THE USE OF HAPPINESS IN SOCIETY

Happiness economics should not imply happiness policy, argues **Jason Potts**

Happiness economics is one of the hottest new research fields in recent times, and increasingly, a fast track to top journal publications and research grants. Even the name makes you wish you'd studied economics. The problem, however, is that it's not just doctoral students and journal editors who think this. Political leaders such as Nicolas Sarkozy in France and David Cameron in the United Kingdom, and invariably more to follow, have already sought to galvanise a new role for the state in delivering aggregate happiness outcomes guided by new happiness metrics and policy. Worryingly, happiness economics is increasingly becoming a political project.

For example, in his 1997 survey of happiness and economic performance, Andrew Oswald, an economist at Warwick University, flatly concluded that 'Economic growth should not be a government's primary concern.' Behavioural economist George Loewenstein has said that he 'doesn't see how anybody could study happiness economics and not find themselves leaning left politically.' The policy implications section of most research in happiness economics is often unashamedly tilted towards an interventionist and redistributionist agenda. British sociologist Frank Furedi explains how 'what commentators describe as the Nanny State is more accurately described as a therapeutic state' and that 'the aim of today's happiness crusade seems to be to politicise the quest for self-fulfilment ...

This shift in government policy, towards attending to individuals' emotional needs, is seen as a step up from traditional redistributionist social policies.'

I want to highlight the political ambitions of happiness economics. But I also want to propose an alternative interpretation of what happiness economics can be about, namely, adaptation in the manner of Hayek's famous 1945 paper on 'the use of knowledge in society,' which explained how the price system coordinates distributed knowledge. I propose that 'happiness signals' work similarly, distributing knowledge about good choices, enabling learning and adaptation. Happiness self-organises and does not require government planning. Without this recognition, happiness economics (and happiness policy) is shaping up as Keynesian economics all over again.

What is happiness economics?
Happiness economics is the endeavour to measure, by survey, utility or happiness or subjective wellbeing (the terms are used

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interchangeably) on a 1–5 scale and then map that to economic correlates such as income, employment, inflation and the like. Happiness economics has arisen in parallel with *positive psychology*, also a 'new science' that focuses on the psychology of human potential. Happiness economics more or less has the same agenda, but works with economic correlates and the specific prospect of using economic policy to serve the ends of social happiness.

The seminal article was Richard Easterlin's 1974 inquiry into whether economic growth makes us happier. Using long-running global survey data on self-reported happiness mapped to real GDP growth, Easterlin found that economic growth doesn't make us happier. Although Justin Wolfers and Betsy Stevenson of the University of Pennsylvania debunked this statistical claim recently, for the past few decades happiness economics has sought to explain this 'Easterlin paradox' (the main

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explanations are 'adaptation set-point theory,' which supposes that we all have a 'natural happiness level' that we return to after positive or negative 'shocks,' and the 'relative income hypothesis,' which supposes that it is not absolute income that matters but our income relative to peers) and to ask 'if more income doesn't make us happier, then what does?' The depressingly favoured answer, it seems, is 'more government.'

Happiness economics intersects psychology, utility theory, and macroeconomic policy. First, happiness economics challenges a rudiment of modern microeconomics, namely the empirical principle that people's preferences and utility cannot be studied directly but only through observation of the actual choices people make (this is known as 'revealed preference theory' in economics, and claims that you cannot describe the utility of any choice on, say, a 1–5

scale, but only in rank comparison to something else, e.g. an agent prefers X to Y, but not in terms of a cardinal measure such that, say, X = 3 utils and Y = 2 utils, etc). Yet using survey methods from psychology, happiness economics argues for the scientific validity of direct survey-based measures of utility. Second, these cardinal measures are dependent variables in analysis of the happiness effect of independent variables such as unemployment, inflation, public goods, GDP, and political institutions. Happiness economics claims that changes in the independent variables can explain changes in happiness measures.

Happiness economics is composed of micro-foundations (in psychology), statistical methodology (econometric regressions over surveys and indices), and macroeconomics (inferred economic correlates). This micro-macro completeness, coupled with explicit empirical methodology, enables happiness economics to present itself as a coherent scientific framework with immediate and important policy implications. This is prima facie compelling. Here we have a new science connected to modern economics that departs in interesting ways. It's based on new data that say something can be done about matters of widespread or broad concern and also squares with popular politics such as more aggressive income redistribution, job security, and taxes on the rich or on 'unnecessary' consumption.

