Happiness Research*

Contributions to Economic Ethics[1]

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Empirical happiness research has been gaining wide acknowledgement recently and offers a promising new access to the question how choice and happiness relate to each other. Since this is a central question to both ethics and economics, it seems worthwhile to investigate what this perspective can contribute to economic ethics.

Keywords: economics ethics, happiness, rational choice, social welfare.

1. Introduction

The interest in empirical and experimental economics has virtually exploded among economists during the last few decades. A symptom of this development, and probably a boost to future research, has been the award of the 2002 Nobel Prize in Economics to Vernon Smith and Daniel Kahneman, an experimental economists and a psychologist, respectively. This change is accompanied by increasing efforts on the side of economists to bridge disciplinary cleavages, in particular that towards psychology. This widening of perspective is gradually breaking up the axiomatic seclusion of economics and in particular that of its behavioral foundations.

While this development has sparked substantial critique at the neoclassical conception of behavior and decision making, few scholars go so far as to question the underlying idea of rational utility maximization as such. Such a more fundamental critique, it will be argued here, will emerge once the remaining disciplinary gaps between economics and psychology on the one hand and that between economics and ethics on the other hand are tackled.

Rather than using such interdisciplinary bridges merely for firing ethical critique at the other side, ethicists, or more precisely economic ethicists, should recognize that such bridges can and should be walked both ways. By asking themselves how ethics can be enriched by empirical research, they stand to gain much more than they can lose. The purpose of this article is to do just that: to investigate what empirical happiness research can contribute to economic ethics.

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To do so, I will have to start with a brief analysis of the psychological foundations of economics in which the free will (or rather its absence) plays the central role and represents the (missing) link to ethics. A discussion of happiness will then clarify this concept without attempting a complete definition. Section four will report some empirical evidence of happiness research and assess its significance for economic ethics. The conclusion will then look at the results obtained from a methodological perspective.

2. The psychological foundations of economics

The science of economics can be interpreted as being nothing more than the deduction of specific rules from a single general psychological principle, to wit utility maximization. Additional principles may be invoked in specific contexts — such as risk avoidance, time preference etc. — but these represent just specifications of, not departures from, the utility maximization principle.

The nature of this principle is well known. Basically, it says that whatever people do, they do it in order to maximize their utility (this premise is also known as "psychological hedonism" and is usually ascribed to Hobbes).[2] To decide which choice will actually maximize an individual's utility, people are assumed to have a consistent set of preferences that allows them to decide — given the information and intellectual capacity they actually have — which of any number of alternatives is in their best interest, or (in the case of incomplete orderings[3]) whether one alternative is at least not less "optimal" than the others. These preferences are not only internally consistent (in the sense of ruling out self-contradictory behavior), but also reasonably well-calibrated in the sense of furthering the individual's good. In other words, it is assumed that people do not fool themselves, that they learn from past mistakes, and that they make reasonably accurate predictions of the consequences of their choices. Furthermore, people are assumed to follow their preferences rather than acting erratically or mindlessly. The actual meaning of the concept of utility is rarely spelled out, but it is usually taken to be similar to "happiness" or "satisfaction." As such, it is not necessarily to be understood as materially egoistic[4] behavior or as aiming at superficial pleasure only, but rather as an encompassing experience of satisfaction from various sources (including "psychic income").[5]

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2 Whether they succeed in doing so is a question to be separated from psychological hedonism and requires some claim of rational anticipation (*cf.* next paragraph).

3 *Cf.* Sen (2002). Even though Sen's inclusion of incomplete preference orderings — *i.e.*, situations in which an individual neither prefers one alternative over another nor is indifferent between them — renders the maximization framework more "realistic", this by itself does nothing to restore compatibility with a free will.

4 By "not materially egoistic" I mean that actors are assumed to derive utility from others' well-being as well (what Sen (1983c: 91) calls "sympathy"), even though strictly speaking all behavior has to be interpreted as egoistic (or more precisely: "solipsistic") under a paradigm of psychological hedonism.

5 To be sure, the precise understanding of utility maximization comes in many shades (for differentiated and critical discussions *cf.* Sen 1983a, Etzioni 1988), but the purpose of this short sketch is to present the most common understanding of utility maximization found in the economic literature. The following discussion will not depend on the details of a concept of utility maximization.

This concept of behavior is well known, as is its extensive critique, and this is not the place to dig deeper into this issue. What does deserve emphasis, though, is the *identity of choice, value, and happiness* implied by this particular variety of psychological hedonism. People are assumed (i) to value things exclusively for the happiness they expect to experience, (ii) to make choices by the single criterion of (expected) happiness, (iii) and to anticipate with reasonable accuracy their choices' effect on their happiness. As a consequence, people left to their own devices will by definition make the best of their lives. By implication, when people get addicted to drugs, this is seen as "rational addiction" (Becker/Murphy 1988); and when a consumer indebts herself buying luxury goods, this is deemed the behavior that is in her best interest.

2.1 Psychological mathematics

In a book from 1881 entitled "Mathematical Psychics", Francis Y. Edgeworth provided a mathematical account of human behavior, stating that "the first principle of Economics is that every agent is actuated only by self-interest" (Edgeworth 1881: 16). What is most striking about this mathematical anthropology is the almost complete absence of any empirical backing. It seems all too obvious that the anthropological principles adopted in economics gained acceptance because of their internal consistency that allowed to analyze human decision with mathematical tools, and not because of their close correspondence with actual psychological processes. When "mathematical psychics" is tested against empirical evidence, the former's inadequacy becomes embarrassingly clear, as will be documented in section 4 of this article. At this point, this inadequacy shall merely be illustrated by means of an example.

