Frontiers in Business, Economics and Management
ISSN: 2766-824X | Vol. 7, No. 1, 2023

Research on the Relationship Between Income and Happiness: From the Perspective of Economics

Jiawei Hu[1, *]

[1]School of Shanghai University, Shanghai, 200000 China
[*] Corresponding Author

Abstract: With the Economic Reform and Open-up, China's per capita disposable income had been greatly improved since the beginning of the 21st century. However, according to the survey, the relationship between income and happiness was not simple linear. Based on this, this paper analyzed and discussed the relationship between income and happiness from the perspective of economics, and gave answers to how to improve happiness. Specifically, this study first discussed the linear relationship between income and happiness, then putted forward the "income" and "non-income" factors that affect happiness and their mechanisms, and finally putted forward relevant suggestions on how to improve happiness.

Keywords: Happiness, Income, Utility, Desire.

1. Introduction

The central argument of modern economics is that economic growth leads to happiness increase. But as the discussion progressed, the study found that the relationship between income and happiness was not entirely positive. A case in point is the Gallup survey of Chinese consumer happiness. According to the data, with the increase of per capita disposable income, the happiness index of Chinese consumers showed a trend of first rising and then decreasing from 1994 to 2004. The score was 69 in 1994, 71 in 1997, and 67 in 2004. Surprisingly, the economic growth had not brought about a higher consumption index. This is the famous "Easterlin paradox". In microeconomic theory, economists simply equate "happiness" with "utility", thus transforming happiness into a measurable variable.

According to a simple analysis from the perspective of economics, with the increase of income, the budget constraint line gradually moves to the upper right, consumers can buy more goods or services, and the utility they get also increases. The simple analysis above leads to the conclusion that high income represents high happiness. But this does not explain the "Easterlin paradox".Utility is not completely equivalent to happiness, and happiness also depends on many variables. When the negative utility of other variables can offset the positive effect caused by rising income.

2. "Non Income" Factors Affecting Happiness

2.1. Desire

Samuelson, the Nobel laureate in economics, pointed out that personal happiness=material wealth/consumption desire, and happiness is positively related to wealth and negatively related to desire. According to Samuelson's happiness equation, happiness depends on the relative size of wealth and desire. To judge whether a person is happy or not, we can get from the answer: if the dividing line is 1, less than 1 is not happy, equal to 1 or much happier than 1. When desires are fixed, individuals with greater wealth are happier; When wealth is set, the less desire, the happier. So there are two ways to get happiness: increase your wealth or decrease your desires. When wealth and desire increase together, if the rate of increase of wealth is slower than the rate of increase of desire, happiness will decrease. For example, a monthly salary of 6,000 yuan is more than enough for most young people, but far from enough for middle-aged people who need a lot of money to support their families. At the same wage level, new employees may be happier, while seniors may be less happy.

However, the reality is that personal desire is constantly rising. The dissatisfaction with current income, the decrease of happiness, the expansion of desire or the pursuit of higher consumption level will increase the motivation of individuals to increase their income by increasing work intensity. When the income growth is stuck in the bottleneck, the desire cannot be satisfied, which will lead to the decrease of self-evaluation, and finally lead to the decline of happiness. This process will lead individuals into a vicious circle. To sum up, after the income meets the basic needs of life, we should seek new stimulation points or reduce desire to improve happiness, rather than blindly pursue high income.

2.2. Self-realization

Abraham Maslow, an American psychologist, putted forward the hierarchy of needs theory from the perspective of human motivation, which emphasized that human motivation was determined by needs. In addition, in each period, there was a demand that dominates while other demands were subordinate. Human needs are divided into five levels: physiological needs, security needs, belonging and love needs, respect needs and self-realization needs. Requirements are formed and met from low to high.

In Maslow's view, the goal of hungry people was to find food, the goal of people who lack a sense of security was security, belonging was the same as the need for love and respect. While "self-realization" was "the road few people take", only those who truly meet low-level needs could easily achieved self-realization. From the perspective of material wealth effect, income could only meet low-level physiological and security needs. When the income could meet people's basic needs, happiness will increase. However, income alone could not meet high-level needs.

For example, educators who work hard at the grassroots level. On the one hand, their work attitude is respected by parents and loved by students, on the other hand, they also gain the joy of education and realize their self-worth. The improvement of happiness brought by imparting knowledge cannot be realized by income alone.

In addition, there are non-economic factors such as family, health, freedom and living environment, and if income increases at the expense of these factors, it will be difficult to improve happiness.

3. The Effect of Income on Happiness

3.1. Nominal Income versus Real Income

Nominal income refers to the income obtained by people in the form of currency without considering market factors. Real income is the purchasing power of nominal income, which is the goods and services that nominal income can buy compared to the previous period. In general, nominal income is the absolute amount of money, excluding the influence of price factors, real income is the income under the influence of changes in the price level. Affected by inflation, when the rate of wage growth is lower than the rate of inflation, the rate of income growth will be slower than the rate of price growth. This leads to a decline in purchasing power, living standards and happiness. When expected inflation is high, residents are generally negative about the future economic situation. People will offset worries about the uncertain future by reducing their current consumption.