Happiness researchers back these forms of policy intervention because they seem to follow directly from their own findings. For example, one much publicised finding is that beyond relatively low levels of income, further income growth does not correlate with increased happiness. If absolute income growth does not cause happiness, then policies to promote economic growth (such as free markets) will, it is inferred, not increase happiness. This is taken as evidence that economic growth should not be a primary economic goal. Furthermore, if it is relative income or spending that really matters, then policies that reduce income inequality or increase the cost of luxury spending will, it is inferred, increase aggregate

happiness. This leads to arguments for much more 'progressive' income or consumption taxes. If being unemployed is a source of unhappiness then, it is inferred, policies to promote income security will increase happiness. And so on. Wherever an economic factor negatively correlates with aggregate happiness, a countervailing (and often populist) policy will invariably be proposed.

A further class of findings concerns unemployment and inflation, both correlating with unhappiness. This is taken as evidence against the voluntary unemployment hypothesis (in New Classical macroeconomics) and against the monetarist hypothesis that only unexpected inflation is problematic. Bruno Frey and Alois Stutzer extend this to include institutional factors connecting democratic participation to happiness. It is noteworthy that Frey and Stutzer are rare examples of happiness researchers who are sceptical of inferring interventionist social welfare proposals. Instead, they direct policy attention towards economic institutions that 'lead to the best possible fulfilment of individual preferences.'

A 2007 IEA monograph by Susan Johns and Paul Ormerod reviews the statistical foundations of happiness economics. They point out that not only do time series data on income growth not seem to correlate with increased happiness but a raft of other factors that might be expected to influence happiness—such as reduced inequality, discrimination, growth of public spending, longevity, and even the rise in depression—also show no correlation with happiness. Their central criticism is simply that there is no information in the independent variables of happiness data, suggesting that correlations are spurious. Johns and Ormerod find the time series properties of happiness surveys to be extremely poor measures that are entirely incapable of providing the sort of explanatory power that is often inferred of them. They note, for example, that happiness is often measured on a bounded 1–5 or 1–10 scale, while income has no upper limit. Yet their main critique comes from demonstrating that sampling errors can explain most of the annual movements in recorded happiness. Johns and

Ormerod find that 'the happiness data contains about as much information on the overall level of social well-being as a series of random numbers drawn from an appropriate probability distribution.' The micro to macro correlates of happiness economics are simply wrong at best and actively misleading at worst. They conclude that 'happiness time series are, by construction,

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incapable of conveying useful information on the level of overall social wellbeing and their use should therefore be rejected by policy-makers and social scientists.'

A further extensive critical review is Will Wilkinson's 2007 Cato paper that also builds on this 'bad science' line, focusing more on analysis and 'bad moral-philosophy.' He explains the problems with the surveys and target of measurement, concluding that 'few of the alleged redistributive policy implications actually follow from the evidence.' Wilkinson provides a comprehensive account of logical errors between happiness theory, happiness evidence and happiness policy. He asks, appropriately, what is happiness economics research then good for? He suggests that it might 'be good for providing insight into how to live wisely and agreeably well,' which is to say that its value, as with positive psychology, lies at the level of individuals seeking to improve their own lives rather than a new contrivance for governments to intervene in the lives of citizens.

The problem with aggregate happiness

Arguably, the most controversial proposal emanating from happiness economics concerns the push for alternative measures of economic performance, specifically, the construction of broad 'social well-being indices' that use happiness surveys as a key input. The Hayekian point is that happiness indices are a bad idea when they confuse or displace with localised

and often tacit information about what rules of choice work best in particular times and places.