In economics, it is standardly assumed that work constitutes disutility for people and that they would prefer not to work if they did not need the salary. The following passage from a standard labor economics textbook represents this typical assumption:

> "For most people work is undertaken primarily for pecuniary gain. For the vast majority work is essential to secure the income necessary to buy the goods and services that support their standard of living. Work is undertaken because it is a means to this end and, although many individuals find aspects of their work and the social environment in which they work enjoyable, few find it so enjoyable that they would be prepared to pay for the privilege. For most people, work is, in the main, a source of disutility and they therefore require payment to compensate them for the time they devote to it" (Elliott 1991: 3-4).

Note that the author does not with a single word refer to any empirical backing for his hypothesis. As soon as one directly asks people about their attitude to work, it becomes clear that it does not stand up against the evidence. Campbell, Converse, and Rodgers (1976), for example, asked 1114 respondents (each of whom worked at least 20 hours per week) the following question:

> "If you were to get enough money to live as comfortably as you'd like, for the rest of your life, would you continue to work?"

Those who said they would were then asked:

"Would you continue to work at the same job as you now have?" (Campbell *et al.* 1976: 291).

As a result, a total of 69% answered they would rather continue to work (40% at the same job, 29% at a different one). Not even one third of employees, therefore, would prefer a life of paid leisure to a life of paid work. Defenders of the above cited theory might say that people's reluctance to accept low-paid jobs would be evidence of people's preference of leisure over work. This argument, however, requires a number of additional assumptions to be valid, and these are obviously not usually met.

As illustrated by this example, the psychological assumptions made in economics lack empirical foundation. Rather, they seem to be *ad hoc* assumptions based on casual observation and driven by an ambition to formalize and quantitatively analyze human behavior. Furthermore, assumptions that may even be plausible at the individual level — *e.g.*, that ordinary consumption decisions usually raise the consumer's satisfaction — are naively extrapolated to the societal level. Yet, just as one cannot conclude from the observation of a flat horizon that the earth is flat, one cannot conclude from one's happiness with a raised consumption level that society as a whole will become happier when everybody's consumption rises (more on this below in section 4.3).

After considerable progress in the field of experimental economics and psychology, and after the award of the Nobel Prize 2002 in economics to Vernon Smith and Daniel Kahneman, economists can no longer ignore the validity of experimental evidence and of self-reports as reliable sources of data with which economic theories of human behavior can be put to a test. Before the evidence from these sources and their significance to economic ethics is assessed (pp. 149), I shall develop the central argument that the root cause for the shortcomings of the rational utility maximization hypothesis is the paradigm of determinism or, what amounts to the same thing, the rejection of a free will.

2.2 Volitional rationality

The perhaps fiercest critique at the economic model of utility maximization comes from moral philosophers who claim that people may also act out of a moral commitment which cannot be reduced to a calculation of costs and benefits. Economists typically reject this objection by saying that what appears to be selfless commitment, such as giving money to charity (without the expectation of a material benefit), is really itself a source of utility ("psychic income"), thus reinterpreting moral behavior as utility maximization behavior (*e.g.* Kirchgässner 2000/1991: 176). This argument is not easy to counter. Why else, the economist would ask, would anybody give to charity? And do people not actually feel some kind of pleasure, in the form of self-respect and a good conscience, when they give money to a good cause?

The argument is intriguing, but it is hard to maintain once its wider implications are recognized. In fact, utility maximization must assume that a person's preferences exist 'out there' in a very concrete sense and that they are given. "Given" does not mean immutability, of course. It rather means that preferences are not chosen by the individual who holds them, but that they are the purely deterministic result of the interplay of external factors, such as genetic endowment, socialization, parental education, and experiences in general. In other words, preferences, and their changes, are thought to be externally determined, which is the same as saying that people have no free will. A model of human behavior that is built upon a deterministic anthropology, however, is in stark contrast with our ordinary belief that we are endowed with a free will. And even though, strictly speaking, neither claim — determinism and free will — can be falsified, empirical evidence is rather supportive of a free will, as demonstrated below.

The perseverance of the deterministic model of utility maximization in economic theory seems to stem from the difficulty to defend the free will in scientific discourse. It is almost the defining feature of scientific inquiry that it imputes causal determination to its objects. Acknowledging freedom of will, however, means to suspend, at least to some extent, the laws of causal determination within the domain of human decision making. As Kant put it, "how pure reason can be practical — to explain this is beyond the power of human reason." (Kant 1977/1785: 99)[6]

To give this problem some flesh and blood, consider the case of two heavy smokers who both declare they want to quit smoking, but only one of them actually does so. In common language, we would praise this person's strength of will and say she merits respect for this feat. Of course, such a judgment only makes sense when a free will is imputed, since we can only meaningfully praise a person for things that would not necessarily have occurred. To a defender of determinism, however, a person who manages to stop smoking simply was lucky to have such a constellation of preferences and constraints that made the benefit from quitting smoking be larger than the costs (Becker/Murphy 1988: 693-94). The preferences of the person who continues smoking, on the other hand, were such that the costs of stopping would have been larger than the benefit. In this perspective, there is no real difference between a person's quitting smoking and a pool ball's movement upon being hit by the queue: both are just inevitable, perfectly determinate outcomes of prior events. The crucial point to note here is that people are assumed to simply *have* such and such preferences, and not to choose them. The issue is of course not whether people are *entirely* free to choose their preferences arbitrarily, free from psycho-physical predispositions. Obviously, people cannot choose their preferences by discretion, in empty space so to speak. For example, human beings are naturally born with a preference for sweet tastes and a natural dislike of bitter ones, and it appears outright impossible to reverse these preferences. Rather, the issue is whether people have *some limited scope* of freedom in affirming[7] or revising their preferences.

