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Why Don't the Rich Just Buy More Happiness?

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Abstract

Using the title question, this paper presents the development of a theoretical framework for examining the money-happiness relationship. The concepts of time, efficiency, and happiness-producing behaviors were incorporated with basic economic principles regarding preferences, diminishing marginal utility, and budget constraints to construct the Money-Happiness Model. The model not only provides a framework to aid future research, but also provides educators and counselors the conceptual relationships necessary to design more effective financial programs and interventions.

Introduction

For years I have espoused as truth to my personal finance students and workshop participants the oft-quoted maxim that “money doesn’t buy happiness.” The idea that money is not the solution to life’s problems, indeed, that the pursuit of money is sinful, has been around for many years. For example, the Christian Bible (King James Version), identifies the love of money as the primary source of all evil (1 Timothy 6:10), and states that a rich man has little chance of getting into heaven (Luke 18:25). Student comments during in-class discussions about money and happiness suggested that these old money values are still a major influence on our collective consciousness. For example, over the years I have noted, especially within academia, the reluctance of most people to admit that they “love” money and that they do their job, in large part, “for the money.” I can still recall being told by an administrator during a faculty meeting early in my career that teachers should quit worrying about their salaries and teach “for the love of teaching.” I’ve also observed that while many people will publicly support the money-doesn’t-buy-happiness adage, few seem to believe that it applies to them; instead, they “spend” much of their lives trying to prove it wrong.

The purpose of this paper is to present the development of a practical theoretical model that explains some of the relationships between money and happiness. Several assumptions guided the construction of the model:

1. People prefer more happiness to less happiness.
2. Happiness is not experienced directly through an individual’s behaviors; that is, there is a lag between the happiness-producing behavior and the happiness experienced.
3. Satisfaction (utility) or dissatisfaction is the immediate experience of all behaviors.
4. Some behaviors may provide high satisfaction, but little happiness. “For example, addictive drugs can produce immediate psychic highs, but their long-term effects are often extremely unhappy” (Parducci, 1995, p. 16).
5. Because individuals often misperceive which behaviors will produce happiness (Nettle, 2005), they seek to maximize happiness by maximizing total utility.

Constructing the Model

The model was constructed based on two types of people: (a) those who experience higher levels of satisfaction from just having more money, and (b) those who experience higher levels of satisfaction from consuming more of the goods and services that money will purchase. If happiness were a direct function of income only, $H = f(\$)$, then additional income would increase the level of happiness for both types of people, and the happiest people would always be those with the highest incomes.

Some studies have provided empirical evidence that rich people may be happier than other people (see Bruni & Porta, 2005). This relationship appears to be strongest when comparing the rich to the very poor (Argyle, 2001). However, when comparing the rich to individuals with at-or-above-basic-needs incomes (i.e., the less rich), the relationship between income and happiness, as illustrated in Figure 1, is not as pronounced. Some evidence suggests that the slightly greater happiness of the rich is based on relative, not absolute, income. That is, happiness is relative to what everyone else has; if everyone’s income were to increase (or decrease) by the same amount, there would be no change in happiness (see Frank, 2005). At some point, though, having more income apparently brings little or no additional happiness (Myers, 1992).

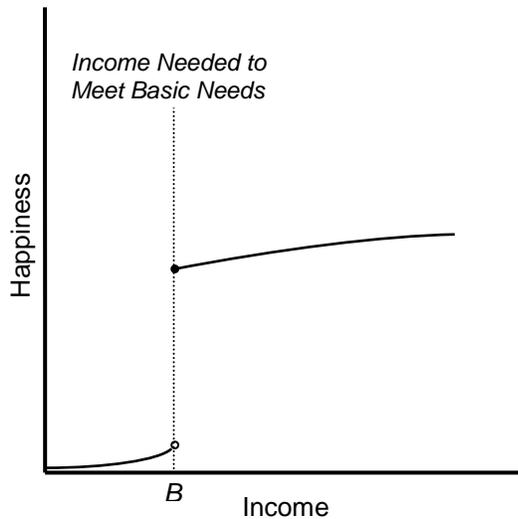


Figure 1. Relationship between happiness and income. The level of income necessary to meet basic needs (B) distinguishes the very poor ($I < B$) from the rich ($I \gg B$) and the less rich ($I \geq B$).