Economic performance is conventionally measured with GDP as the market value of the output of a nation. There are many well-known problems: it discounts non-market production and fails to account for qualitative changes or depletion of resource stocks, among others. The new twist is that it also fails to account for how well we're all feeling. The subtext here is that bad economic policy may yet be okay if it makes us feel good. This is a cost-benefit argument of the form that we have not enough measured the benefits, which now should properly include happiness. In 2008 French President Sarkozy commissioned a report on the 'Measurement of Economic Performance and Social Progress' prepared by Joseph Stiglitz, Amartya Sen, and Jean-Paul Fitoussi. While not the first such initiative—various Human Development Indicators and Genuine Progress Indicators

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have been developed; and of course the tiny Himalayan kingdom of Bhutan has had a Gross National Happiness measure since the 1960s—this is by far the most serious and widely cited proposal yet in progressive circles. So what's the problem?

In a perceptive review, journalist Dan Ben-Ami points out, citing Sarkozy's opening line of the report—'I hold a firm belief: we will not change our behaviour unless we change the ways we measure our economic performance'—that the 'alternative measures' project is unambiguously a stalking horse for social engineering. Now maybe we're off-guard with the promise of greater happiness for all. But there's not much specific in that, and a moment's reflection reveals that it cannot possibly be 'for all': by definition, some will be worse off. What is being elided here is a substitution of 'broader' measures of life-satisfaction over material measures of economic output. This is not trivially to

insist that there is more to life than material output—of course there is. But the 'alternative measures' project represents a deliberate and radical attempt to shift the goals and targets of public policy towards substantially less tangible and more evanescent measures, and to do so with clear redistributionist objectives and centralised planning outcomes in mind.

That we should all individually seek happiness and enjoy a right to the pursuit of happiness is uncontested. At issue is whether aggregate survey-based measures of happiness are a valid, objective function for redistributive economic policy. Yet there is a fundamental difference between positive psychology and the economics of happiness. While positive psychology uses scientific knowledge to illuminate how individuals may improve their own lives and maximise their own potential, happiness economics goes one critical step further by explicitly seeking to assimilate the instruments of economic policy into the same project. Positive psychology is applied with self-help manuals and academic courses, not with government departments and law. Yet a world of difference separates happiness research in positive psychology, which studies the individual correlates of happiness, offering helpful suggestions to people about how they might make changes to improve their own lives—for example, cultivating friendships, avoiding long commutes, and engaging in activities that express 'flow'—and the notion that individual happiness should be a proper concern of public policy, carrying with it the full instruments of law and legislation.

In short, why create a national happiness index if you're not going to use it? Let's not lose sight of why we measure GDP at all. It's not simply to track economic markers but to evaluate economic progress with comparable data over changed economic factors, such as new technology, productivity growth, or resources, and, more importantly, to evaluate the effectiveness of economic policy (such as deregulation, deficit spending, and tax changes). We measure the aggregate performance of the economy precisely to evaluate our *interventions* into the economy. A minimal libertarian

state that does not seek to intervene would have no need to measure aggregate economic performance. The rise of GDP measures necessarily coincided with the rise of mixed and planned economies. Any discussion of new and better measures of economic progress is inherently premised on a broad shift in the types of interventions to be undertaken. A national happiness index is inescapably premised on some design of national happiness planning.

This pretension can be directly observed in a recent comment by UK sociologist William Davies on opendemocracy.net, where he says:

> Happiness economics has already cast doubt on our privileging of consumption in the dominant political-economic discourse, but this lacked any 'official' statistical endorsement. The government's happiness indicators will change this, and in doing so will create an opportunity for *political leaders to articulate a vision of how we should best produce, both within firms and as a society*. [emphasis added].

This is an unambiguous admission of the vision of those supporting the construction of happiness indicators as a tool to advance the planned economy.

Measures matter. Many market reforms of the 1980s, for example, which imposed very real costs on those in previously protected or privileged positions, were ultimately justified by pointing to the aggregate improvements in GDP. We should expect no less from aggregate happiness measures that may provide political cover for otherwise dubious actions. An example from Bhutan is illustrative. Former Harvard President Derek Bok notes:

> Different [happiness] goals sometimes conflict with one another, requiring difficult trade-offs. In order to promote the goals of health, environment and equity, the government has chosen to restrict individual freedom by such

measures as prohibitions on smoking and private medical practice along with compulsory dress codes and architectural requirements on all new buildings.

In the interests of national happiness, Bhutan has enacted some highly illiberal policies that in other contexts would unequivocally be called fascist (compulsory dress codes, banning private practice in essential services). If we measure aggregate happiness for the purposes of maximising national happiness, then other criteria will soon subordinate to that, and troublingly, as Bhutan illustrates, this is likely to be individual freedom of choice.