The free will cannot be saved, as is sometimes attempted, by stipulating the existence of meta-preferences on the basis of which an individual then "chooses" her preferences. While the distinction between mundane preferences and meta-preferences may be a useful heuristic device to separate instrumental from volitional rationality (see below) and manifest desires from reflected valuations, it does nothing to reconcile

[6] Translation by T.K. Abbott (www.bartleby.com/32/604.html).

[7] Even if a manifest preference can be considered "natural"—such as a mother's interest in the well-being of her child—it can still at the same time be regarded as freely chosen to the degree it is actively affirmed as a result of an ethical examination of this particular preference's legitimacy.

maximizing behavior with a free will because, on a more fundamental level, it is logically impossible to derive determinate outcomes (in this case: decisions) from an indeterminate basis (unless further artificial assumptions are made, such as a rigid temporal separation between an indeterministic and a deterministic phase of life). Since, with a free will, the choice of one's preferences is the indeterminate manifestation of volitional autonomy, one can by definition not indicate a causal decision rule specifying how this choice is made. Any conception of maximizing behavior, I contend, is bound to negate the subject-quality of the person that manifests itself most conspicuously in the faculty of volitional autonomy.

While freedom of will implies the suspension of deterministic causality in the realm of human decision making, we do require that the choice of one's preferences be orderly and make use of some criteria of reasonableness, rather than being an arbitrary decision or a chance event. In other words, we require them to be reasonable without being determinate, which requires what I will call *volitional rationality* as opposed to *instrumental rationality*. This distinction is analogous to the famous distinction by Weber (1980/1922: 12) between value rationality (*Wertrationalität*, corresponding to volitional rationality) and goal rationality (*Zweckrationalität*, corresponding to instrumental rationality), but intends to avoid the agnosticism of Weber who does not seem to recognize that one may still have (non-deterministic) reasons to prefer one value over another.

Defenders of determinism who demand from advocates of volitional rationality to spell out how exactly volitional rationality is supposed to work in detail miss the point since volitional rationality is precisely defined by the absence of causal, deterministic decision rules. Such demands resemble creationists (people who believe in the biblical account of divine cosmic creation) who feel confirmed by the fact that physicists cannot explain what caused the Big Bang.

Even though a lot more could be said about the problem of a free will, the purpose of this brief discussion is merely to point out the tremendous significance of the question of the free will to the conception of happiness. If desires (or preferences) are not simply given but chosen, then — to the degree happiness is seen as a function of desire fulfillment — happiness will also depend on one's free will, and one will be able to distinguish between more and less legitimate happiness. How happy a person is will then not be a deterministic function of life circumstances and innate personality traits, but ultimately each person's free *judgment* of how decent and enjoyable he deems his living conditions to be. And the legitimacy of the happiness a person experiences in the love to her children can be evaluated differently from that of a safari hunter who kills endangered animals just to show off exotic trophies. With a free will, a preference for hunting rare animals is not inevitably forced upon a person but can be revised upon critical evaluation by virtue of volitional rationality.

More fundamentally, morality as such becomes entirely meaningless in the absence of a free will. A person who has a preference for killing people cannot be held accountable for murders he commits for he just happens to be endowed with such preferences. A murder he commits will be the necessary, inevitable consequence of past events (genetical heredity, socialization etc.) which in turn came about in a deterministic fashion as part of a causal chain that has its origin in the Big Bang. By contrast, as a matter of fact we usually do impute to a murderer that he could not have wanted to kill[8], even though it is usually conceded that an adverse biography may make a person more disposed to wrongdoing and that such a person may have more difficulties "to conform his behavior with the norms of legal propriety" (*cf.* footnote 8). To be sure, the fact that a free will is usually imputed to human beings is no proof of its existence. The point I am making here is simply that a deterministic theory of human behavior is at variance with the most fundamental convictions about human nature.

Now, for a model of human behavior to be of practical use, it does not have to be realistic as long as it helps us analyze, predict, and understand human behavior.[9] On this account, it seems, the economic model of human behavior does rather well, considering its capacity to predict the interplay of supply, demand, and prices in well-defined markets. After all, nobody can seriously doubt that self-interest is a major motivating force of most people most of the time. Looking more closely, however, it becomes clear that the economic model is good at predicting behavior where instrumental rationality alone is concerned, but that it runs into problems when volitional rationality is concerned as well.[10] To conclude this brief discussion of the free will, it shall be posited that both conceptions of human behavior, instrumental and volitional rationality, have some merit. The concept of instrumental rationality is useful as a heuristic model to predict behavior where ends can be taken as given, while the concept of volitional rationality is appropriate where choice between ends is concerned. As long as each concept of human behavior respects its limits, no conflict should arise between the two.

As has been pointed out above (p. 142), instrumental rationality is typically held to be exclusively motivated by the maximization of one's happiness. Happiness is also seen, in the utilitarian tradition, as the only and ultimate purpose of intrinsic value. The next section will therefore take a closer look at happiness and try to relate the empirical concept of subjective well-being to an ethical perspective on happiness.

