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**The Marginal Utility of Income**

**R. Layard, G. Mayraz and S. Nickell**

## **Abstract**

In normative public economics it is crucial to know how fast the marginal utility of income declines as income increases. One needs this parameter for cost-benefit analysis, for optimal taxation and for the (Atkinson) measurement of inequality. We estimate this parameter using four large cross-sectional surveys of subjective happiness and two panel surveys. Altogether, the data cover over 50 countries and time periods between 1972 and 2005. In each of the six very different surveys, using a number of assumptions, we are able to estimate the elasticity of marginal utility with respect to income. We obtain very similar results from each survey. The highest (absolute) value is 1.34 and the lowest is 1.19, with a combined estimate of 1.26. The results are also very similar for subgroups in the population. We also examine whether these estimates (which are based directly on the scale of reported happiness) could be biased upwards if true utility is convex with respect to reported happiness. We find some evidence of such bias, but it is small—yielding a new estimated elasticity of 1.24 for the combined sample.

JEL Classifications: I31, H00, D1, D61, H21

Keywords: Marginal utility, income, life satisfaction, happiness, public economic, welfare, inequality, optimal taxation, reference-dependent preferences

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Richard Layard is Director of the Wellbeing Programme at the Centre for Economic Performance, London School of Economics. Guy Mayraz is an Occasional Research Student for the Wellbeing Programme at CEP, and Research Student in the Department of Economics, LSE. Stephen Nickell is Professor of Economics and Warden of Nuffield College, Oxford. He is also an Associate of the Labour Markets Programme, CEP.

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