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By definition, any happiness policy by redistribution or restrictions will need to trample on some existing rights and expectations. A national happiness policy will by definition make some people less happy, so unanimous agreement is out. The success of any such policy will therefore need to rely on a 'greater good' argument or a mass compelling 'good for me' argument. So now we're back in public choice theory, seeking to unpack the effects of how competitively different 'happiness interest groups' lobby. Happiness policy, in its standard form, has no claim to rising above this.

A further criticism of the aggregate happiness measure is what such an index is intended to replace, namely a political focus on economic growth and development. The policies that promote economic growth and development everywhere involve hard political choices because they require a shift in power from state to market. But if economic performance is redefined as measured by aggregate happiness surveys, then strong incentives will emerge to engage in short-term interventions (income redistribution through steeper income taxes and luxury consumption taxes) or restrictions (bans on firing employees, or bans on certain

markets) that are suggested by happiness economics findings in the aggregate, but which have the deeper and more long-lasting effect of corroding market function and blunting economic incentives. While these may potentially maximise an aggregate happiness measure in the short run, they will invariably come at the cost of economic growth and development. This sort of public pursuit of happiness is likely to make most of us privately worse off. So this looks a lot like Keynesian economics all over again.

Modern happiness economics has a distinct colouring in policy implications. These are broadly against economic growth, against luxury consumption and the marginal utility of increased income, and broadly in favour of income equality through redistribution and an expanded welfare state, including highly regulated labour markets. This is shot through with a behavioural economics sentiment based on a belief that people don't necessarily know

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what is good for them. This opens a potential role for public intervention to correct these systematically flawed individual choices. Modern happiness economics is thus a reworking of social welfare theory. Specifically, the economics of happiness literature has strongly emphasised the *negative externalities* from happiness, such as Robert Frank's 'hedonic treadmill' that features in every book with 'affluenza' in the title. Policy recommendations typically point to the welfare gains from, for example, steeply progressive taxation that seeks to step us off this 'wasteful social competition' for our own good. But I want instead to emphasise the *positive externalities* to other people being happy, in particular, what we may learn from them. This proposes a signalling theory of happiness as a mechanism of social adaptation of good rules for choice.

Happiness signalling theory

Happiness is plainly a subjective, individual experience, but it is also a social signal. We can know when others are happy by observing them, and they too may know when we are happy. From the perspective of evolutionary economics it is this signalling aspect, and not the level's effect (i.e. individual subjective well-being), that may be the key economic fact about happiness and its role in economic dynamics and adaptation.

Yet the standard approach to the economics of happiness stops at the point of subjective experience. It does not then consider its effect on others through the distributed information signals involved. But this was precisely Hayek's point about how market signals work to produce a spontaneous order. An analogous argument can be made about 'happiness signals' and their adaptive efficacy. Happiness should be understood as part of the distributed market mechanism, not as an excuse to politically over-ride it.

If you are happier than someone else, one possible explanation is that you've made better decisions, and vice versa. Obviously other factors such as luck matter too. We can learn and adapt our behaviour from other people's happiness signals, just as we can learn and adapt from price signals. The critical importance of price signals is, as Hayek explained, about local information and about time and place; happiness signals are likewise, but also about good rules of choice in relation to time and place. This distributed happiness signalling is therefore a further mechanism that shapes economic evolution. Happiness is to the consumer side of economic dynamics what profit is to the producer side, namely, a signal of useful information about ideas, rules and technologies that work in a particular choice environment.

I know what makes me happy, more or less. I also know how to observe signs of happiness or seeming contentment in others with their life. Most healthy adults can do this, not just happiness researchers. We notice happy people; we tend to find them attractive. Much of that is instinctual but also functional: it induces us

sometimes to seek to learn about what makes them happy and what choices they have made. We do this to consider adopting those choices or rules too. It's a decentralised signalling coordination system.