3. Understanding Happiness

Even though everybody of whatever mother tongue appears to have an intuitive understanding of the idea of happiness (Veenhoven 1996: 2), the concept itself seems to defy a narrow definition. At least partly, this difficulty stems from the multiplicity of perspectives one can take in approaching the phenomenon of happiness.

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8 This practice is documented in penal codes and adjudication around the world. For example, the Swiss federal penal court (Bundesgerichtshofs in Strafsachen, BGHSt) once ruled that "the deeper reason for the accusation of guilt lies in the natural disposition of human beings to free, responsible, moral self-determination and their ability to opt in favor of righteousness and against wrongdoing, to conform their behavior with the norms of legal propriety." (Decisions of the BGHSt 2, 194, 18 March 1952, quoted in Dreher 1987: 11, own translation).

9 That a theory should not only predict but also explain has been argued by Etzioni (1988: 17).

10 As an example, consider the phenomenon of a *decrease* in blood donation upon introduction of monetary incentives in Japan. Even if this behavior could be modeled as utility maximizing (instrumentally rational) behavior after the facts (as any behavior can), it could not be predicted beforehand because the outcome of people's free judgment (volitional rationality) defies analytical prediction.

Making no attempt to give an iron-clad definition of happiness, I will nevertheless try to specify how "happiness" will be understood in this paper, and in particular what happiness is *not* meant to stand for. To begin with the latter, happiness is not taken to stand for the *summum bonum*, *i.e.*, the ultimate criterion of the goodness of a person's life. Defining happiness as the *summum bonum* risks depriving happiness of the substantive content it is conventionally identified with — joy, pleasure, enjoyment — whenever these do not strictly go together with the *summum bonum*. It would merely become a synonym for the *summum bonum*, thus fulfilling no distinct role in our vocabulary and giving rise to tautologies of the sort "it would be good if people were happier." It would also imply a marginalization of other potential constituents of a good life — such as meaning, compassion, love etc. beyond their contribution to joy, pleasure, enjoyment — since they would be subsumed under the label of happiness with no separate, specific value left. More in general and perhaps more importantly, it would presume that it makes sense to talk of a single *summum bonum* in the first place — a presupposition which smacks of reductionism and which may reasonably be doubted.

For the purpose of this treatment, it seems appropriate to distinguish between two perspectives on happiness. First, in an empirical-psychological perspective, happiness can be understood as *subjective well-being* (SWB). The crucial term here is "subjective". It means that SWB really is the unquestioned perception of each individual himself as expressed on a one-dimensional scale, rather than some objective concept of "actual well-being" beyond the consciousness of the person in question. When it is stated, for example, that the SWB of person *A* is higher today than it was yesterday, this does not — at least not necessarily — mean that this person is actually faring better today than he was yesterday (*i.e.*, in terms of quality of life). It does mean, however, that he judges his well-being more favorably today than he did yesterday. SWB alone, therefore, does not suffice to tell us how good an individual's life is in an absolute, ethical sense. In interpreting SWB, it should simply be taken at face value, namely as a subject's statement on his perceived degree of well-being.

Secondly, in an ethical perspective, happiness is understood as "the happiness that is justifiably valued" (for short, "valued happiness"). "Valued happiness" would require not only (but also and necessarily) subjective well-being, but also the reflected approval of its propriety by the respective person herself in the presence of all relevant information. A slave, *e.g.*, who does not even envision the possibility of liberty and therefore declares to be happy after being sold to a relatively benign owner would not qualify for valued happiness in this sense when he would, upon deeper reflection, disapprove of his miserable conditions as a reason to happiness. Similarly, a wife who is ignorant of her husband's infidelity might *feel* happy (*i.e.*, report a high degree of SWB), yet would not consider herself happy if she disposed of all relevant information. Hence, in my terminology, she would not *be* happy in the sense of valued happiness. Robert Nozick (1989) makes a similar point by means of a thought experiment. If we disposed of a happiness machine that could give us the perfect illusion of happiness without any negative effects, we would still not regard that experience of happiness equivalent with the happiness we experience in real life, for we do not just care about what we experience in some pleasure center in our brain, but also about the state of the world in the absolute. After all, a cuckold wife is not unhappy for having *learnt* about her husband's infidelity, but about his *being* unfaithful. In other words, we do not only care about our experience, about our self, but about what is actually the case "out there," independent of our personal experience (and hence also independent of our knowledge of what is going on out there). Valued happiness, therefore, is not a solipsist concept — like SWB and the economic concept of utility — but a self-transcendent concept in the sense that it extends beyond the self of the subjectively happy (or unhappy) person.

In this perspective, the status of happiness is radically different from the utilitarian view. Whereas in the utilitarian conception happiness is the only end of intrinsic value with all other ostensible ends being just instrumental and of derivative value, self-transcendent conceptions see happiness as a non-intended consequence or symptom of the accomplishment of a purpose that is a *reason for* a person to be happy — rather than a *cause of* her happiness. In this conception, it is the reasons, not the resulting mental state, that ultimately matter as the *content* of a person's happiness which can therefore best be interpreted as a judgment. As a corollary, happiness cannot be produced or controlled; it must ensue as a byproduct.[11]

The distinctions made here between SWB, valued happiness, and the *summum bonum* (if it makes sense to assume its existence) is a distinction of perspective. It is not suggested that they will generally diverge. On the contrary, it seems safe to assume that in general SWB goes together with valued happiness, and that the criterion of valued happiness will usually lead to a similar ranking of decision alternatives as the criterion of the overall goodness of one's life. When this assumption is accepted, it becomes legitimate to interpret empirical evidence on SWB as equally valid in terms of valued happiness as long as no pertinent reasons are brought forward as to why a particular finding in the space of SWB should not be equally valid in the space of valued happiness.

