

Abstract

Economic Freedom and Eudaimonic Well-Being: Exploring the Socio-Economic Paths to Psychological Functioning

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It is well established that economic freedom promotes economic development and social progress. However, economic freedom can also promote income inequality that can stifle economic mobility and harm citizens. While previous studies have examined the relationship between economic freedom and hedonic well-being (life satisfaction and affect), this paper explores how economic freedom affects people's personal and social psychological functioning (flourishing) defined as one's resilience, autonomy and control, mastery and engagement, environmental mastery, positive relationships, and self-acceptance. To do this, I plot the mean score for each country's economic freedom against their mean score for social and personal psychological functioning. In addition, using structural equation modelling, I explore the socio-economic paths from economic freedom to psychological functioning via the channels of economic development, income inequality, unemployment, inflation, democracy and individualism. The results indicate that economic freedom is positively correlated with both personal and social functioning. Overall, these results suggest that perceived problems with economic freedom do not outweigh its well-being benefits.

Keywords

Economic Freedom, Well-being, Personal Functioning, Social Functioning, Human Flourishing, Structural Equation Modelling

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ECONOMIC FREEDOM AND EUDAIMONIC WELL-BEING: EXPLORING
THE SOCIO-ECONOMIC PATHS TO PSYCHOLOGICAL FUNCTIONING

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TABLE OF CONTENTS

| | |
|---------------------------------------|----|
| Chapter One: Introduction | 3 |
| Chapter Two: Theoretical Foundations | 6 |
| Chapter Three: Hypothesis Development | 13 |
| Chapter Four: Data & Methods | 20 |
| Chapter Five: Results | 23 |
| Chapter Six: Discussion & Conclusion | 30 |
| Works Cited | 32 |

CHAPTER 1

Introduction

Throughout history, different political regimes have emphasized the social benefits of various economic systems. More capitalistic societies, for example, promote greater personal, political, and economic freedom. Socialistic societies, on the other hand, focus on creating more equal economic outcomes, which often comes at the expense of personal and economic freedom. In other words, a key problem that any economic system tries to solve is how to distribute political and economic power, and whether decision making should be centralized or individuals given more freedom. It is by now well-established that countries with a high degree of economic freedom are more likely to have higher levels of economic development and social progress. For example, people who live in more economically free countries are more likely to have higher incomes, better material standard of living, better career opportunities, face less discrimination, higher levels of health, and experience overall happier lives (Hall & Lawson, 2014; Nikolaev, 2014; Bennett et al., 2016). Despite this evidence, however, economic freedom may also lead to higher levels of income inequality that can stifle economic mobility and be detrimental to the well-being of its citizens (Pickett and Wilkinson, 2015). Furthermore, some claim human irrationality means strong central governments are the best way to organize markets (Akerlof & Shiller, 2010). On the other hand, there is no evidence that people are more rational as voters than they are as consumers, nor is there evidence that policy makers are any more rational than the average citizen (Niskanen 1971).

Theoretically, the aim of all public policy is to allow citizens to live a fully flourishing and fulfilling life. In this respect, well-being must be studied in order to determine the opportunity cost of economic freedom (Stroup 2007). Although it can be difficult to empirically study an abstract concept such as well-being, several measures of well-being have been developed. Scholars have debated what really constitutes a “good life” for centuries, but recent empirical advances in psychology have made analyzing this question more practical (Ryan & Deci, 2000; Seligman, 2012; Ryff, 2014, Diener 1984).

Several prevailing measures of well-being exist: subjective well-being, evaluative well-being, and psychological functioning. Hedonic well-being measures the presence of positive affect and negative affect and evaluative well-being is a cognitive assessment of one’s life quality (Diener 1984). Some psychologists, however, argue that positive affect and life satisfaction are not sufficient measures of well-being (Ryff, 2014; Ryan and Deci, 2000). In contrast to this more hedonic approach to well-being, the contrast of eudaimonic well-being captures overlooked areas of psychological functioning such as authenticity, meaning, excellence, and growth. Eudaimonic well-being in modern psychology is measured by psychological functioning which highlights self-acceptance, personal growth, purpose in life, environmental mastery, autonomy, and positive relations with others (Ryff, 2013).

While previous studies have explored the effect of economic freedom on hedonic and evaluative well-being (Nikolaev and Bennett, 2017; Rode, 2013; Gehring 2012), this study investigates how economic freedom relates to eudaimonic well-being (psychological functioning). Data on economic freedom were collected from the Fraser Institute’s Economic Freedom of the World Report, and data on psychological functioning came from the European Social Survey

(ESS). The empirical analysis was based on multiple methods. Specifically, I used bi-variate correlation plots, multivariate regression models, and structural equation modelling to estimate the marginal effects of economic freedom on personal and social psychological functioning. Overall, the results indicate that economic freedom is significantly positively correlated with both personal and social functioning. In addition, I find that the economic freedom is correlated with personal functioning through its positive correlation on economic development, but also through its negative effect on inflation, unemployment, and income inequality. Overall, these results suggest that perceived problems with economic freedom do not outweigh its well-being benefits.