Utility theory (see Samuelson & Nordhaus, 1992) suggests that those who derive happiness from having relatively higher incomes have a set of preferences similar to those illustrated by the utility curves in Figure 2. The popular expression, “I’m happy so long as I make more income than my wife’s sister’s husband,” succinctly states the relative-income position of the rich. Why, then, are the rich, who experience this presumed happiness-producing behavior of income comparison, not substantially happier than the less rich? Three possible explanations follow.

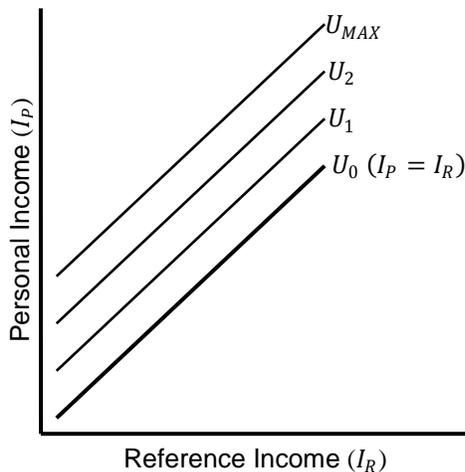


Figure 2. Utility curves illustrating an individual’s preference for relatively-more income. The U_0 curve (no utility) represents the condition when personal income is identical to the reference income. As personal income exceeds the reference income, higher levels of utility (U_1, U_2, U_3) are experienced until maximum utility (U_{MAX}) is achieved. When maximum utility is achieved, additional income provides no additional utility.

First, the behavior of acquiring relatively more income is simply not a happiness-producing behavior; there is no relationship between money and happiness. Studies that find a positive relationship must in some way be flawed.

Second, individuals do not (or cannot) practice only happiness-producing behaviors. That is, based on personal needs or desires, individuals prefer a combination of both happiness-producing behaviors and other behaviors (see Figure 3). However, because more happiness is preferred to less, and the much greater incomes of the rich would

always allow them the ability to “purchase” greater quantities of all behaviors (moving them higher on their behavior-preference curves), behavior preferences alone do not explain why the rich appear to be only slightly happier than the less rich.

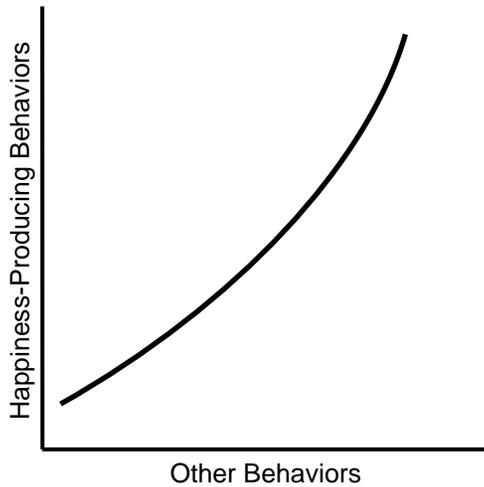


Figure 3. The behavior-preference curve. Each point on the curve represents the preferred (or optimal) combination of happiness-producing behaviors and other behaviors for a given level of happiness; greater levels of happiness are achieved at points on the curve farther from the origin.

The third explanation is rooted in the law of diminishing marginal utility, which suggests that marginal utility declines with each additional unit of relative income, resulting in total utility growing at increasingly slower rates (see Samuelson & Nordhaus, 1992). In an effort to maximize total utility, individuals at point *M* (see Figure 4) will switch to other behaviors whose marginal utilities are still greater than zero.