4. Insights gained by empirical happiness research

Being a rather young discipline, or rather field of research that has gained wider recognition only about a decade ago, empirical happiness research is often encountered with initial skepticism at its epistemological foundation and methodological soundness. Instead of an elaborate discussion of these questions, I will here merely discuss the main points of critique and refer the reader to the relevant literature.

As already mentioned, empirical happiness research investigates subjective well-being, rather than happiness in a more inclusive or even moral sense. It can therefore, *qua* empirical science, make no normative claims to the effect of recommending an increase in SWB. As a corollary, it cannot be criticized from outside for trivializing happiness or for reducing happiness to a one-dimensional, psychological concept. It simply is not about happiness itself but merely about SWB as a related but nevertheless distinct concept. On the other hand, the factual findings of happiness research can of course be used to back up normative claims with empirical evidence (*cf.* Veenhoven 1991).

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[11] *Cf.* Frankl (1978: p. 20); similar Thomä (2003: 22, 269).

Critics might further doubt that self-reports of SWB, the most common source of happiness data, be meaningful in the first place. Yet, psychometric evidence strongly suggests that self-reports produce fairly valid and reliable indicators of SWB (Diener 1994, Larsen/Fredrickson 1999). Even though any single observation may suffer from some measurement problem, such problems concern only a minority of observations and do not appear to be very serious when larger samples of data are concerned. Measurement problems may be more relevant when making comparisons across languages and/or cultures, but their magnitude is not such that they would dominate the true variance of the data (Diener 1984, Veenhoven 1996). Finally, the objection that, *e.g.*, a rich person simply relabels an actually happy state of mind "unhappy" (because he became accustomed to his prosperous life) is invalid because it confuses the space of living conditions with that of subjective experience and judgment (*cf.* Sen 1983b).

Despite the shallowness of this brief justification of empirical happiness research, the skeptical reader may grant in what follows that the methodology of happiness research is indeed as firm as stipulated here. Based on this assumption, it will be argued that empirical happiness research (4.1) is more supportive of a free will than of determinism; (4.2) demonstrates that people's behavior is not always motivated by attaining happiness and, even when it is, that people make systematic errors in anticipating the consequences of their choices on their happiness; (4.3) suggests that adverse systemic effects of individual consumption decisions are pervasive.

4.1 Empirical support for the free will

A number of empirical findings are difficult to interpret without reference to a free will. To be sure, since freedom of will and determinism are *a priori* concepts prior to any experience, no empirical evidence (or theoretical reasoning) can falsify either of them. The argument here is therefore none of falsification or corroboration, but of plausibility. When more and more auxiliary hypotheses are needed to defend the position that one or another introspective reality is in fact just an illusion, that position's plausibility erodes. Under a deterministic conception of human behavior, many types of behavior are not intelligible and have to be reinterpreted by means of such rather far-fetched *ad hoc* assumptions to fit the deterministic conception.

One consistent finding is that a hedonic event typically has two effects of opposite direction on an individual's SWB, and that it is highly context-dependent which effect will dominate. Tversky and Griffin (1991) call these effects *endowment effect* — the direct, affective contribution of an event to one's happiness or satisfaction — and *contrast effect* — the indirect comparison-standard effect of an event on the evaluation of subsequent events. For example, in one experiment college students were asked to recall an event two years in the past. One group of students was asked to recall a positive event, another to recall a negative event. Within each group, one subgroup was asked to recall an event that "happened two years ago", while the other subgroup was asked to recall an event that "happened two years ago, that is, before you came to university". It appeared that the mere reference to a student's college entry reversed the outcome: recalling a *negative* rather than a positive event lead to *lower* SWB when college entry was not mentioned (endowment effect), but it lead to higher SWB when college entry was mentioned (contrast effect; Schwarz/Strack 1999). This pattern strongly suggests that how a given event affects SWB cannot be deduced from the nature of the event, its recency and other objective attributes, but rather that the impact depends crucially on the way an individual thinks about it. What is more, not all respondents react the same way in such experiments. While for some people, rare experiences of intense happiness may have a negative overall effect on life satisfaction (as argued by Parducci 1995), "a few glorious moments could sustain a life-time of happy memories for those who can cherish the past without discounting the present" (Tversky/Griffin 1991: 117). A proponent of a deterministic decision theory will have to argue that these idiosyncratic differences are again the deterministic result of prior events, while a proponent of an indeterminate conception will point to the free will and reject demands to exhaustively explain such differences. She will maintain that the way a person uses a particular event in the evaluation of his life satisfaction is simply up to his free judgment and inherently unpredictable. Amos Tversky, after intensive experimental research in decision making and judgment, concluded that

> "people often do not have well-defined values, and their choices are commonly constructed, not merely revealed, in the elicitation process. […] The systematic failure of the standard model, I suggest, is not due to its complexity, but rather to the fact that people often do not have a global preference order" (Tversky 1996: 185 and 195).

> "If different elicitation procedures produce different orderings of options, how can preferences and values be defined? And in what sense do they exist?"(Tversky *et al.* 1988: 383)

It would be mistaken to interpret this unpredictability simply as unreflected spontaneity or neurological random. After all, people (mostly) have *reasons* to "construct their choices" one or another way.