These happiness signals can often be read directly from the outward demeanour of a person. We instinctively recognise many of these are signs and furthermore come to share as social knowledge. Happiness then is not just an end state of individual hedonics but also a social signal of good choices that can be read and acted upon (possibly through imitation) by other agents. Happiness signals form a distributed mechanism to coordinate the continuous updating and adaptation of preferences and rules for choice. Happiness thus has *positive externalities* in the form of local decentralised signals of information about choices in a particular time and place. There is no good reason for public intervention in this otherwise natural communication and coordination process by which happiness is locally discovered and socially communicated. As monetary inflation distorts price signals, so may happiness policy distort the happiness signals that otherwise coordinate the evolution of preferences in a dynamic economic order.

Yet evolutionary theory in happiness research has hitherto mostly been directed at supporting the 'individuals systematically make bad choices' line, supplying micro-foundations to underpin proposed social welfare interventions (such as changes in tax policy). But to say that we have evolved instinctual tendencies is not to say we are stupid. As best we can, we reason, review, discuss and re-examine our relative happiness estimates of others, and stop only when we are ready to act (or not) to change our behaviour by adopting better rules for choice. But unlike Sarkozy's vision of the rules for economic behaviour that makes for happiness issuing from government, is it more likely to come from your neighbour or friends in your social network or from colleagues and peers. Still, this is an evolutionary argument from biology and psychology because it supposes the human adaptation of a general capacity to both signal happiness and to interpret happiness

signals (we are very good, for example, at detecting fake happiness, implying that the signal has strategic value). But 'happiness signalling' theory is also an evolutionary economic argument in recognising the adoption of other people's preferences and rules for choice as a mechanism of economic evolution.

The obvious policy implication of a negative externality view of social competition is to raise the cost of these signalling games, which we

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presume are corrosive to human happiness by the hedonic treadmills they set up. Yet happiness signalling theory makes a very different claim about the value of social competition, arguing that social competition actually underpins happiness due to the induced effect of adopting better rules for choice. Happiness *signalling* thus allows agents to learn from each other in adopting rules for choice and action. Happiness signals coordinate the flows of adoption of rules for choice that are effective in particular environments. The more effectively this adoption and adaptation process works, the faster economic adaptation and economic evolution occurs.

This mechanism casts new light on the interactions between inequality and institutional evolution. First, it is well known that at a point in time the economically more successful are happier. Where different rules of behaviour and choice can be discerned, we may expect that the rules of the more successful will be increasingly adopted into the population. Happiness signals working through social networks are therefore part of the process of economic self-organisation and adaptation as decentralised signals operating over social networks that convey information about how particular economic rules work in particular economic environments.

Consider economic inequality. The richer are happier; that's a robust finding of happiness economics. But it doesn't stand

up over time, or through changes in wealth. That's an equally robust finding. The resolution is evolutionary dynamic. Inequalities are mediated by happiness signals: those with low happiness are incentivised to change their own rules for choice and action, toward adopting the rules of the happier over their local space of social network markets. This suggests an evolutionary mechanism by which *economic inequality* is actually diminished by the differential adoption of happiness signalled rules for choice and action, but which relies on robust *social competition*.

This suggests a mechanism by which social competition translates into improvements in aggregate economic happiness by the adaptive and self-organising evolution of good rules for choice. This process already occurs extensively and works well at a decentralised level. Just as markets do not require government guidance to function well, for reasons that Hayek explained clearly in 1945, neither does happiness.

Conclusion

Modern happiness economics has some shaky foundations upon which some seriously wobbly policy ideas have been constructed.

Yet there is nevertheless a strong case for a new happiness economics constructed on an evolutionary theory of happiness signalling. Like prices, happiness is also a decentralised signalling mechanism that coordinates a socio-economic order. This implies a very different approach to the standard policy line on happiness economics, which favours increased social equality (i.e. as corrected with happiness policy). Happiness signalling theory instead emphasises the emergent consequences for the evolution of rules for choice through social competition (i.e. unleashing happiness discovery). The model of happiness signalling therefore extends Hayek's price signalling coordination hypothesis to the observed happiness states of other people.

We are happy or otherwise, for the most part, because of the choices we make. But we can learn from other people's choices too. Happiness signalling theory generalises this mechanism as a self-organising decentralised process. To be happy, it is important to pay attention to our social connections and cohorts, and to reflect on our own lives. Government can't actually make us happier than we can do by ourselves (with a little help from our friends).