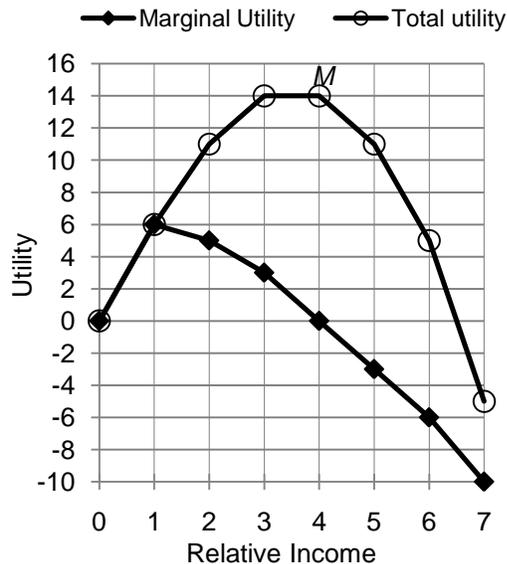


Figure 4. Changes in marginal utility (MU) and total utility (TU) as relative income increases. Maximum total utility is achieved at point *M*, where $TU > 0$ and $MU = 0$.

Thus, happiness-producing behaviors and other behaviors mutually influence each other through behavior preferences and diminishing marginal utilities, which interact to both constrain and facilitate each type of behavior

(see Figure 5). The rich who gain happiness through the status of having relatively-more income are quickly limited by their preferences for other behaviors, and by the low marginal utility of additional income.

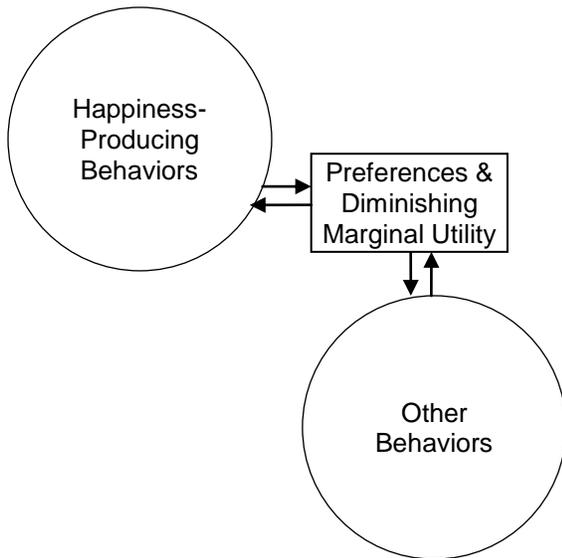


Figure 5. The interactions of preferences and diminishing marginal utility with happiness-producing behaviors and other behaviors. Preferences for one type of behavior results in more of those behaviors until diminishing marginal utility makes the other type of behavior preferred, resulting in increases in the newly-preferred behaviors. The process continues until an optimal combination of both types of behaviors (i.e., maximum combined utility) is achieved.

Economists often use indifference curves to examine questions of consumer choice between two goods (or services). Each curve represents all combinations of goods and/or services that provide the same level of utility. Curves farther from the origin represent higher levels of utility. Based on the assumption that consumers always prefer more to less, the best choice for the consumer is that combination of goods and/or services that lies on the curve farthest from the origin. However, consumers generally are prevented from making their desired choice by market prices and their income, which comprises their budget line/constraint (see Figure 6).

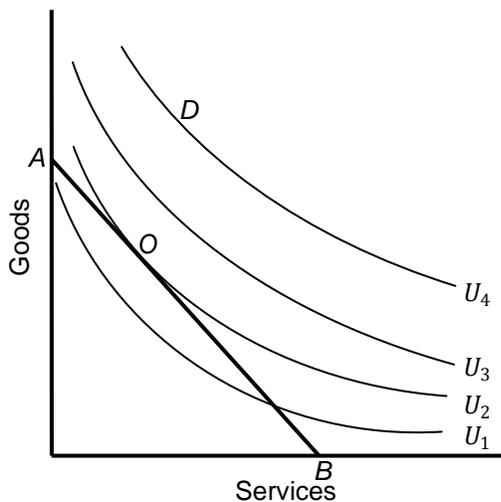


Figure 6. Indifference map for all goods and services. Line *AB* indicates the budget constraint imposed by prices and income. Point *D* is the desired choice. However, Point *O* represents the optimal combination of goods and services (i.e., the point of maximum attainable utility given the constraints), and is the point where the budget line is tangent to the highest indifference curve.