4.2 Empirical evidence against rational anticipation and happiness maximization

Theoretically, when people fail to make choices that maximize their happiness, this may be due to one of two reasons. Either their anticipation of their choice's consequences on happiness is erroneous, or they are motivated by concerns other than expected happiness. Empirical evidence strongly suggests that both explanations have a role to play.

As far as erroneous anticipation is concerned, people appear to make systematic and substantial mistakes in predicting (and remembering) the satisfaction they expect to derive from particular choices. For example, people systematically overestimate their taste for diversity, choosing more variety when having to make simple consumption choices (such as selecting from a variety of chocolate bars) for the next couple of days in advance than when making an individual choice each day ("diversification bias", Read/Loewenstein 1995). They also overestimate the importance of particular features on life satisfaction when attention is drawn to them, for example when asked whether moving to California would make them happier ("focusing illusion", Schkade/Kahneman 1998). The ability to cope with pain and suffering is also systematically underestimated. People are far too pessimistic when asked how they would feel about an adverse medical report (such as being HIV positive), or when assessing the SWB of a person suffering from a debilitating disease (Loewenstein/Schkade 1999).

Yet, even when people do manage to make rather accurate predictions of their SWB, they fail to make decisions consistent with happiness maximization. For example, when presented with the hypothetical alternatives (*A*) to earn $33,000 when one's colleagues earn $30,000, or (*B*) to earn $35,000 when one's colleagues earn $38,000, most people (84%) believe that they would feel *more satisfied* in situation *A*, while a minority (38%) say they would actually *choose* situation *A* (Tversky/Griffin 1991: 114-15).[12] This finding can be interpreted as reflecting the influence of conventional norms of what one rationally ought to want, and the overstatement of hard criteria in these norms. The amount on one's paycheck may simply and without giving it deeper thought be considered more relevant to the job decision than how happy one will actually feel having that job with that pay structure. The authors interpret this finding in the following way:

> "When people are asked to assess the hedonic value of some future states (*e.g.* job offers) they try to imagine what it would feel like to experience those states. But when asked to choose among these states, they tend to search for reasons or arguments to justify their choice. [...] judgments of satisfaction and choice can yield systematically different orderings" (Tversky/Griffin 1991: 114).

Others go even further:

> "Many decisions involve little conscious deliberation. People decide based on rules ..., habits ..., and gut feelings, none of which involve explicit predictions of future feelings. The most common source of experimental surprise could therefore be the *absence* of an explicit prediction in the first place" (Loewenstein/Schkade 1999: 100)

If this interpretation is correct, the significance of these findings to economic theory can hardly be overstated. Decisions do not only deviate from utility maximization because people make errors in the anticipation of satisfaction. They also do not seem to rely on happiness as the overriding choice criterion. On the contrary, choice seems to be guided by socially accepted standards of reasonableness which overemphasize "hard" and tangible cues, in particular monetary ones. For example, people have been found to be far more reluctant to buy an hour of leisure (when offered to buy suppression of ads on TV, or to pay for reduced commuting time) than they are willing to sacrifice an hour of leisure for paid work (as implied by their marginal wage rate; Scitovsky 1974), perhaps because they follow a norm that 'one ought to economize on money expenditure', such as pay-TV subscriptions, when the sacrifice consists "only" of intangible benefits, like leisure time. Lane, *e.g.*, posits that "the market culture teaches us that money is the source of well-being," and that people, "lacking privi-

12 The satisfaction question and the choice question where asked to two different groups of 32 and 34 respondents, respectively.

leged knowledge of the causes of their feelings, ... accept conventional answers" (Lane 2000: 72).

4.3 The consumers' dilemma

The perhaps single most important finding of empirical happiness research is that income contributes to an individual's SWB not so much through its absolute size, but merely to the degree it exceeds, or falls short off, a comparison standard of income (or, more precisely, consumption). An individual earning $20,000 a year (in terms of 2001 US dollars) is likely to belong to the happiest group in Russia today (where average income is $7,100) and would have been among the happier in the US in the 1950s (when average income did not exceed $14,000). With the same absolute income, however, a person's happiness is likely to be well below average in the US today with a per capita income of $34,000 (figures are from UNDP 2003). Similarly, when in the US people were asked, in each year between 1950 and 1986, "What is the smallest amount of money a family of four needs to get along in this community?", the average amount mentioned grew at almost exactly the same pace as actual incomes, always being at roughly three quarters of average income (Rainwater 1994: 26).

There are at least two distinct reasons for this "relative-income effect." First, people get accustomed to most kinds of comfort. This "hedonic adaptation" (*cf.* Frederick/Loewenstein 1999) effect reduces the pleasure one derives from a new car, good concerts, one's favorite meal, or even a multimillion dollar yacht when these pleasures are experienced frequently (*ibid.*). Hedonic adaptation as such would not pose a problem if people correctly anticipated this effect and took it into account in their decisions, but they seem to largely ignore this effect (Loewenstein/Schkade 1999).

Much more important in this context, however, is a second effect, the "frame-of-reference effect" (Frank 1997). The main idea behind this effect is that one's satisfaction with one's consumption standard is assessed with respect to a frame of reference which is made up of the consumption patterns prevailing in one's society (or a more or less well-defined reference group which may include one's brother in law or Hollywood movie stars). This implies that when *A* increases her consumption, this will have a negative impact on *B*'s SWB because it raises *B*'s frame of reference. In other words, consumption comes with a negative "positional externality" (Frank 1997). In an ethical perspective, two cases of such externalities ought to be distinguished.

