effort has been put into attempting to predict the factors that will lead to increases in GDP.

Policymakers make trade-offs between different outcomes and to do so examine a wide range of indicators, representing a wide range of policy objectives. However in practice they often select the option that best promotes economic growth. For example, education policy targets have for years been expressed in terms of the qualifications required based on the needs of employers, whilst the wider benefits of education in terms of equipping people to live rounded lives are almost never mentioned, at least at headline level. This is not to suggest that the needs of employers don't matter but that at present there is a bias towards this indicator.

We suspect that this is largely because policymakers have accepted classical economic models which suggest that increasing income is the most efficient means of promoting well-being. And policymakers have previously never had systematic access to well-being data with which to assess the costs and benefits of policies in these terms, or headline indicators of well-being at which to aim. The Office for National Statistics' (ONS) robust and systematic measurement of well-being, begun in 2011, will now give policymakers an evidence-based method to examine the likely and observed effects of their policies, not just on growth but on the lives of citizens as well.

Subjective well-being measures

> *Happiness measures are short-term, transient and shallow measures of people's genuine wellbeing.*
>
> Peter Boettke and Christopher Coyne

Some contributors raise important concerns around the issue of defining 'happiness' and 'well-being' and the potential narrowness of the concepts. In addition to Peter Boettke and Christopher Coyne (quoted above), Mark De Vos critiques well-being economics as having an *"egoistic, hedonistic, individualistic bias".* These objections are based on the idea that well-being data is produced simply by measures of moment-by-moment, or day-by-day, happiness, which is not what most proponents in fact suggest. The conception of well-being that David Cameron talked about in this speech launching the National Well-being programme was a much broader one – for example, he talked about 'control', 'purpose' and 'belonging'. Many proponents, including **nef**, argue that these factors should be directly measured, and this 'eudaimonic' approach is reflected in one of the ONS's four key subjective well-being measures. Once this issue is addressed, in many ways it appears that De Vos supports the use of well-being measures: *"Adding happiness to the array of perspectives on policy issues can insert a human angle and force us to ponder effects that would otherwise remain ignored".*

Concerns about the fluctuations of 'moment-to-moment mood' raised in the publication can be largely discounted once large enough survey samples are considered (such as the 200,000 of the Integrated Household Survey, within which the subjective well-being questions will be included). Good survey and sampling methodologies mean that these fluctuations average out and ensure that these factors do not have a systematic impact on results. In addition, if a range of questions, covering different aspects of well-being, such as meaningful activities or life satisfaction, are asked, then the potential of fluctuations in moment-to-moment moods to affect overall scores will also be decreased.

A detailed methodological criticism is made by Ormerod about the use of subjective well-being measures. He notes that measures such as life satisfaction and overall happiness commonly use a bounded scale, so that respondents have to pick a point between e.g. 0-10, 0-5 or 0-3 in rating their happiness or satisfaction. He argues that because respondents who have chosen the highest value cannot subsequently score any higher, even if their well-being rises, the measures fail to adequately capture changes in levels of well-being. Furthermore, he says, as subjective well-being is related to variables such as GDP or income, which in theory appear to be able to rise without limit, any increases that this rise brings will become increasingly difficult to recognise on a bounded scale.

This is a genuine issue. Hypothetically, if respondents were all rating themselves as the highest score, then of course they cannot score any higher. However, in practice it is highly unlikely that the bounded scale is the explanation for the logarithmic relationship between income and well-being, which we describe in more detail later. Evidence shows that the curve flattens before the bounded scale has become a limiting factor, and there is good empirical evidence and theory that attributes this to a genuine effect of diminishing marginal returns. In addition there are differences between individuals and populations in the point at which the curve flattens. It is important not to overstate the difficulties involved.

Much of Ormerod's argument is focused on the use of three-point response scales, which have been largely replaced by seven or eleven point scales in most well-being research. Differences between average levels of reported well-being in developed countries show that the measures are far from saturated, with considerable increases required for the UK to reach the levels reported in Denmark, for example. Ormerod fails to adequately recognise the research which has shown that life satisfaction *has* changed in response to economic conditions (e.g. Wolfers & Stevenson, 2008; Easterlin *et al.,* 2010; Di Tella *et al.,* 2003). What is more, bounded measures pose no difficulty in being used to identify changes in the slope of the curve, and thus the income levels at which income becomes relatively less important in driving well-being.