The paper is organized as follows: First, I provide overview of the basic theoretical constructs used in the study (e.g., economic freedom, psychological functioning, etc.). Second, I introduce the main theoretical framework and then develop the hypotheses. Third, I describe the data sources and methods used to test the hypotheses. Finally, I summarize the results and discuss their implications.

CHAPTER TWO

Theoretical Foundations

Well-being

An emerging literature has established the relevance of economic institutions such as competitive markets and the banking system to economic growth and prosperity (Lawson & Hall, 2008; Bennett et al., 2016). For example, people who live in countries with institutions consistent with the principles of economic freedom are more likely to earn higher incomes, face less unemployment, have more job opportunities, experience less discrimination, and generally, enjoy better material standard of living (Lawson & Hall, 2008; Nikolaev, 2013).

Well-being, however, is a multi-dimensional construct that reflects not only material standard of living, but also variety of psychological states such as the experience of vitality, autonomy, purpose, self-esteem, optimism, and life satisfaction, to mention a few. Many of these psychological states (e.g., life satisfaction) are strongly correlated with economic development (Sacks et al., 2010), but there are also striking discrepancies, especially when it comes to people's own perceptions of how well their lives are going (Stiglitz et al., 2008).

In recent years, various initiatives around the world have been launched in order to provide a more comprehensive view of socio-economic progress. In 2016, for example, the OECD pledged to “redefine the growth narrative to put people's well-being at the center of government efforts.” (OECD 2016). These developments show a profound shift in thinking about the measurement of socio-economic progress and challenge conventional methods of gauging

prosperity that largely rely on objective measures of personal and national income and production.

Aristotle

The history of science behind measuring well-being is complex and highly contested even today. Scholars from a wide range of disciplines have undertaken many different approaches to defining what it means to live a good life, even dating back to antiquity. Aristotle, for example, is credited with an early account of well-being from his discussions on eudaimonia. Eudaimonic well-being focuses on higher capacities such as virtuous action and meaningful achievement over simply searching for pleasure in life. The later view of well-being which defines well-being as the sum of all positive affect less the sum of all negative affect is now referred to as the hedonic approach to well-being. Aristotle's ethical approach to well-being essentially follows his quest to find the 'ergon' or function of the soul. He argues that in order to achieve the highest order of well-being we must practice virtue and excellence, not just engage in what provides pleasure. Etymologically, eudemonia can be split into "eu" which means "well" and "daimon" means "divinity" or "spirit". Putting them together, you get that eudaimonia means "living in a way that is well favored by God". (Kraut, 2017). For much of the 20th century well-being research was dominated by the hedonic approach (Cacioppo & Berntson 1999, Diener 1984, Deci & Ryan 2001). Only recently, have scholars reexamined well-being with eudaimonic elements in mind.

Hedonic Well-being

Hedonic well-being is focused on the difference between positive and negative affect. Positive affect is accrued through pleasure while negative affect is the result of pain. A hedonic view of well-being suggests that well-being is equal to the total of positive affect in an individual's life less the total of the individual's negative affect. If the resulting summation is positive than the person is said to be experiencing hedonic well-being where as a negative result would indicate a lack of hedonic well-being. In other words, hedonia represents feelings of pleasure and comfort or the lack thereof. Examples of feelings associated with hedonic pleasure are joy, happiness, relaxation, or painlessness. Hedonic well-being is capable of addressing very basic and simple quality of life factors. It is the most intuitive way to quantify feelings that constitute the base of happiness. Despite the intuitive nature of hedonic well-being, it is severely lacking as a comprehensive measure of well-being. Life cannot be fully captured by just accounting for pleasure and pain.

To supplement hedonic approaches, Ed Diener created the concept of subjective well-being (Diener 1984). Subjective well-being combines traditional hedonic accounts of well-being with evaluative methods which aim to introduce cognition in an effort to fill the gaps that affect cannot address. These evaluative accounts allow people to judge their lives from their own perspective as each individual considers the importance of each individual affect. Generally, evaluative accounts represent the individual's cognitive evaluation of his or her life quality. Diener asserted that subjective well-being is a "global measure" meant to consider every aspect of the individual's life in order to accurately grasp their well-being. However, despite adding the

evaluative portion, subjective well-being is still not comprehensive and ignores important components of well-being.