In the case of *regretted externalities*, the negative effect comes as an unintended side-effect of consumption. That is, the benefit for which a good is desired does not *depend* on the negative externality. The "perpetrator" can therefore regret the externality without committing inconsistencies. An example for a regretted externality is the wearing of decent clothes. An individual who buys good clothes simply to make a good appearance and to not look neglected contributes to raising the common standard of a decent outward appearance even if she preferred not to do so and is not concerned about standing out from the average. As Adam Smith already remarked,

> "A linen shirt [...] is, strictly speaking, not a necessary of life. The Greeks and Romans lived, I suppose, very comfortably, though they had no linen. But in present times, through the greater part of Europe, a creditable day-labourer

> would be ashamed to appear in public without a linen shirt, the want of which would be supposed to denote that disgraceful degree of poverty, which, it is presumed, no body can well fall into without extreme bad conduct." (Smith 1976/1784: 870)

While Smith's linen-shirt example may seem irrelevant to our times, it is in fact representative of a more general social dynamic that is rather more, not less, relevant today than in Smith's days. As a society becomes richer, certain functionings (Sen 1985) may simply become more costly. For example, as more and more people own a private car, public transport tends to deteriorate, making it more difficult for people without a car to get around, just as Smith's poorer contemporaries found it more and more embarrassing to appear in public without a linen shirt. In effect, then, the higher consumption standard brought about by economic growth exerts a negative externality that neutralizes much of the income gains of those who benefit from economic expansion while it actually hurts those who see their incomes stagnate.

These kinds of regretted externalities are essentially equivalent to the problem of environmental pollution from heating one's house. In both cases, an as such "innocent" consumption activity happens to inflict costs on society. In the absence of these external costs, the consumption activity would not lose its value to the consumers.

By contrast, *intended externalities* occur when the benefit of a consumption activity is contingent on the cost imposed on others. A classical example of intended externalities is competition for status by means of "conspicuous consumption" (Veblen 1986/1899, *cf.* also Frank 1999). When an individual buys an expensive car for the mere purpose to lift herself above the average, her car will enhance her status exactly to the degree it lowers that of others since competition for status — or *positional competition* (Hirsch 1976: 52) — is essentially a zero-sum game: "What winners win, losers lose" (*ibid.*). In effect, the satisfaction conspicuous consumption conveys to the consumer is "satisfaction [...] derived from scarcity itself" (*ibid.*: 28).

> "The power of the money in my pocket is far from being merely the liter of milk or the pleasure it buys. It is also the relative lack of money in the pockets of the others" (Giannetti da Fonseca 2002: 80)

Since individual benefit and social cost are two faces of the same coin, the consumer cannot sincerely regret the cost she inflicts on others since her consumptive value relies on that very cost.

Competition for status seems to account for a significant share of expenses, or effort in general, in industrialized societies. Purchases of luxury goods seem to be largely motivated by a consideration for status. The spread of cosmetic surgery implies an increasingly negative exposure of oversized noses or natural wrinkles, making the need for cosmetic interventions ever more painfully perceived by those who cannot afford the treatment. Job applicants spend more and more money on fine suits to out-dress their competitors, and executives on handcrafted watches to impress their business partners.

Yet, the zero-sum game of positional competition is not limited to competition for status. It rules wherever people compete for benefits that are scarce absolutely, *i.e.*, where supply is fixed rather than increasing with demand. No matter how many colleagues put in extra hours to increase their odds to succeed their parting boss, only one of them can get the job. And no matter up to which amount art lovers bid up the price of Rembrandt's masterpieces, there will only be so many of them around until the end of times.[13]

In an ethical perspective, the legitimacy of conspicuous consumption seems to be questionable. Spinoza, writing a century before Kant, already implicitly posited that conspicuous consumption should not be a basis for happiness:

> "Whoever considers himself happy because fate has given a better lot to him than to others, is still ignorant of real happiness. [...] [People should] not desire something which they do not also desire for the rest of mankind" (Marcuse 1962: 199).

In particular circumstances, the legitimacy of conspicuous consumption may be difficult to appraise. This is the case when status is aspired as a means to a legitimate end, or when an increase in status means an improvement from a low starting point. For example, an attorney may buy a prestigious car in order to signal her ability (since otherwise potential clients may conclude that she must be a very bad lawyer for not being able to afford a better car), even though she does not personally care about status. Demanding from her to drive a more modest car might mean asking too much, considering the loss in income which might ensue. Similarly, it would seem presumptuous to deny a person with serious facial deformation the right to cosmetic surgery on the grounds that this will have a negative effect on those who cannot afford such treatment.

On a societal level, positional competition is essentially a prisoner's dilemma, *i.e.*, a situation where a socially benign outcome requires a commitment to social norms from each individual or an institutional solution involving constraints or incentives to influence behavior into the desired direction. The money job applicants spend on suits, *e.g.*, does not buy any overall improvement for job applicants as a whole. If all job applicants together could agree on, and enforce, an agreement to cut in half their respective apparel-budgets, they would save a significant amount of money while not reducing anybody's chances to a job. While this example is admittedly illusory as there seems to be no way to enforce such an agreement, the idea as such is not far fetched. Union agreements stipulating maximum working hours in effect protect job applicants from positional competition in terms of working hours, and the ban of steroids allows athletes to win Olympic medals without putting their health at risk in a self-destructive positional rat race.