Finally, using a bounded scale in this setting may in fact be the most appropriate way to reflect reality: after all, when people rate their happiness, they are doing something like considering how they feel now compared to the happiest they could be, or the unhappiest they could be. People don't seem to consider happiness to be a boundless concept and it seems sensible to suppose that there is an upper limit to happiness. It may be that it is only classical economic theory, predicated on limitless growth, which considers limits in this context to be a problem.

Well-being objectives

There are several instances in the IEA publication where the debate is over-simplified. For example, in a corollary of the critique that GDP is the only measure governments currently pursue, Paul Ormerod suggests well-being proponents believe that well-being measures should be the *only* measures that guide policy in the future. Mark De Vos objects to the idea that individual subjective measures of well-being would "supplant overall economic progress". But this is not what most serious proponents are suggesting. At **nef** we argue that subjective well-being indicators should form part of the way that we measure progress, not that they should be the only way. In '*Measuring our progress*', our contribution to the ONS consultation on measuring national well-being, we suggested that subjective well-being indicators should form part of a dashboard which would also include a set of Drivers of Well-being: objective indicators – such as GDP or unemployment – that would be used to help paint a full picture of national well-being.

We do not dispute De Vos' contention that "*to put it plainly and simply: happiness cannot be the sole measure if human beings are to survive over time.*" But we do argue that measures of well-being add to the information we already gather on the quality of life of individuals, in a way that can improve policymaking.

In the chapter by J.R. Shackleton on well-being at work, the impact of employment protection legislation on well-being is discussed. However, an assumption is made that promoting well-being at work *only* means protection legislation. While legislation may be part of the solution, trust and engagement between employers and employees are also widely emphasised means of achieving well-being at work.

Well-being and income

A contribution to the collection by Daniel Sacks, Betsey Stevenson and Justin Wolfers claims to provide evidence that undermines the Easterlin paradox – that despite large increases in per capita income, average happiness has remained relatively constant over time in a number of developed countries, but within and across countries, cross-sectional data shows rising income leads to increases in subjective well-being. Whilst the Sacks *et al* chapter shows that this pattern holds in a number of key countries (for example the USA, the UK, Germany), the authors present data showing a correlation between changes in log GDP and changes in life satisfaction in several countries. This contradictory finding forms part of a larger empirical debate, particularly between Stevenson, Wolfers, Sacks and colleagues on the one hand and Easterlin and his colleagues on the other, over what is an appropriate period of time over which to consider this relationship; which countries should be excluded from the analysis; whether particular data are of high enough quality; and how much the length of the time-series will affect the conclusions drawn.

This chapter raises some important points; but provides an inaccurate description of the basic relationship between well-being and income.

The chapter summary states:

> *Contrary to popular perception, new statistical work suggests that happiness is related to income. This relationship holds between countries, within countries and over time. The relationship is robust and also holds at higher levels of income as well as at lower levels of income. This calls into question the assertion that people are on a 'hedonic treadmill' that prevents them becoming happier as their income rises beyond a certain level of income.*

The finding that income is related to well-being is well-established in the well-being literature.[3] In fact, a review of cross-national studies found a *higher* correlation between log GDP per capita and measures of well-being (normally life satisfaction) than in this chapter, of between 0.5 and 0.7 (Diener & Biswas-Diener, 2002).

What the paper does not explain clearly enough is that using the logarithmic transformation of income (the 'log of income') allows the authors to plot as a straight line what is most naturally represented as a curve.

Statements such as "*we present evidence that wellbeing rises with absolute income: full stop"* underplay the fact that their evidence clearly demonstrates that there are diminishing marginal returns to increases in income.

Although the relationship between income and well-being may be robust even at higher levels of income, it is definitely *not* linear: as individuals get richer, there are diminishing marginal returns to increases in income, so as an individual becomes richer and richer, income matters *less and less* in terms of improving their well-being. The curved shape of this relationship is now established by a wealth of literature[4].

