

Self-Reported Satisfaction: Determinant or Outcome?

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Introduction

Although social science surveys have long asked respondents to report levels of life satisfaction or happiness, economists have only begun to use those data in the last ten years or so. Frey and Stutzer (2002) suggest that measures of life satisfaction or subjective well-being can proxy for utility. If one accepts these measures as a proxy for utility then one can then estimate what directly yield utility. Frey and Stutzer suggest that studying the determinants of life-satisfaction will yield implications for economic theory and public policies. If one is willing to assume that life-satisfaction measures can be used to construct a social welfare function one can then examine how social welfare increases or diminishes with policies such as taxes, income redistribution, levels of inflation, and unemployment.

This paper investigates an alternative interpretation of self-reported happiness - that it possibly measures at least two things – one's fundamental state of mind and the psychological result of consumption activities. Using panel data from Great Britain (British Household Panel Study) and Germany (German Socio-Economic Panel), I show that unhappy people are more likely to start smoking and that people are more likely to quit when they become happier. These results are consistent with a model in which individuals are not addicted to cigarettes but instead use cigarettes to medicate symptoms of a preexisting mental condition. The model implies that one's state of mind determines consumption not the reverse. It also implies that reduction in smoking brought about by an increase in taxes will reduce consumer welfare. More generally this paper shows, using longitudinal data that allows us to document levels of and changes in life satisfaction *before* or *after* an individual consumes a particular good.. This evidence can then be used to assign the direction of causality between life satisfaction and consumption.

References

Frey, B.S. and Stutzer, A. (2002), What can economists learn from happiness research, *Journal of Economic Literature* 40, 402-435