

Human well-being and priorities for economic policy-makers

*The implications of new measures of
social progress*

2nd December 2011

Charles Seaford
Centre for Well-being
nef (the new economics foundation)



Context

- WIFO 2010: “more of the same” would not equal success for most groups.
- OECD 2011: growth – but a new kind of growth
- Autumn 2011: protests in 900 cities

And to come:

- 2012: squeezed living standards, sovereign debt, attacks on democracy, no agreement on climate change

But:

- In the absence of an alternative, decision makers will revert to traditional solutions

The overarching task is to increase environmental and well-being efficiency of the economy

Conceptual framework for societal progress

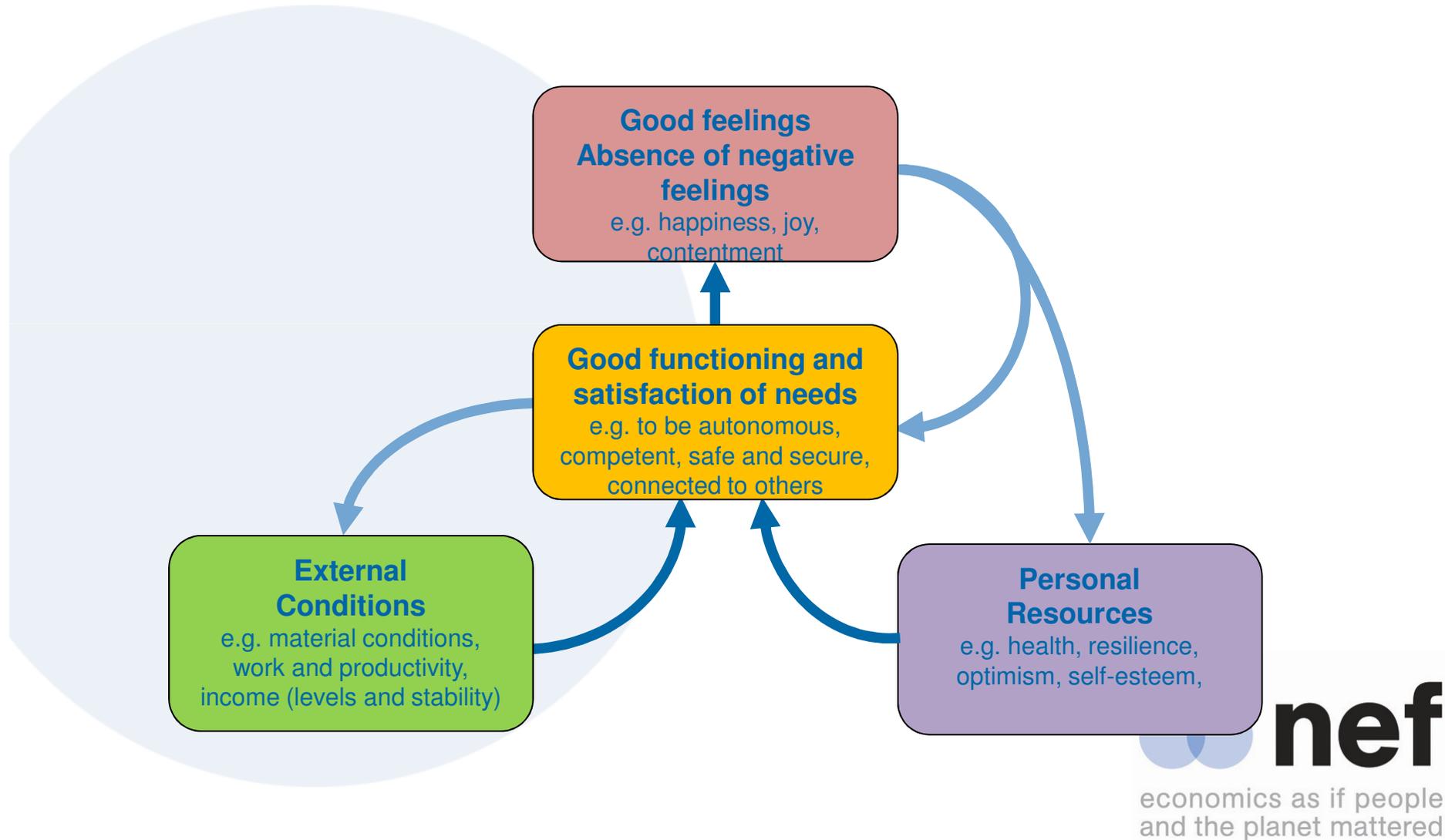


New measures of social progress can help us do this

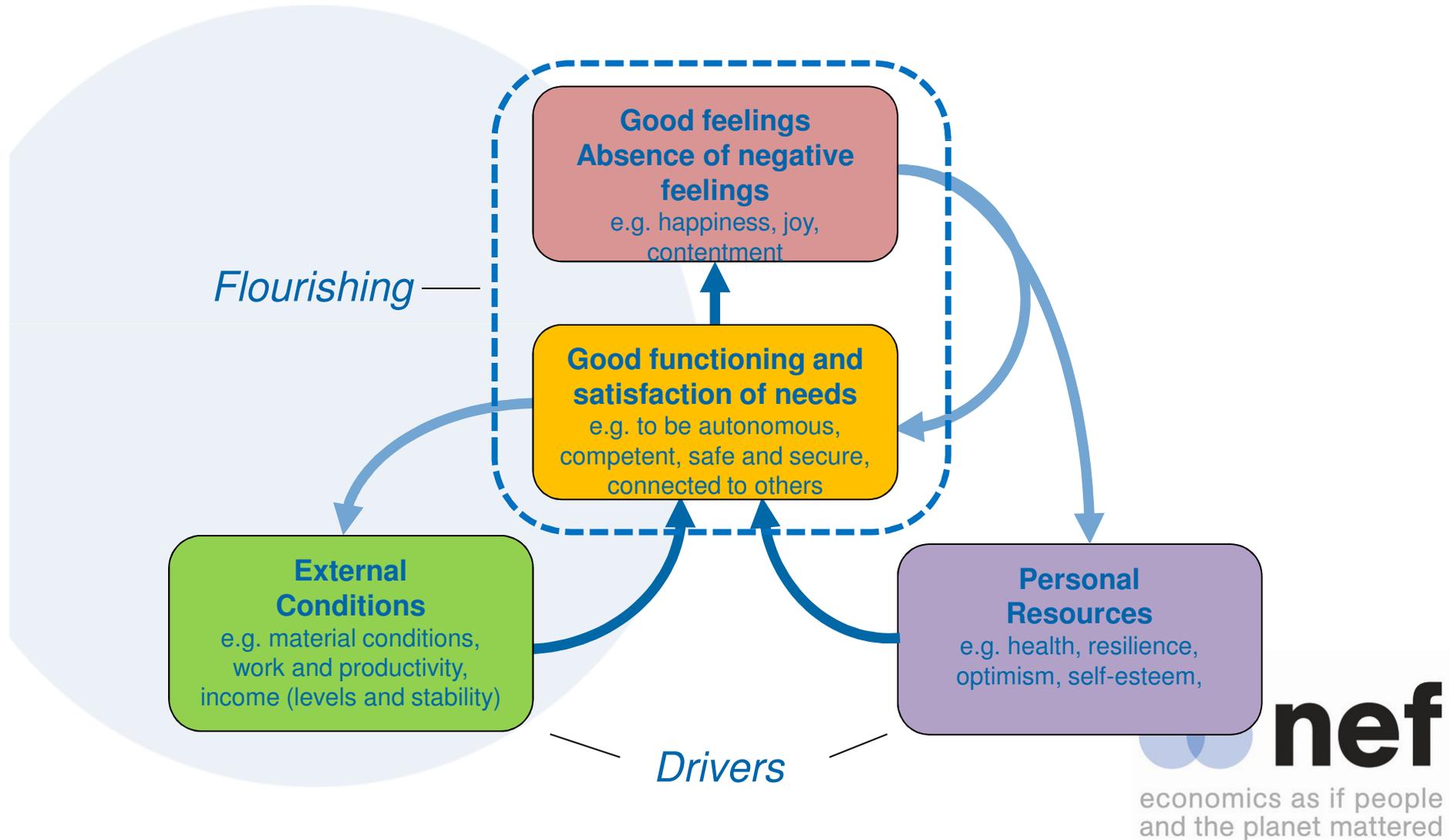
I will focus today on well-being efficiency