This is an important point. The initial inference from a continuous straight line is that, as an individual, if you want to maximise life satisfaction you should always strive to earn more and more money, no matter how wealthy you already are. But *log* income has little psychological meaning for people and so should not be the target for governments designing policies to maximise well-being (Seligman, 2011). This is because time is linear, not logarithmic, and is precious. This means that there are often better ways to spend this precious time to improve our well-being than by making more money – especially when you are already comfortably off.

This also suggests that there would be substantial gains to the overall level of well-being of a country if wealth was redistributed from the richest people to the poorest, something that directly contradicts the arguments in Christopher Snowdon's chapter on inequality and well-being.

However, whilst we feel that a clearer explanation of the relationship between well-being and income would have been better, we do welcome this paper as an important contribution to the empirical debate. After all, we of course agree that income matters – in our model of well-being income appears as an important factor in creating conditions for individual well-being. And we are pleased to see that the authors' conclusions, that "*subjective well-being data is indeed likely to be useful in assessing trends on global well-being"* and that "*the causal impact of income on individual or national wellbeing and the mechanisms by which income raises subjective well-being remain open and important questions".* This clearly supports our own arguments advocating the use of well-being data in policymaking.

Well-being and inequality

The chapter by Christopher Snowdon deals with the relationship between well-being and inequality and argues that there is a lack of evidence that the two are in any way related.

> *There is no evidence that equality is related to happiness. Indeed, the proponents of greater income equality admit that they are unable to cite such evidence and instead rely on very unsatisfactory forms of indirect inference. The clearest determinants of wellbeing would seem to be employment, marriage, religious belief and avoiding poverty. None of these is obviously correlated with income equality.*

There are papers which provide direct evidence of a correlation between inequality and average well-being in a country (Oishi & Diener, 2011; Winkelmann & Winkelmann, 2010; Senik, 2005; Alesina *et al.,* 2004). Data on this area is relatively scarce. Unlike with GDP, we don't have year-on-year Gini coefficients[5] even for those countries with the most organised statistical systems. But just as Phillip Booth argues elsewhere in the volume with regards to income – "*the absence of evidence of a relationship between well-being and income is not evidence of the absence of such a relationship"* – a lack of evidence of the relationship between inequality and well-being is not evidence of the absence of such a relationship.

Existing evidence is not properly represented by the author's arguments. When referring to a paper by Alesina *et al* (2004) he says, *"...the study showed that perceptions of fairness and social mobility are more important than inequality itself"* but nowhere in the paper is it claimed that perceptions are *more important* than inequality. Alesina and co-authors looked at Gini indices calculated at the state level (USA) and country level (Europe) and showed that overall, inequality is adversely associated with the well-being of Americans and Europeans (Alesina *et al.* 2004). They also found that there are differences in the income and ideological groups that have the *most adverse* associations with inequality in the two regions: overall happiness decreases with inequality in particular for poor and politically left-leaning people in Europe, whilst in the US it is the well-being of the rich that is associated with worse outcomes at higher levels of inequality. However despite differences in the particular groups, overall, the message is very clear: *"individuals have a lower tendency to report themselves happy when inequality is high, even after controlling for individual income, a large set of personal characteristics, and year and country (or, in the case of the US, state) dummies"*.

Further evidence from the work of Sacks *et al* that suggests a negative relationship between inequality and well-being is not referenced in the IEA collection. The Sacks *et al* contribution to the publication is based on a paper published in 2008 by Stevenson and Wolfers. This earlier paper discussed the different situations in Europe and the USA. In the case of Europe, the authors argued that there have indeed been increases in happiness over the last 50 years, and that this is consistent with the outcomes which would be expected from the economic growth observed over the period. In the case of the USA, however, there has not been an increase in happiness, which they explain, in the face of growing GDP, with reference to the fact that median incomes have not increased. This is a very plausible explanation, which says, in other words, that the benefits of growth have not gone to the average American, but rather to the richest. As the authors say there, *"the sharp rise in inequality over recent decades puts a large wedge between the rise in the log of average income (which is what we typically observe in macro data), and the average of log income (which is the relevant aggregate for predicting average happiness)"*. This evidence shows that whatever the benefits of increasing GDP, they have been neutralised by widening inequality.