This kind of reasoning, one might object, is not really new and does not require empirical happiness research. After all, the relativity of poverty and welfare was already stipulated by Adam Smith (see quotation above) and was backed up empirically already in 1949 by Duesenberry. However, a purely theoretical argument would be vulnerable to its own argument of the relativity of satisfaction. After all, it might be ob-

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13 The examples given here can still be distinguished further. The case of colleagues competing for a job promotion, *e.g.*, might even be worse than a zero-sum game, with the loss of the losers larger than the gain of the winner, just as in a lottery with a negative expected value.

jected that hedonic adaptation and social comparison will nullify the benefit of saving money on suits, working less hours, or maintaining one's health because whatever people will do with their saved money or saved time, they will adapt to these gains as well and compare themselves with others and be once more left without any durable increase in SWB. Fortunately, however, empirical psychological research shows that not all kinds of consumption (or nuisances) are subject to hedonic adaptation and social comparison. For example, people clearly do not adapt to noise, to stress from commuting through dense traffic, to chronic pain, to a lack of holidays, and above all they do not adapt to unemployment which in study after study is found to dramatically reduce SWB (Frank 1999). They also derive happiness from the absolute number of holidays they can take per year, and appear not to care much about how that number compares to the holidays of others (*ibid.*). Therefore, diverting resources away from suits, luxury watches, and cosmetic surgeries towards noise abatement, research on pain treatment, holidays, and the reduction of unemployment can be expected to lead to a sustained net increase in SWB. On a more fundamental level, social waste from positional competition would be most effectively reduced if people were less status-minded and derived satisfaction from doing their job well (a game against nature) rather than from excelling over others (a game against people; Layard 1980: 744).

5. Conclusion: Contributions to economic ethics

Rather than with a summary, I shall conclude by making explicit the nature of the contribution empirical happiness research can make to economic ethics. To be sure, empirical happiness research does not offer entirely novel modes of ethical reasoning, and it does not add much, if anything, to the conceptual groundwork of modern economic ethics. Rather its contribution lies (1) in bolstering theoretical arguments with empirical evidence and (2) in demonstrating far-reaching congruence between demands derived from utilitarianism and those derived from Kantian ethics.

(1) For good reasons, the debate around the appropriateness of homo oeconomicus as a model of human behavior is largely a theoretical one. After all, since motives of human decision making cannot be observed, one can stipulate basically anything to be the object of intentionality. In a Popperian sense (Popper 1959/1934), therefore, the motivation of human behavior is beyond falsification and not a proper object of scientific theories. This is of course one reason for the prominence of "assumptions" in economics, since, as a behavioral science, economics would not get anywhere without them. Now, by postulating an identity between choice, motives, and happiness, economics opens an entry point for empirical evidence to the degree happiness can be observed. As has been argued in this paper, empirical psychology is now in a position to do just that, and it already produced sufficient evidence to cast doubt on the economic model. On an individual level, the evidence suggests that people *make* rather than just *have* preferences; that, as a corollary, people have at least some discretion in choosing what they want to derive happiness from; and that they are not exclusively motivated by happiness maximization. In addition, even where people are motivated by increasing their happiness, they frequently fail to do so due to systematic prediction errors. On a societal level, happiness research shows that even individually success-

ful happiness maximization is self-defeating in many, though not all, domains because of the pervasiveness of prisoner's dilemma situations and of hedonic adaptation.

(2) As a matter of fact, economics continues to be dominated by utilitarian thinking. Non-utilitarian ethicists typically try to convince utilitarians of the weakness of their philosophical foundations, but that strategy seems to bear little fruit. As an alternative "second-best" strategy, however, happiness research now allows them to show that prescriptions derived from utilitarian reasoning converge in important respects with those derived from more egalitarian ethical concepts when empirical evidence on happiness is brought into the utilitarian equation. A case in point is the argument by Richard Layard, a confessing utilitarian economist, that a marginal tax rate of around 60% — roughly of the magnitude prevalent in most European economies (taking together direct and indirect taxes) — is justified on the basis of positional externalities and people's failure to anticipate hedonic adaptation (Layard 2003, similarly Frank 1999). What seems to be an argument of distributive justice and a renunciation of the principle of efficiency — an almost sacred principle in (welfare) economics — is here in fact a utilitarian efficiency argument backed up by empirical evidence. More fundamentally, the very way of utilitarian thinking about inequality and poverty changes when happiness research is taken seriously. Traditionally, a scenario where the rich get richer while the poor's incomes stagnate is not considered problematic in (new) welfare economics because the Pareto criterion is still satisfied: As long as no one loses any income, the increase of somebody's income is deemed an unconditional social improvement. When happiness is no longer axiomatically equated with income, however, the scenario described no longer satisfies the Pareto criterion because empirical happiness research shows that the rise of the incomes of the already affluent imply deepening destitution for those whose incomes stagnate at a low level. In other words, efficiency in the space of happiness is not the same thing as efficiency in the space of incomes. In this sense it can be shown that the position of an "empirical utilitarian" tends to converge at least some way towards that of a more egalitarian social ethic.

The pragmatic approach and the ideological permissiveness of the argument developed here might alienate moral philosophers. Yet, when economic ethics is understood as having not only an epistemological ambition but also a practical one, *i.e.*, as seeking not only to clarify what constitutes good economic and business practice, but also to contribute intellectually to its becoming reality, the present endeavor may be forgiven the dents and bumps in the disciplinary bridges it has attempted to erect.

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