- What does well-being science tell us?
 - Principally cross-sectional and time series statistical studies
- What implications does this knowledge have for economic policy objectives?
- What implications do these objectives have for an approach to economic policy?
- What do we need to do next?

Human well-being can be thought of as a system...



We can measure both the goal – flourishing – and its drivers



So what do we know about these drivers?*

1. **Income** is important to well-being, but only **up to a certain level** which varies from society to society; most people have not reached this level
2. **Equality is positively associated** with well-being, although the relationship is complex
3. **Unemployment** is very damaging to well-being
4. **Economic instability** is damaging to well-being
5. The various components of a '**good job**' are strongly associated with well-being – this includes **the right amount of work**: not too much or too little
6. **Increases** in national **income** do **not** necessarily **translate into better jobs** in this sense.
7. **The way we consume** does not optimise our well-being, and advertising may contribute to this
8. Some types of personal **debt** are associated with low levels of well-being
9. There are other features of society, such as the strength of personal relationships and **social capital**, which are strongly associated with wellbeing and which are influenced by the design of the economy

*Sources available on request

1. The income point has been much debated

- **A positive but declining relationship** between income and well-being when measured at any given time in a particular country
 - The curve varies with the measure of well-being used but there tends to be an ‘inflection point’ suggesting that the returns to income decline steeply *at a certain level*
 - In the US affect measures inflect at c.\$50,000 and flat line at \$75,000 (well above median)
- Time series data suggests that in US – and other countries with GDP/capita above *a certain level* – **GDP growth does not cause well-being increases**
 - This is true despite cyclical effects and the impact of recovery in ‘transition economies’
- There are **a number of explanations** of this (‘Easterlin’) paradox:-
 - **Stagnant median earnings** (over 30 years in the US and 10 years in the UK) – but well-being stagnant even when median earnings were rising
 - The importance of **relative income** once a certain level of income achieved (*not* just status!)
 - Concurrent **changes in society** which have had a negative influence (eg fragmentation) which *may* be a consequence of growth or the pursuit of growth
 - Changing frame of reference – **hedonic treadmill** (well-being as function of growth *rate*?)
 - **Measurement error** (we always say the same)
- It seems what matters is getting **everyone to a certain level**
 - unless measurement error entire explanation of Easterlin Paradox

2. The evidence for equality is complex

Declining marginal utility has always been an argument for equality – BUT countered to the extent that incentives are needed to maximise output

The evidence suggests that the optimal level of equality is high

1. Marginal utility (measured as affect) is **zero** above a certain level so the traditional argument is reinforced
2. **If** you have achieved the base level after which **relative income** is what matters, then **you cannot justify inequality** because it produces growth
 - The growth will not increase well-being (Easterlin) but the inequality is well-being inefficient
 - However inequality may be justified to prevent economic collapse and unemployment
3. In any case growth may not produce higher median/sub-threshold incomes
4. In addition evidence that inequality has directly **negative effects**
 - stimulate material aspirations – which are not just a zero sum but a negative sum game: social comparisons make happiness more expensive
 - a negative impact on physical and mental health in the population as a whole