Eudaimonic Well-being

Aristotle differentiated between hedonic and eudaimonic accounts of well-being to highlight the distinct nature of each category. Whereas hedonic well-being pertains to pleasure and comfort, eudaimonic well-being relates more to ideals such as authenticity, meaning, excellence, and growth. The virtue-centered nature of Eudaimonia cannot be captured with hedonic measures and therefore a new method was needed in order to completely grasp well-being. One model that takes into account Aristotle's conception of well-being is Ryff's (1989) model of psychological well-being. Psychological well-being has been used as an outcome variable in dozens of studies. Research shows that eudaimonic well-being can vary in an individual over time (Ryff 2004).

The six factors included in psychological well-being are self-acceptance, personal growth, purpose in life, environmental mastery, autonomy, and positive relations with others. Self-acceptance is defined as a positive attitude towards the self and acceptance of both good and bad qualities. Personal growth can be understood as continued development in terms of openness to new experiences, realization of personal potential, and continuous improvement and positive change. Purpose in life is simply concerned with the individual's direction, objectives, and sense of meaning. Environmental mastery has to do with managing the external context surrounding one's life. An individual with high environmental mastery is able to effectively take advantage of opportunities and chose the contexts that best allow for fulfilment of personal needs and values. Autonomy is concerned with an individual's ability to resist social pressures, regulate behavior

from within, and evaluate himself through personal standards. Finally, positive relations with others covers social aspects of an individual's life such as the quality and quantity of relationships, concern for the welfare of others, and capacity for empathy, affection, and intimacy. These factors are better suited to highlight important pieces of well-being such as reaching life goals, utilizing talents, and maximizing potential as a person.

Psychological well-being is divided into two categories: personal functioning and social functioning. This distinction is important because the relationship between the two categories can affect overall well-being as an individual chooses when to prioritize social elements versus personal elements. Neglecting either of the two categories will bring down overall psychological well-being in an individual, so appropriate balance is imperative. More on the distinction between social and personal functioning will be explained in the following chapter.

Economic Freedom

Economic Freedom is a hallmark of modern liberal society. Economists dating back to Adam Smith assert that economic freedom is the best institution to promote economic activity and prosperity (Hall & Lawson, 2013). Evidence is abundant that economic freedom is positively correlated with economic growth and income levels (Faria and Montesinos, 2009), gender equality (Stroup, 2008), and civil peace (de Soysa & Fjelde, 2010). Additionally, the impact of higher material standards should not be downplayed. Studies show higher levels of personal income allow individuals to live longer, happier, healthier lives (Frey & Stultzer, 2009), as well as experience freedom from capital restraints (Stroup, 2007).

If economic freedom has such widespread benefits, then why is it not promoted more around the globe? Critics of economic freedom cite increases in income inequality (Carter, 2007)

and dominance of big business in free economies. However, evidence also exists that, on average, disproves the existence of systematic inequality in free economies (Ashby and Sobel, 2007; Berggren, 1999; Scully, 2002). Other criticisms state that capitalism creates more pressure at work and is merciless to disadvantaged members of society because free economies do not incorporate large welfare states. Furthermore, some argue that not all consumption decisions are fully rational and therefore the government has a mandate to rationalize these decisions (Gehring, 2013). Proponents of economic freedom respond to these criticisms by arguing that people are no more rational as voters than they are as consumers. Further, politicians are not more rational or less self-interested than the rest of the population (Caplan, 2007; Cosmides & Tooby, 1992).

Indirect evidence suggests that economic freedom is positively correlated with subjective well-being (Rode, 2013; Gehrig, 2013). As research shows there is a significant and positive correlation between economic freedom and both economic growth and income per capita (Faria and Montesinos, 2009). Furthermore, studies show that economic growth and income are positively correlated with subjective well-being. People with higher levels of income are more satisfied with their lives both within and across countries. Importantly, recent research shows that as countries become richer, life satisfaction increases (Sacks, Stevenson, & Wolfers, 2010). This implies that economic freedom can increase subjective well-being through its positive effect on economic growth and development.

Economic freedom has many components and can therefore be difficult to systematically measure. In 1996, the Heritage Foundation published the first Economic Freedom Index of the World (EFW) which attempted to objectively create a comprehensive ranking of economic freedom for over 140 countries. The index is updated annually and now contains 142 countries

that are ranked on 42 variables on a scale of 1-10. These variables are categorized into 5 main areas: (1) Size of government, (2) Legal System and Property Rights, (3) Sound Money, (4) Freedom to Trade Internationally, and (5) Regulation. Size of government refers to government spending, taxation, and power of government-controlled enterprises, which shift decision making from individuals to central government and thus reducing economic freedom. Legal System and Property Rights has to do with the protection of individual's fairly acquired property which is a key element of economic freedom. The role of sound money is ensuring that inflation is minimized and protects the value of individual's property. The freedom to trade internationally highlights the rights to buy and sell without restrictions and should not be hampered. Finally, regulation refers to the government's usage of exchange limitations that cripple economic freedom. The three main principles that determine the index's methodology are objectivity, accuracy, and transparency (Hall & Lawson, 2014). The most free countries in 2018 are Hong Kong, Singapore, New Zealand, Switzerland, Ireland, and the United States, while the least free countries in the world are Venezuela, Libya, Argentina, and Algeria.