3.2. The Relativity of Income

The amount of income will affect individual happiness, but how to compare income has also become a key issue affecting happiness. Typically, people don't use absolute income as a basis for judging their happiness, but rather compare it vertically and horizontally with others.

In a stable economic environment, the currency value fluctuates less. When an individual makes a longitudinal comparison of his or her income in different periods, if the income increases steadily or excessively according to the expectation, it can offset the negative effect of inflation, then the person's happiness will be improved, otherwise it will decline.

People will compare their current income horizontally, mostly with classmates, friends and colleagues, because their main characteristic is that their income is not very different. Since income is the most direct and quick indicator to judge one's achievement and social status, happiness will be generated when one's income is higher than that of his counterpart. At the same time, people will not compare themselves with those with a wide income gap, because these people are a social minority and their huge wealth is composed of many factors, which is not achieved through their own efforts, so the resulting gap has little impact on happiness.

As human beings are social animals, the welfare brought by social progress can benefit all human beings. That is to say, when the income of social members increases generally, the impact of absolute income on subjective well-being is weaker than that of relative income due to the influence of comparison psychology.

3.3. The Marginal Effect of Income

Marginal effect refers to the diminishing utility of each additional unit of goods or services consumed by consumers. This paper replaces the utility of goods or services with the utility of income. Generally, with the increase of income, its utility will also increase, but the marginal utility of income will decrease. When a certain inflection point occurs, the increase of income may not bring about the increase of utility.

For families with low Engel's coefficient, when the physiological and security needs of family members are met and the material desire is saturated, the increase of income cannot significantly improve the sense of happiness. On the contrary, the physical and mental pressure brought by high income will reduce happiness. For families with higher Engel's coefficient, the improvement of income can significantly improve their quality of life and their sense of happiness. Therefore, the national income distribution reform has become an important means to affect the overall well-being of the country's residents.

3.4. Income Adaptability

Income adaptability means that people will adapt to the growth of income, that is, long-term income rise will not significantly affect the overall happiness. Since China's reform and opening-up, its economy has developed rapidly, and its material life is extremely rich. The increase in income has temporarily improved the happiness of residents who need to solve the problem of food and clothing. However, with the steady development of economy, people have developed adaptability to income. High consumption and enjoyment have become the norm. The increase of income cannot improve happiness as it did at the beginning. Therefore, the growth of happiness needs new stimulus points.

At the same time, due to the ratchet effect (people's consumption habits are irreversible, which means that it is easier to increase consumption rather than decline), the decline of income level will lead to a decrease in consumption. However, people's consumption habits are difficult to change in the short term, and they are not adapted to the lower consumption level. The gap between past and present consumption caused by income will lead to a great sense of imbalance. If the income is still difficult to recover to the original level after hard work, It will also cause a sense of frustration and loss, thus reducing happiness.

4. Suggestions for Improving Happiness

4.1. National Aspects

As China is still among the developing countries, sustained economic growth is still the top priority of development and reform. As mentioned above, for families with weak economic foundation, the improvement of income is particularly significant to the improvement of happiness. Therefore, increasing the per capita disposable income, optimizing the national income distribution policy, narrowing the income gap and reducing the national Gini coefficient have also become the key to improving the overall happiness of the country. At the same time, the country needs to work hard to stabilize prices, reduce inflation, avoid major economic fluctuations, and enhance residents' confidence in economic development.

4.2. Personal Aspects

Individuals should learn to reasonably control their desires. According to Samuelson's happiness equation, reducing their desires can improve their happiness under the condition of constant income. In addition, individuals should establish a correct concept of happiness, recognize the inequality between income and happiness, and increase their own happiness in different ways, rather than just regard income as the whole of happiness. Finally, individuals need to find correct and reasonable life goals, establish correct values, meet their social and respect needs while achieving income growth, and realize their life values.

References

[1] Sun Jiling, Hu Ronghua. Income Level, Consumption Pressure and Happiness [J]. Finance and Trade Research, 2017, 28 (02): 1-8.(In Chinese)

[2] Wu Limin, Chen Huixiong. Construction of Structural Equation Model of Income and Happiness Index -- Taking Small Towns in Zhejiang Province as an Example [J]. China Rural Economy, 2010 (11): 63-74.(In Chinese)

[3] Zhou Yi. Research on The Difference of Income and Happiness of Different Occupational Groups [D]. Zhejiang: Zhejiang University of Finance and Economics, 2015.(In Chinese)

[4] Li Qingqing Economic Analysis of the Correlation between Income and Well being [D]. Guangdong: Jinan University, 2011.(In Chinese)