However direct statistical evidence not that clear cut

Recent evidence suggests well-being in the US higher in periods of greater equality also some correlation between Gini co-efficient and well-being levels but too many other factors to ascribe causation

3. The evidence on unemployment is very clear

- The unemployed
 - have sharply lower life satisfaction scores (**5–15 per cent lower – UK 6.3 vs 7.4**)
 - are 19 per cent less likely to have a high life satisfaction score
 - 15 per cent less likely to have a high overall happiness score
- These effects are **stronger than** those associated with the equivalent **income loss** (which are in turn higher than with the equivalent income gain)
- The unemployed **do not adapt** to their circumstances in the way that those who gain or suffer income changes generally do
- The effects are **scarring** and can lead to lower well-being even once back in employment
- High levels of unemployment are associated with **loss of wellbeing amongst the employed**
- There is a positive association between doing at least some work and well-being amongst the otherwise **retired**.

4. As is the evidence on instability

- **Loss of income** damages well-being significantly more than a comparable gain enhances it
- Well-being is negatively associated with very high growth rates, presumably because of the **disruption** almost always accompanying very high growth
- **Job security** is the job feature most commonly cited by employees as desirable
- **Casual workers** enjoy lower levels of well-being than full-time workers
- **Inflation** is negatively associated with well-being (although the impact is significantly less than the impact of unemployment) and **volatile** inflation rates are worse than steady inflation rates
- Levels of **wealth** are more strongly related to levels of life satisfaction than are levels of income; this may partly be because wealth allows consumption above income, but may also be because of **the value of economic security** which wealth provides

5. Good jobs are associated with well-being

- Over 50% of workers say they would accept a corresponding drop in income to achieve a **drop in hours** to 34 hours a week
- Part time workers enjoy lower levels of well-being than full time workers. Well-being **rises** as hours worked rises – **up to a point after which it falls.**
- Also highly valued are good **social relations** at work and the opportunity to do work that is **interesting and stretches** the employee but which he/she is good at

6. But increases in national income do not always result in good jobs

- Overall **job satisfaction in the UK** fell between 1989 and 1997 and then rose back to 1989 levels by 2005 – in other words it has **not risen in line with national income.**
- Similarly job satisfaction **fell or was flat between 1997 and 2005** in 9 of 15 OECD countries while rising in 6



economics as if people
and the planet mattered

7/8. The way we consume does not optimise our well-being

- Our decisions about how to consume and spend our time do not maximise our well-being
 - We are **not very good judges** of what will make us happy
 - We spend a relatively large amount of our time on **passive pursuits** such as watching television, even though the evidence is that active pursuits contribute disproportionately to well-being and that people who watch lots of TV have lower well-being
 - There is good evidence that those who value material goals relatively highly are less happy than those who value other things and that societies such as the UK that are relatively more **materialistic have higher levels of mental ill health and lower levels of child well-being** than societies (such as some in continental Europe) that are less materialistic.
- **Advertising** may make our consumption decisions (even more) sub-optimal: it only works because it can exploit and exacerbate imperfections in our information processing.
- So – does advertising induce sub-optimal decisions because it encourages materialism and passive pursuits at the expense of active pursuits?
- And resulting **short term debt** definitely damages well-being

9. Other features of our society mediate between the economy and well-being

- There is a positive correlation between well-being and **participation** in the community and volunteering
- Seeing **family and friends** is positively associated with wellbeing
- **Social trust** (i.e. trust in most other people) is positively associated with well-being
 - positive responses in the UK to the question ‘do you think most other people can be trusted’ fell from c. 60 per cent in the 1950s to c. 30 per cent in 2002.
- **Children’s** well-being, both as children and later in life, is negatively associated with frequent **moves of home**
- Living close to open **green space** has been shown to enhance people’s well-being
- Negative externalities such as **pollution and aircraft noise** are (unsurprisingly) negatively associated with well-being
- These factors are all **influenced by** design of the **economy**

