Journal of Economic Psychology 33 (2012) 940–950

Contents lists available at SciVerse ScienceDirect

Journal of Economic Psychology

journal homepage: www.elsevier.com/locate/joep

Subjective well-being and relative poverty in rural Bangladesh

Mohammad Niaz Asadullah [a,b,c,d,*], Nazmul Chaudhury [e]

[a] School of Economics, University of Reading, UK
[b] ESRC Centre on Skills, Knowledge and Organisational Performance (SKOPE), Oxford University, UK
[c] IZA, University of Bonn, Germany
[d] Research and Evaluation Division (RED), Bangladesh Rural Advancement Committee (BRAC), Bangladesh
[e] The World Bank, Bangladesh

ARTICLE INFO

Article history:
Received 6 February 2012
Received in revised form 4 April 2012
Accepted 12 May 2012
Available online 18 May 2012

JEL classification:
O12
I30
I31

Keywords:
Poverty
Well-being
Institutions
Bangladesh

ABSTRACT

This paper revisits the debate over the importance of absolute vs. relative income as a correlate of subjective well-being using data from Bangladesh, one of the poorest countries in the world with high levels of corruption and poor governance. We do so by combining household data with population census and village survey records. Our results show that conditional on own household income, respondents report higher satisfaction levels when they experience an increase in their income over the past years. More importantly, individuals who report their income to be lower than their neighbours in the village also report less satisfaction with life. At the same time, our evidence suggests that relative wealth effect is stronger for the rich. Similarly, in villages with higher inequality, individuals report less satisfaction with life. However, when compared to the effect of absolute income, these effects (i.e. relative income and local inequality) are modest. Amongst other factors, we study the influence of institutional quality. Institutional quality, measured in terms of confidence in police, matters for well-being: it enters with a positive and significant coefficient in the well-being function.

1. Introduction

Of late, there has been a spate of economic investigations on the determinants of subjective life-satisfaction. Arguing that life-satisfaction scores provide a measure of true utility,[1] findings of these studies have been used to highlight both economic and non-economic aspects of individual well-being. Evidence suggests that relative to income, influence of other factors is either of equal or even greater importance. This is a promising line of inquiry in the context of the existing debate on the multidimensionality of poverty. Life-satisfaction research, by way of jointly studying the role of institutions, belief system, income and, economic inequality and so on, provides a convenient way to compare and contrast economic and non-economic factors in determining individual well-being. If well-being cannot be defined in the commodity space, the influence of income vis-à-vis

* Corresponding author. Address: School of Economics, University of Reading, Whiteknight, Reading, RG6 6UD, UK. Tel.: +44 008801746614623.
E-mail address: m.asadullah@reading.ac.uk (M.N. Asadullah).

[1] There is a wide-acceptance of the use of subjective data today. Although economists have traditionally focused on revealed preferences, analysis of self9-reported wellbeing measures reveals that (a) well-being equations are broadly "similar" across countries suggesting that the data does not just contain noise; (b) answers to life satisfaction questions are clearly correlated with a number of observable phenomena that are true indicators of wellbeing such as the risk of coronary heart disease, hypertension, stress, depression, anxiety, pain, blood-pressure measures (Blanchflower & Oswald, 2008); (c) suicide rate (which is based on behaviour rather than subjective opinions and arguably a true measure of utility) also predicts life-satisfaction (Helliwell, 2004). This suggests that even if happiness scores measure true internal utility with some noise, the signal-to-noise ratio is sufficiently high to make empirical research productive (Di Tella & MacCulloch, 2006).

0167-4870/$ - see front matter © 2012 Elsevier B.V. All rights reserved.
http://dx.doi.org/10.1016/j.joep.2012.05.003

that of non-income variables should be modest. To this end, research using developed country data finds that non-income related factors matter as well. Well-being is lower in countries where inflation is high, institutions are of poor quality (Helliwell, 2003, 2006) and, inequality is high (Alesina, Di Tella, & MacCulloch, 2004).[2] Cross-country analysis on the correlates of well-being reveals that even after holding income constant, difference in happiness is explained by unemployment level in the economy (Clark & Oswald, 1994) and level of trust in the society (Helliwell & Putnam, 2004; Helliwell and Huang, 2009; Helliwell & Wang, 2011).

Using four rounds of World Values Survey data spanning 75 countries, Helliwell (2003) finds that income effect is dominated by government quality. Another notable aspect of this study is the finding that for different stages of development, different type of government institutions is relevant. Honest governments are more important in low income countries whilst political stability is more relevant for developed countries. Second, the effect of institutional quality is found to dominate that of GDP. Lastly, well-being gains from better institutions are larger amongst the poor (because they suffer most from corruption).

