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Do private and public transfers received affect life satisfaction? Evidence from Romania

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ABSTRACT

This paper uses Romanian survey data to investigate the determinants of individual life and financial satisfaction, with an emphasis on the role of public and private transfers received. A possible concern is that these transfers are unlikely to be exogenous to satisfaction. We use recursive simultaneous equations models to account both for this potential problem and for the fact that public transfers are themselves endogenous in the private transfer equation. We find that public transfers received have a positive influence on both life and financial satisfaction, while private transfers do not matter. People receive private transfers irrespective of their economic and demographic characteristics in Romania, which could be explained by some social norm motives.

1. Introduction

As expressed by Smith (1776) and as introductory textbooks in economics teach us, *"it is not from the benevolence of the butcher, the brewer, or the baker that we expect our dinner, but from their regard to their own interest."* The homo economicus is expected to behave as a rational and self-interested actor who desires wealth, meaning that more income should be associated with a higher level of life satisfaction in general, and of financial satisfaction in particular. In this paper, we focus on the specific effect of different income components on self-reported measures of well-being and study whether public and private transfers influence individual life and financial satisfaction.

Romania offers an interesting scenario in this context. The political crisis during Ceausescu, followed by the dramatic collapse of the economy during the first years of transition, made Romania face a severe increase in poverty.[1] Public transfers were for many years chronically under-funded during Communism, and the first years of transition found them in a rapid

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[1] On average, Romania experienced a negative growth rate from 1990 to 2002, as opposed to other transition countries within the region (World Bank, 2003).

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process of disintegration. Also, while formal transfers are very limited, several authors have pointed to the importance of private transfers for the Romanian people (Amelina, Chiribuca, & Knack, 2004; Mitrut & Nordblom, 2010).

During the last two decades, economists have devoted a lot of attention to the determinants of subjective well-being (see van Praag & Ferrer-i-Carbonell, 2008; Dolan, Peasgood, & White, 2008). By focusing on the impact of public and private transfers on life and financial satisfaction, our contribution is closely linked to two lines of research.

The first one is about the determinants of life satisfaction.[2] While psychologists have long been interested in understanding human life satisfaction (Diener, Suh, Lucas, & Smith, 1999), the economists' interest in this topic started with the work of Easterlin (1974), Easterlin (1995).[3] Looking at the effect of income on happiness, he stated the "paradox" of the increased real growth in Western countries during the last fifty years, without any corresponding increase in the reported levels of happiness. Some studies show that absolute income matters (Oswald, 1997), while Blanchflower and Oswald (2004) find support for the fact that both relative and absolute income matter. At the same time, there is a growing literature focusing on some other aspects closely linked to self-reported well-being, like the effect of unemployment, marriage, children, and health status on overall life satisfaction. Some other studies have focused on the role of democratic institutions and social norms on individual well-being (Frey & Stutzer, 2002; Stutzer & Lalive, 2004).

The second strand of research closely linked to the present study is the literature on private transfers among households (see Laferrère & Wolff, 2006). In the earliest papers on this topic, inter-household transfers were assumed to be altruistically motivated, implying a crowding-out effect of the private contributions by government transfers (Barro, 1974; Becker, 1974). Some authors have instead considered that transfers could be explained by self-interest concerns. Cox (1987), Cox (1990) suggests that financial transfers to children are made in exchange for services received from them or have to be reimbursed later. Private transfers may also allow households to share risk within networks of family and friends through mutual insurance (Fafchamps & Lund, 2003; Foster & Rosenzweig, 2001).

Theoretically, there are many ways in which public and private transfers may affect life satisfaction. The obvious and presumably most important channel is a pure income effect. Since receiving transfers increases household resources, this should in turn increase both happiness and financial satisfaction. However, several other explanations may come to mind. For instance, the different income sources may reflect different degrees of permanent versus transitory income, which would be expected to affect life satisfaction differently.[4] Also, receipt of private transfers could pick up aspects of life satisfaction that come directly from having friends or people to socialize with, while public transfer income may be associated with a stigma. At the same time, people may feel less satisfaction from public transfers because they feel they are entitled to them because they paid into the system.

In this paper, we study whether public and private transfers have an influence on both subjective well-being and financial satisfaction, but do not investigate the channels that lead to public and private transfers having a potentially different effect than other income. As private transfers are very common in Romania, one would expect them to have an influence on satisfaction. Curiously, the link between private inter-household transfers and life satisfaction has not been studied before.[5] Our contribution is thus twofold. First, as Andrén and Martinsson (2006), we bring evidence on the determinants of happiness in Romania, but with a focus on the role of public and private transfers received. Secondly, we investigate the interplay between these two types of transfers and the possibility of a crowding-out effect.[6]

We rely on an unusually rich Romanian household survey to study the determinants of life and financial satisfaction. With respect to the main determinants of happiness such as income and working status, our results are in line with other findings in the literature. When disentangling the impact of the different income components, we find that both non-transfer income and public transfers have a positive and significant impact on life and financial satisfaction, while income from private transfers does not seem to matter. Our results hold when taking into account the endogeneity of both private and public transfers in the life and financial satisfaction regressions and of public transfers in the private transfer regression. Furthermore, people receive private transfers irrespective of their economic and demographic characteristics and respondents who benefit from more public transfers receive less private transfers, but the crowding out effect remains incomplete.

The rest of the paper is organized as follows. Section 2 briefly describes the Romanian context. We present the data in Section 3, while the main determinants of life and financial satisfaction in Romania are investigated in Section 4. In Section 5 we account for the potential endogeneity of private and public transfers received on satisfaction. Finally, Section 6 concludes the paper.

[2] In this paper, we use the terms happiness, life satisfaction, and individual (self-reported) well-being interchangeably. Several papers have shown that these measures are highly correlated.

[3] Actually, income satisfaction evaluation based on subjective income-satisfaction questions was pioneered by van Praag (1971) and the so-called Leyden School.

[4] Public transfer income may represent permanent income (for instance a pension received until death), which could increase happiness, whereas some component of non-transfer or private transfer income may be transitory, with an unclear effect on happiness.

[5] Meier and Stutzer (2008) analyze how volunteer work influences happiness in Germany. Also, Bruhin and Winkelmann (2009) and Wolff (2006) use questions on the subjective well-being of parents and children to study the existence of altruism between these two generations, but they do not take transfers (either private or public) into consideration in their empirical analyses.

[6] There are few empirical studies on the relevance of a crowding-out effect between private and public transfers. Cox and Jakubson (1995), Maitra and Ray (2003), and Jensen (2004) are interesting exceptions.