This implies priorities for economic policy

1. A target band of **income** for everyone based on the 'certain level' (propositions 1 and 2)
2. Minimal **unemployment** (proposition 3)
3. Economic and social **stability** (propositions 3 and 4 and proposition 9).
4. **Satisfying work** for all (parts of proposition 5 and 6)
5. Work for all in the **right quantities** (propositions 5 and 6)
6. Ensuring **active forms of consumption** and correcting the biases created by advertising (propositions 7 and 8)
7. Incorporating **externalities** effectively into decision making (proposition 9)

Targeting GDP growth is not the best way of delivering these

- Median earnings do not follow GDP and may simply raise the 'certain level'
- It is possible to imagine situations where GDP growth is pursued at the expense of one of more of these
- In addition we need to take into account sustainability

So what do we do to achieve target band of income and minimise unemployment?

- In principle this might mean increasing the demand for (and supply of) mid-level (high non-graduate) **skills** and increasing **wages** in low wage sectors
- **In the UK** increasing demand for mid-level skills may mean increasing demand in those sectors with higher than average proportion of NVQ3s
 - Buildings 550,000*
 - Retail 550,000
 - Care and Development 430,000
 - Travel and Hospitality 405,000
 - Manufacturing 372,000
 - Finance 201,000
- Note mostly **non-traded sectors** – largely about the domestic economy
- **Buildings** demand heavily dependent on public policy and there is housing shortage - *but* demand is in one place and unemployment in another....
- **Care** demand also dependent on public policy – *but* badly paid
 - Care NVQ3 pay range £17-£21,000**
 - Machinery manufacturing NVQ3 pay range £27-£34,000

* Numbers = numbers of NVQ3 employees in those parts of the sector with a concentration of NVQ3 employees higher than the national average ** nef estimates based on ONS/SSC data

Indicative implications – active use of power...

Skills

- Use **state planning power** to ensure everyone has a decent and sustainable home and grow Buildings sector
- Use **state planning, purchasing & fiscal powers** to stimulate the economy in relatively depressed regions
 - Identify and build regional comparative advantage vis a vis rest of country and world
 - Identify scope for and support local import substitution (eg more face to face services)
 - Also boost industries employing graduates to help pay for transfers/higher care etc wages
- Use **state purchasing & fiscal power** to up skill quotient where it is possible to move an industry out of a low wage equilibrium

Wages

- Use **state purchasing power** to drive up wages in Care (and elsewhere)
- Use **state legislative power** to encourage unionisation in low wage sectors such as Hotels and Care and to drive up minimum wages
- Use **state fiscal power** to flex vat etc to soften transitional impact of this

There are many problems with these proposals – it is the approach that is important

- It is **not** just identifying and then **correcting market failures** – since the aim is not simply GDP maximisation and allocative efficiency
- The approach is **pragmatic**: we cannot wait for the new theory
 - How do we reach these objectives? How do we deal with the obstacles? How do we deal with the bad side effects?
- But it is principled, **evidence based** and can **be metric driven**
- It is highly **interventionist** – the desired outcomes won't just happen
 - The debt markets will have to be managed....
- It requires a very '**joined up**' approach to policy – **unified top team**
 - home ownership and regional industrial policy, tax and minimum wage policy, land planning and skills policy – etc etc (the team has to unify instead of the theory)
- It requires **co-ordinated** action at EU, national, regional and local **levels**
- It is active and relatively **high risk** – but the consequences of not taking action may well be even more risky

What do we need to do next?

- Wide **understanding of the drivers** of well-being (and sustainability)
- Make clear the **limitations of existing theory** – without waiting for a new theory
- Development of **metric sets** to **link** popular and **political imperatives** with detailed **policy** making
- Pragmatic **policy making** within progressive political parties focussed on objectives
- More time on **team building** and less time on theory building in politics (in UK)!
- Much more effective **co-ordination at European level** to counter the default 'business as usual' narrative

- www.neweconomics.org
- Charles.Seaford@neweconomics.org