In parallel to the cross-country studies, there exists a large body of literature which employs country-specific micro datasets. This research finds sizable reference group effects. For the US, it is found that relative income not only affects well-being positively, change in welfare owing to increase in mean income in residential locality is equal to fall in personal income (Luttmer, 2005). Similarly, Helliwell and Huang (2009) find that family/personal income and mean income in census tract equally affect well-being in Canada.[3] Similarly, using Danish data Clark, Kristensen, and Westergård-Nielsen (2009) find that conditional on own household income, respondents report higher satisfaction levels when their neighbours are richer. The finding that relative instead of absolute income has a stronger effect as a correlate of well-being has important policy implication: if the poor cares about their relative position in the income distribution, policies that aim to raise their welfare has to additionally address the issue of economic inequality.

This paper builds on the existing developed country studies and contributes to the small but growing developing country literature on subjective well-being using a new household survey dataset from rural Bangladesh that spans 96 villages. In particular, we follow Helliwell (2003) and combine individual and aggregate (i.e. community) level variables to explain well-being. Respondents in our survey were asked, among other things, the following question (which they answered on a scale of 1–10): *"On the whole, how satisfied are you with your life?"* We use this subjective assessment of life-satisfaction or happiness[4] as a proxy measure of "utility"[5] and estimate well-being function focusing on a number of correlates: relative wealth, institutional quality, and social trust. The key hypotheses tested are: (a) Is the effect of absolute income bigger than relative income? (b) Is the relative income effect only specific to the non-poor? (c) How does the income effect compare with that of institutional quality, social trust and economic inequality in the village?

Rest of the paper is organized as follows. Section 2 discusses studies on subjective well-being using developing country data. Section 3 discusses the data and the main hypotheses. Section 4 discusses the methodology. Section 5 presents the main results. Section 6 is conclusion.

2. Literature review: subjective well-being in low income countries

Inspired by the evidence for developed countries, researchers have started to estimate well-being equations using developing country data. Using Malawian data, Ravallion and Lokshin (2010) report that subjective well-being is negatively correlated with mean income in one's neighbourhood but this is true only for the non-poor (i.e. individuals in the upper income category). Needs in developing societies are somewhat basic in nature so that a priori, income deprivation seems to be the correct yardstick to focus on from policy point of view. However, more recent research using Nepalese data contradicts Ravallion and Lokshin. For instance, Fafchamps and Shilpi (2009) find that relative consumption is an important predictor of subjective welfare even in mountainous villages of Nepal where households remain isolated from the influence of modernity.[6] In another related study on South Africa, Kingdon and Knight (2007) also report some evidence of relative income effect: subjective well-being is found to increase with average income in the district.[7] On the other hand, descriptive evidence of reference group consumption effect reported by Guillen-Royo (2011) for Peru suggests that neighbours are 'negatives'. Similarly, using Indian data Carlsson, Gupta, and Johansson-Stenman (2009) find that majority of the marginal utility of income comes

[2] Alesina et al. find that wage inequality depresses reported happiness in a region in both US and Europe.

[3] Similar reference group effect is also reported for other correlate of welfare: Clark (2003) finds that an unemployed person's wellbeing is positively correlated with regional/household unemployment.

[4] We treat the terms "life satisfaction" and happiness interchangeably.

[5] The measurement of subjective well-being confounds inter-personal comparisons of welfare using subjective data (Kahneman & Krueger, 2006). For instance, a methodological problem is that life satisfaction score assumes cardinality whilst satisfaction scores are not necessarily homogenous across individuals. Whilst recent evidence confirms the latter point, at the same time it is pointed out that this issue does not cause bias in the analysis of self-reported well-being data. Beegle, Himelein, and Ravallion (2009) use vignettes to test for heterogeneity in satisfaction score scales and evaluate its effect on happiness scores for Tajikistan. Beegle et al. confirm the presence of individual-specific scales or standards when assessing well-being. But the authors find little bias in the identification of correlates of life satisfaction when vignette responses are included as control variables in standard well-being regressions.

[6] Therefore, for these villages, the correlation between relative consumption and subjective wellbeing cannot be attributed to the possibility that relative comparisons are exacerbated by urban influence and exposure to market activities.

[7] Kingdon and Knight find that close neighbors are 'positives' but that the income of more distant others negatively enters the well-being function. They also find that income of racially defined reference groups have a negative effect.