Economics is undergoing a remarkable new development, which may even be called revolutionary. This development is likely to change economics substantially in the future. Our discipline has, at the same time, a conservative bias, due to its well-established body of knowledge. To this day, the core of economics is universal; the same principles of economics are taught everywhere in the world. This enables scholars to communicate easily. But an unfortunate consequence of this enshrined knowledge is that it is difficult to introduce new ideas not in line with received theory.

Happiness research is, to some extent, an exception. Its findings are slowly being taken into account in standard economics. Indeed, research on happiness has already become a hot topic, particularly among young economics scholars.

The economics of happiness is arguably revolutionary in three respects:

**Measurement** The measurable concept of happiness or life satisfaction allows us to proxy the concept of utility in a satisfactory way. It proposes the opposite of something that was considered a revolution in the 1930s, when Sir John Hicks, Lord Lionel Robbins, and others claimed that utility cannot and need not be measured. This was a great advance, and it opened the way to a fruitful application of microeconomics to economic issues, and more recently to issues far beyond economics. But the situation has changed dramatically since the 1930s. Psychologists have taught us how to measure happiness and thus to fill the concept of utility with life. Although these measures are certainly not ideal, they can usefully be applied to economic, political, and social problems. At the same time, the ways of measuring experienced utility are continually being improved.
Approximating experienced utility by using measures of subjective well-being allows us to extend economic theory into new areas. In particular, it enables us to analyze errors in decision making. Standard economic theory equates the utility expected when deciding between consumption bundles with the utility experienced when consuming them. Individuals always maximize their utility and only make errors in a random way. In contrast, happiness research demonstrates that individuals tend to make systematic errors when choosing between alternatives. For example, they often mispredict the utility gained by future consumption. They overestimate the satisfaction they derive from having a higher income in the future, and they underestimate the utility gained from immaterial aspects of life, such as friendship and social relations. As a result of these errors in judgment, they find themselves less satisfied with life than they could be according to their own evaluation. Similarly, individuals’ utility is lower when they are subject to significant self-control problems, such as when they are induced to watch more television than they think they should.

Some economists have pointed out that such deviations from standard economic theory may exist, but this insight has not affected the principles of economics. Happiness research enables us not only to acknowledge these behavioral features but also to analyze them empirically. This was not possible in standard theory based on “revealed preference,” which presumes that observed behavior is the result of a utility-maximizing calculus in which individuals do not make any mistakes.

**New insights**  Happiness research teaches us how human beings value goods and services, as well as how they value social conditions. This applies, in particular, to the effects of income, unemployment, and other economic factors on well-being. The new insights go beyond economics to include non-material values such as the value of autonomy and social relations in the family and beyond.

Happiness research suggests that individual evaluations are much broader than those enshrined in standard economic theory. Most importantly, it shows that individuals derive utility not only from income (as is implied in much of received theory) but also from highly valued social relations and from self-determination, as well as using their own competence. Moreover, individuals derive utility from processes, not just from outcomes.

**Policy consequences**  Happiness research suggests many policies that deviate significantly from those derived in standard economics. With
respect to current economic policy, the research on happiness reveals that the goal of increasing income (or, at the aggregate level, growth in gross national product)—often implicitly or even explicitly assumed in received economics—is not an effective way of increasing utility in a sustainable way. Much of the initial utility increase from higher income dissipates rather quickly. Individuals adapt quite rapidly to higher income, and that leads to higher income aspiration. They also tend to compare themselves with others. Therefore, people do not evaluate income in absolute terms, but rather in relative terms.

Happiness research emphasizes the importance of employment and leisure for individual well-being much more than standard economics does. Moreover, it explicitly takes into account the genetic, sociodemographic, cultural, and political determinants of happiness. As a consequence, individuals can gain many different insights into how government policies affect the well-being of individuals. Proposals for increasing individuals’ life satisfaction include increasing leisure time by raising the minimum vacation entitlements from two weeks to four weeks a year and other specific policies, such as curbing advertising on television and reducing excessive geographical mobility. At the level of constitutional design, happiness research helps to build institutions that enable individuals to achieve their highest level of well-being. It has been suggested that extending individuals’ political participation rights and decentralizing political decision making have positive influences on life satisfaction.

This book advances the idea that a revolution in economics is under way by substantiating the three claims that have been made. Considerable emphasis is placed on going beyond purely theoretical conjectures and providing empirical evidence.

Part I traces the major developments in economic happiness research: Why is its study worthwhile? What is the relationship to utility as used in standard economic theory? It is demonstrated that we have gained major new insights into how income, unemployment, inflation, and income distribution affect human well-being.

Part II pushes the field ahead by looking at topics that so far have been neglected or have been studied in a much different way. Among the topics treated are democracy and federalism, self-employment and voluntary work, and watching television (one of the major activities of modern man). Moreover, it is shown how the concept of utility can be given life by considering procedural utility (beyond the outcome utility
used in standard economics), the tendency of individuals to mispredict future utility of various types of consumption (the utility is sometimes overpredicted and sometimes underpredicted), and a new approach to empirically measuring the value of public goods (as a complement to the traditional willingness-to-pay approaches).

Part III deals with the policy consequences of happiness research. The media and the “positive psychology” movement have drawn on these insights. However, care must be taken not to fall prey to a “benevolent dictator” approach of telling individuals how to reach happiness, or forcing them to take the corresponding actions. Rather, governments should only provide the conditions that allow people to become and remain happy. A crucial role is played by adequate political institutions, particularly decentralized public decision making and a right to direct political participation.

The final chapter concludes that economic happiness research is revolutionary. Though much has been achieved, the field is wide open for future research.

This book does not survey happiness research; that has been done elsewhere. Nor is it possible to give a full account of the revolution we are witnessing. It is too early for that, and the participants are too engaged in the topic to be objective enough. Rather, the book demonstrates what can be achieved by the happiness research undertaken in economics.

The book is, to a significant extent, based on the work of the research group connected to my chair at the Institute for Empirical Research in Economics at the University of Zurich. It is therefore appropriate that the members of the group are listed as co-authors. I was a joint author of all but one of the papers on which the book is based. The following features characterize the work of the Zurich Group:

- It is highly interdisciplinary. In particular, many insights from psychology have been introduced. But political science and sociology also play substantial roles.
- Its members are willing to depart from standard economics if they find the departure useful.
- The work is empirical in orientation. Although theory is important, it is not enough.
- The members are prepared to draw policy conclusions, even when the evidence (as will always be the case) is only preliminary.

Leading the Zurich Group has been an extraordinarily exciting experience. I am particularly grateful to my long-time co-worker Alois
Stutzer, a master of applied empirical work in happiness research. He was kind enough to go through the whole manuscript. But I alone am responsible for any errors.

Parts of this book have been presented at many conferences and lectures around the world. The main ideas were developed in connection with the lecture given on the occasion of my being appointed Distinguished Fellow of 2005 by CESifo at the University of Munich. I benefited greatly from the discussions at an interdisciplinary conference on happiness held at Schwarzenberg, Austria, under the sponsorship of the Progress Foundation.

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