Assuming similar preferences and stable prices, the budget line for an individual with a higher income will always be tangent to an indifference curve of higher utility (i.e., budget lines for the rich are farther from the origin). Why, then, are the rich, whose incomes allow substantially more consumption, not much happier than the less rich? Again, three possible explanations follow.

First, the presumed happiness-producing behavior of additional consumption is, in reality, not a happiness-producing behavior.

Second, like the status-driven rich, the consumption-driven rich are also constrained by preferences and diminishing marginal utilities. Indeed, the interactions depicted in Figure 5 are applicable to all behaviors, by all people. However, this explanation only provides a partial answer for the constraining effects of prices and income on the rich, who can afford substantially greater consumption associated with both happiness-producing behaviors and other behaviors.

The third explanation is that other constraints, not depicted in the typical indifference-curve analysis, prevent the consumption-driven rich from achieving higher levels of happiness. Those constraints are related to time and efficiency. It is plausible that the rich simply run out of time to consume or to enjoy their consumption.

When the budget constraint is defined more broadly to include all resources and behaviors, then the effects of time and efficiency can be included.

If: $T = \text{Time (constant constraint)}$,

$R = \text{Resources other than time (variable constraints)}$,

$t = \text{average amount of time expended per behavior (efficiency variable)}$,

$r = \text{average amount of resources required per behavior (efficiency variable)}$,

$B_{\#} = \text{Total number of behaviors possible}$, and

$T, t, R, r > 0$, then

$B_{\#}$ is constrained by R, r, T, t such that

$$B_{\#} = \min \left\{ \frac{R}{r}, \frac{T}{t} \right\}.$$

The resulting behavior constraints are depicted in Figure 7, and are applicable to individuals of all income levels.

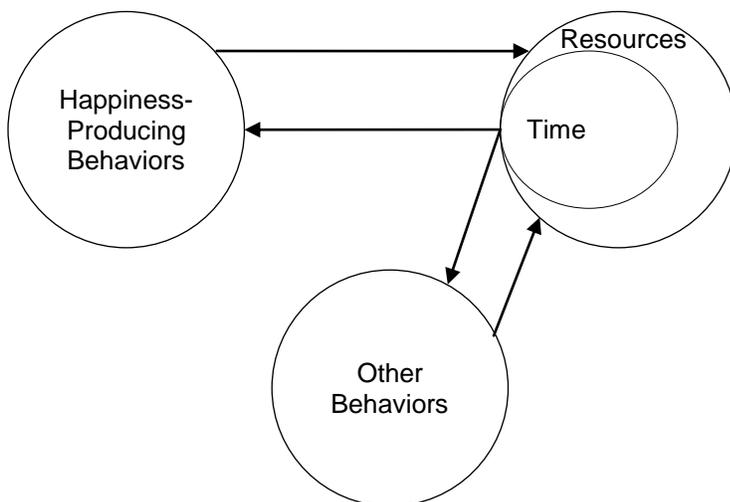


Figure 7. Time and other resources as constraining factors on happiness-producing behaviors and other behaviors. Time is a universal, constant constraint unaffected by any behavior. Other resources are variable constraints that not only limit behaviors, but also decrease or increase in quantity as a result of behaviors. For example, income constrains spending, but employment increases income.

Example of Calculating Behavior Constraints

Suppose that within a 24 hour period ($T = 24$) an individual has total resources of \$100 ($R = 100$), and that on average it requires 1 hour for each behavior ($t = 1$) with an average expenditure of \$10 per behavior ($r = 10$), the total number of behaviors that can be accomplished is:

$$\min \left\{ \frac{R}{r}, \frac{T}{t} \right\} = \min \left\{ \frac{100}{10}, \frac{24}{1} \right\} = \min \{10, 24\} = 10.$$

Given his/her current levels of efficiency, this individual has sufficient time to complete 24 behaviors, but is constrained by resources to only 10 behaviors. To increase the number of behaviors possible this individual would have to lower the expenditure per behavior (i.e., increase resource efficiency) and/or increase total resources. If, all else being the same, this individual's total resources were to increase to \$500, resources would allow 50 behaviors, but time would constrain her/him to only 24 behaviors. In this situation only an increase in time efficiency would increase the number of behaviors possible.