Ideological differences

The above arguments represent significant but not fundamental challenges to the well-being agenda. However both the authors of the report and the panellists at the IEA's accompanying event[6] outline an ideological position that aims to reduce government involvement in citizens' lives. This seems to be the root cause of the IEA's dismissal of well-being, rather than the definitional and methodological issues raised in many of the chapters. The need to prevent 'coercion' by government (and sometimes 'authoritarianism' and 'totalitariansim') was mentioned frequently by the panellists at the IEA event, a number of them contributors to the report.

If one believes that *any* policies that restrict citizens' options, like taxation, are a form of coercion, then one is likely to believe that any tools to improve the design of these policies are also objectionable. This is not a viewpoint we share. but regardeless we would argue that while government exists, and makes policies bound to impact on people for good or ill, using well-being data is likely to lead to significant improvements in our ability to steer those impacts so as to best promote flourishing lives.

In addition to this implicit ideological difference, the report raises a number of ideological concerns. In the final chapter of the collection, Pedro Schwartz argues that happiness is not within the remit of government by applying (in his own words) a 'philosophical' argument:

> *Those who wish to use happiness economics in public policy have no effective way of determining whether an increase in wellbeing should be traded against justice, moral values or a decrease in freedom. It is a utilitarian philosophy which applies a principle that many might use in their own lives to the organisation of society as a whole. Applying such an overarching principle to the organisation of society as a whole is very dangerous.*

One might of course say the same about any overarching principle, for example economic growth or liberty. In fact, well-being is a less rigid goal than either of these and equating it with Benthamite utility is a parody. There is a utilitarian view of well-being, most commonly associated with Professor Lord Richard Layard, but Schwartz mistakenly assumes that there is no debate *within* the politics of well-being. For example, **nef** would agree that Layard sometimes goes too far in saying that happiness trumps all other goals. Nonetheless well-being clearly *is* a goal to which many other goals are subsidiary and so the prominence that he gives to it is not entirely undeserved.

The last three chapters, which comprise Part Three of the publication, are best described as anti-government polemic. They suggest that if well-being measures are used by governments, this necessarily conflicts with the goal of reducing the size of government.

But, in De Vos' chapter, he makes this case by proposing a false dichotomy between promoting hedonistic policies or doing nothing, allowing "bleak adversity" from which, De Vos claims, humans can "triumph". The author makes the analogy of parents raising children: *"Do we indulge them in the latest fashion, TV show and video game, or do we instead install discipline, hard work, teach the limits of money and the value of earned success?"* Of course proponents of the well-being agenda are not advocating either hedonism or bleak adversity and there is absolutely no reason to suppose that either is the correct aim of government action. **nef**'s eudaimonic[8] understanding of well-being as crucially about both feeling good and functioning well – for example pursuing meaningful activities and building strong relationships with others – is very far from a hedonistic view.

Conclusions

The range of methodological objections expressed in the IEA publication to using well-being in public policy can be comprehensively addressed and do not pose a serious threat to this agenda. And although there remain practical and ideological differences on the role of the state, importantly, their contribution shows that even sceptics are starting to engage with the debate.

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Endnotes

[1] Booth, P. (ed). (2011). *…and the Pursuit of Happiness: Wellbeing and the Role of Government.* London: The Institute of Economic Affairs.

[2] Front page of the BIS website: http://foresight.gov.uk/. Accessed 02/03/12.

[3] See for example, our recent working paper (2011) *Well-being: human well-being and priorities for economic policy-makers.* London: **nef**.

[4] See for example, MacKerron (2011); Easterlin & Sawafanga (2010); Layard *et al.* (2010); Kahnemann & Deaton (2010); Clark (2008); Dolan *et al.* (2008, 2006)

[5] Gini coefficients are the most commonly used measure of inequality. A Gini coefficient of 0 expresses perfect equality whilst a Gini coefficient of 1 reflects maximal inequality.

[6] The IEA hosted an event called 'Well-being and the role of government - can government policy make us happier?' on January 25th 2012.

[8] The Aristotlean theory of eudaimonia describes the good life in terms of an individual's interaction with the world.

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