The Economic Value of the Quality of Life, Thomas M. Power

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THE ECONOMIC VALUE OF THE QUALITY OF LIFE

By THOMAS M. POWER
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This book represents an effort to impute an economic value to at least some components of "The Quality of Life" so that ultimately measures of economic welfare such as per capita real income could be adjusted to reflect components of economic welfare derived from sources other than market transactions. The primary focus in this book is on interurban wage differentials as reflecting compensation for differences in the quality of life across standard metropolitan statistical areas. Power's main hypothesis is that in the long run the mobility of labor among cities assures that interurban wage differentials will be equal to workers' monetary valuations of differences in the social, cultural, and environmental amenities available in each urban area. These wage differentials will make at least the marginal worker indifferent as to which city he or she chooses to work and to live in. Thus higher wages do not reflect higher welfare, but rather the monetary compensation necessary to make the worker willing to accept the lower level of urban amenities.

Power finds support for this hypothesis in regressions of average money wage rates against measures of urbanization including population and population density and in reviews of several other empirical studies of wages and city size. He concludes that as a first approximation a tenfold increase in urbanization as measured by population is associated with a 10% increase in wages to compensate for urban disamenities. Power then shows that if this empirical relationship is valid, virtually all of the lower per capita personal income in his home state of Montana may be offset by a higher quality of life associated with the smaller city size there. As a check on this conclusion, Power also makes an effort at the direct measurement of the economic value of lower crime, more recreation opportunities, lower air pollution, and reduced congestion in Montana. These estimates require imputations of unit values for which there is very little empirical foundation. The results of this analysis are carefully qualified. But Power finds tentative support for the conclusion that lower wages in Montana measure the higher quality of life there.

Power draws several conclusions from his theoretical and empirical analysis. First, if labor and capital are mobile among regions, no one region can be substantially better off in the nation as a whole without inducing capital and labor flows to that region which will reduce both the quality of life and money incomes there. Second, a region's lower per capita income is not necessarily a sign of lower per capita welfare. And finally, regional economic growth may be self defeating in the sense that in the long run money income gains will do no more than compensate for reductions in the quality of life.

Since as his own references make clear, Power is not the first to suggest that interurban wage differentials might arise to compensate for differences in some aspect of quality of life, a reviewer must ask what has Power added to our understanding of the nature of the wage/quality relationship and its implications for economic and social policy. His discussion of his conclusions and policy implications is interesting and provocative. It represents a challenge to the conventional "Chamber of Commerce" pro-regional growth point of view without being totally anti-growth. This part of the book deserves to be read by regional economists and policy makers. But on the other side of the ledger, it must be said that the body of empirical evidence is not conclusive with respect to his basic hypothesis. The empirical task he and others have undertaken is basically the estimation of a hedonic wage function. Yet there is no reference to the literature on hedonic price estimation. This literature has much guidance to offer concerning problems of model specification, functional form, and the choice of explanatory variables. This is perhaps not the place to enter into a technical discussion of theoretical and empirical aspects of the estimation of hedonic wage functions. But the reader interested in pursuing these points could consult Meyer and Leone[1] on measurement problems and the results of including a wider range of urban quality variables, and Rosen,[2] Lucas[3] and Freeman[4] for discussions of the hedonic price theory and its application to labor markets.

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1. *See* Meyer & Leone, *The Urban Disamenity Revisited,* in PUBLIC ECONOMICS AND THE QUALITY OF LIFE 66 (L. Wingo & A. Evans, eds. 1978).

2. Rosen, *Hedonic Prices and Implicit Markets: Product Differentiation in Pure Competition,* 82 J. of POL. ECON. 34 (1974).

3. Lucas, *Hedonic Wage Equations and Psychic Wages in the Returns to Schooling,* 67 AM. ECON. REV. 549 (1977).

4. Freeman, *The Hedonic Price Technique and the Value of Climate as a Resource* (paper presented at Workshop on the Economic Impact of Climate Change, Ft. Lauderdale, Florida, April 24-25, 1980).