The complete model (see Figure 8) was achieved by combining the elements from Figures 5 and 7. Although developed from the question as to why the rich are not substantially happier than the less rich, the Money-Happiness Model is applicable to individuals of all income levels.

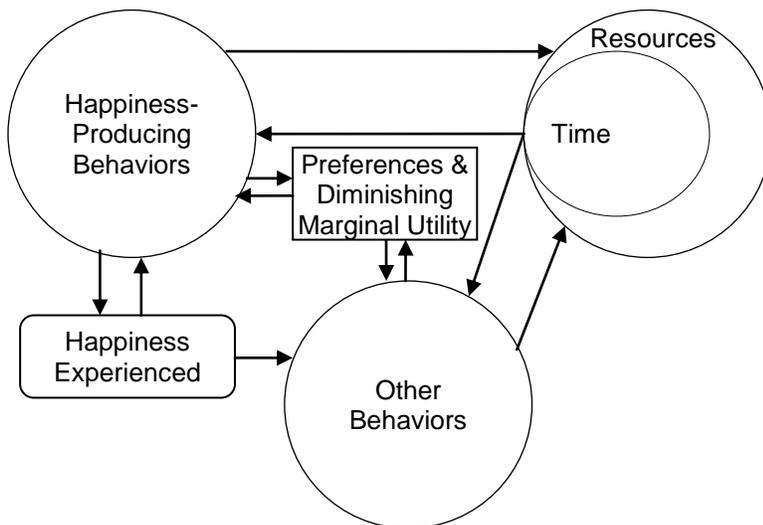


Figure 8. The Money-Happiness Model. Happiness experienced is a direct function of happiness-producing behaviors. Behavior choices are affected by the presence or absence of past happy experiences, preferences, and diminishing marginal utilities. Additionally, all behaviors are constrained by time, other resources, and the efficiency with which all resources are employed.

Applying the Model

The Money-Happiness Model identifies key concepts and relationships that educators and counselors can use to help students and clients pursue a happier life. A first step in applying the model is to assess current preferences, resources, behavior patterns (including time use), and overall happiness. Educators and counselors can employ formal tools such as having students and clients complete income and expense statements, time diaries, and written goals, or they may use informal conversational questions such as “When are you the happiest?” and “What is most important in life?” to make assessments.

Next, educators and counselors should help students and clients identify current behavior patterns that are likely to produce happiness (and those that will probably not). For example, some may be unhappy with their bodyweight, but not realize that their daily behavior of consuming soft drinks, which produces immediate utility, is a contributing factor in their weight gain (i.e., consuming soft drinks is not a happiness-producing behavior for them).

Finally, educators and counselors should help students and clients identify ways to increase resources and/or efficiency in the use of time and resources (possibly through education, job training, or saving and investing). For example, the model indicates that the poor—those who have more time than money—should concentrate on acquiring more resources to raise their level of happiness (in this case money does buy happiness). For the rich and the less rich, those who have more than sufficient resources, the model indicates that to increase happiness they will have to improve efficiency in the use of their time and/or pursue different types of behaviors. For example, they may be counseled to consider hiring someone to do housekeeping, or to devote more of their time and resources to charitable pursuits instead of personal consumption.

Conclusion

The Money-Happiness Model is not without limitations. While the comparative efficiency for two different behaviors can usually be determined (e.g., mowing one's own lawn v. hiring someone else to mow it), it is difficult to measure an individual's overall time- and resource-use efficiency. Additionally, except for the implied influence that past experiences have on preferences and behavior choices (see Figure 8 caption), the model does not explicitly account for the role that perception plays in experiencing happiness. Finally, the model needs further testing and validation through empirical research and program evaluation.

Even with its limitations, the Money-Happiness Model provides a practical, conceptual framework for researchers, educators, and counselors who work to help individuals and families, especially the poor and less rich, to more effectively manage their financial lives in connection with their pursuit of happiness.

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