



24th November 2008

The politics of NAV

“When you’re young it’s fantastically important what sort of car you’re seen to be driving..

“Take your BMW, Alex.. it isn’t simply a means of transport, it’s a symbol of your position in society, your manhood..

“But when you get to my age and position, things like that appear silly and trifling; a car really ceases to have value as a status symbol..

“That’s why I got the helicopter.”

- Rupert to Alex, in ‘Alex’, by Charles Peattie and Russell Taylor.

Trust economists to suck all the life out of a fascinating debate and reduce it to data. In 1974, Richard Easterlin asked whether economic growth improved human happiness. He found, unsurprisingly, that within individual countries, those with higher incomes were more likely to claim to be happy. Intriguingly, however, when it came to making comparative international analysis, average reported happiness saw little variation relative to national income. And although per capita income within the US rose steadily between 1946 and 1970, average happiness showed no longer term trend.

Ruut Veenhoven and Michael Hagerty, in 2003, challenged the Easterlin paradox, indicating that countries did indeed get happier as they got wealthier. And earlier this year, Justin Wolfers and Betsey Stevenson of the University of Pennsylvania [re-examined](#) the Easterlin paradox, and also concluded that increases in income tended to match increases in subjective happiness. Their findings, in summary:

- 1) Rich people are happier than poor people.
- 2) Richer countries are happier than poorer countries.
- 3) As countries get richer, they tend to get happier.

So far, so blindingly obvious. But irrespective of whether Easterlin’s original thesis was correct or not, we seem to have sleepwalked our way into a culture that takes constant growth in GDP as an inalienable human right alongside life, liberty and the pursuit of happiness. As Warwick University economist Andrew Oswald suggested in an interview two years ago,

“If you’re poor, and can’t feed your children, theories about the economics of happiness don’t matter. But in America and western Europe, a lot of us don’t need a TV wider than the one we have, or a third car. We’re still stuck with thinking that applied in 1945, when we needed

economic growth to supply us with basic things. Today, the case for growth remains much stronger in developing countries..”

On a related theme, it has become unchallengeable accepted wisdom that a little inflation (and not too much) has to be a wonderful thing. This is a little like saying that the authorities will operate a policy of carefully managed debauchery of our savings. The Bank of England currently targets an inflation rate of 2%. We can put to one side the degree of manipulation, hedonic or otherwise, inflicted upon that target rate by the west’s central banks.

Perhaps economists should study the bathroom habits of bears in woods next

Measuring Satisfaction

A new study shows that people in wealthier countries are more likely to be satisfied with their lives. Earlier research had suggested that satisfaction did not necessarily increase once basic needs were met.

Percent who rate themselves an 8, 9 or 10 on a 10-point scale of satisfaction



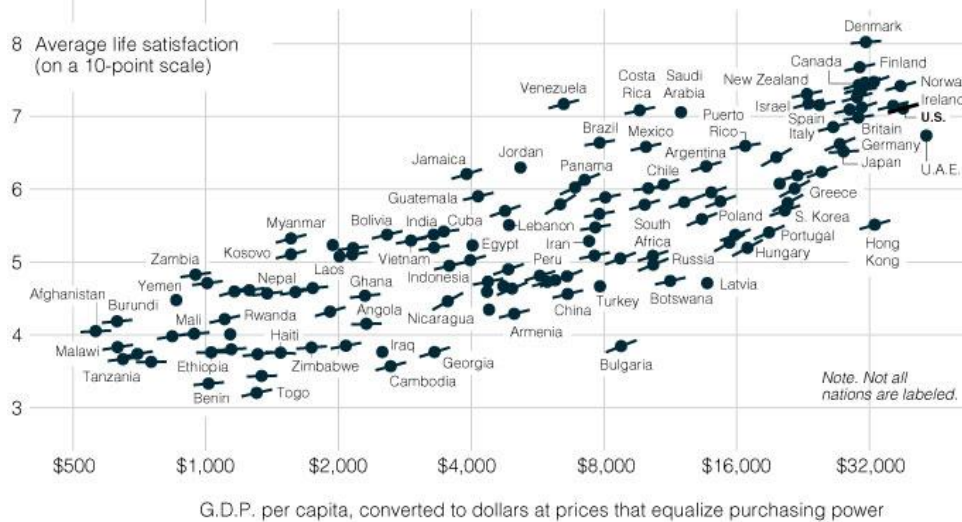
KEY:

● Each dot represents one country

The line around the dot shows how satisfaction relates to income within that country:

— Higher-income people are more satisfied

— Higher-income and lower-income people are equally satisfied



Source: Betsey Stevenson and Justin Wolfers, Wharton School at the University of Pennsylvania

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So it is now doubly unfortunate – for the [politicians](#), let alone the real economy – that both the GDP growth genie and the low inflation genie have apparently been let out of the bottle and to all intents and purposes have vanished altogether. It was Ronald Reagan who said that the nine most dangerous words in the English language were “I’m from the government and I’m here to help”. So government “help” (read: taxpayers’ capital) is now working on behalf of the banking system, notwithstanding grisly moral hazard issues, and will soon be working for an indeterminate number of other “special interest” groups that have apparently given up on the free market ideal and are reverting to crisis socialism.

A year ago, Slate’s Daniel Gross published his book “Pop !” (HarperCollins 2007) which argued, somewhat counter-intuitively, “Why bubbles are great for the economy”. Gross suggested that a predisposition toward colossal bubbles was “another brief in the case for American Exceptionalism, the notion that the United States has traced a unique path of social, economic,

political and cultural development.. The United States wasn't plagued by the socialism, fascism, or violent revolutions that ravaged the Old World.. precisely because it had no history of feudalism against which the masses could revolt." Gross also cited psychologist John Gartner's "The Hypomaniac Edge" (Simon & Schuster, 2005) which argues that a neurotic tendency on the part of entrepreneurs is a fundamental aspect of the American character, such that bubbles are reflections of what Gross calls "episodic outbursts of American entrepreneurial id". And while the US government, through the mechanism of tax credits, patent policies, procurement and legislation, the tax code and direct subsidies has helped incubate and then sustain economic booms deriving from rapid innovation, it has on the whole allowed free marketeers to get on with the business of risking, making and losing vast amounts of capital. Europe, by way of contrast, has invariably allowed heavy government intervention to smooth over the economic blips and bumps triggered by investor mania, in turn moderating the opportunity for Europeans to generate immense wealth out of disruptive technologies.

But the supposed boom triggered by the growth of credit was a false boom. Rising property prices do not equate to true wealth creation. And as we now know to our cost, the profits associated with new credit products were largely illusory. Ominously, Gross suggested in "Pop !" that US financial hegemony was built on the infrastructure of "a sound banking system, transparent and lightly regulated capital markets, and a robust home lending system." In which case, US (and for that matter Anglo-Saxon) financial hegemony is over – an observation reinforced by the National Intelligence Council analysis "Global Trends 2025" which pointed to a long-term decline in US economic and political heft.

It was always absurdly foolish of Gordon Brown, or any other politician, to claim a premature or indeed any kind of victory over 'boom and bust' – to believe that bureaucrats, rather than markets, are the best allocators of economic capital, or that the business cycle had been vanquished. It remains foolish to believe that unthinkingly pounding that GDP treadmill and hurling any amount of both current and future taxpayers' money at failed industries will soften the damage and the crisis rather than extend them. Whereas the telegraph, railroad and internet bubbles left lasting value in their wake, there are no obvious signs of prospective benefit in the rubble of the credit boom – other than the forced shrinkage of an overbanked financial system.

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