CHAPTER THREE

Hypotheses Development

Personal Functioning focuses on factors at the individual level such as resilience, meaning and purpose, autonomy and control, engagement, competence, and self-acceptance. Resilience is a measure of someone's ability to cope with difficult circumstances. More resilient individuals are able to adapt and maintain positive well-being in the face of challenges or uncertainty. Challenges and uncertainty can be excellent motivation for some people, but others crack under the pressure. People in free countries are expected to provide for themselves because welfare benefits are minimal. Welfare is a large government-run institution that is fundamentally antithetical to the principles of economic freedom (Saint-Arnaud & Bernard 2003). This work-driven culture can be stressful at times, leading to opportunities for resilient individuals to excel. Free economies promote resilience among their citizens, therefore increasing personal functioning and psychological well-being.

Similarly, meaning and purpose are closely aligned with economic freedom. The intentional pursuit of future-oriented goals is a key component of personal functioning and highlights the belief that current actions will make a tangible difference in future outcomes. As the name would suggest, economic freedom leads to more opportunity. Countries with higher levels of economic freedom, specifically in property rights, fiscal freedom, and monetary freedom are correlated with entrepreneurial activity (McMullen, Bagby, & Palich, 2008). Economic freedom gives ambitious and driven individuals the arena they need to pursue their

goals. Free trade, sound money, and low taxation benefit high earners because they allow the laborer to receive the full fruit of their labor. Consequently, free economies are better equipped to improve personal functioning.

Autonomy is another aspect of personal functioning that benefits from economic freedom. Individuals who live in accord with their own personal convictions independently of others are said to be more autonomous (Metaal, 1992). Autonomy and independence are basic needs and both are seen as fundamental to experiencing well-being in any form. Free economies provide individuals with autonomy by lessening their economic dependence on others. As previously mentioned, economic freedom creates an environment where labor is appropriately rewarded and thus people have means to live on their own terms. Research shows that people who believe their choices determine their outcomes have a greater appreciation for freedom of choice than those who believe the outcome of their actions comes from external factors (Verme 2009). Autonomy and personal responsibility are the cornerstone of economic freedom. We can expect that as economic freedom increases, the resulting culture will exhibit a higher degree of autonomy.

Engagement is the practical element of personal functioning that lays the foundation for the other more abstract elements. Economic freedom requires a level of professional creativity to find one's niche or competitive advantage as proven by the aforementioned correlation between entrepreneurship and economic freedom (McMullen, Bagby, Palich 2008). Entrepreneurship involves finding a unique corner of the economy in order to provide value to society. To find that niche, entrepreneurs seek out work that fully allows for engagement, in whatever form that takes. Entrepreneurship is directly correlated with personal functioning as well (Nikolaev, 2014). The same principles apply to employees as well. Research shows that freedom within a work

environment leads to higher engagement (Ryde & Sofianos, 2014). To create job safety, employees are encouraged to learn new skills and continue their professional development which translates into continuous engagement. The dynamic environment created by free economies encourages engagement and therefore increases personal functioning.

Competence can be defined as an individual's ability to apply personal strengths and abilities to areas of performance and decision making. Again, free economies are best setup to promote competence among its constituents because people are encouraged to find their competitive advantage and maximize their personal potential. The reward people earn is theoretically proportionate to their competence at their profession. Economic freedom minimizes the transaction costs that take away from an individual's reward for competence. As a nation's level of economic freedom increases, so too does their population's competence and as a result, personal functioning improves.

Self-acceptance is the final element of personal functioning. Intuitively, self-acceptance has to do with an individual's understanding of what strengths and limitations he possesses and accepting them for what they are. As far as personal functioning is concerned, self-acceptance is critical in achieving well-being. Economic freedom provides the opportunity for individuals to take chances and follow whatever kind of life path they may chose. This may make it easier to achieve self-acceptance if the individual knows that their situation is a result of the choices that they made.

Resilience, meaning and purpose, autonomy and control, engagement, competence and self-acceptance are the key components of personal functioning (Ryan & Deci, 2000; Seligman, 2012; Ryff, 2014). Each component of personal functioning is fundamentally linked to economic freedom, thus suggesting that personal functioning should increase with economic freedom.

Additionally, personal functioning is positively correlated with subjective well-being because the same components that constitute personal functioning also influence life satisfaction (Deci & Ryan, 2017; Seligman, 2012; Ryff, 2013). This suggests that the combination of personal functioning factors allow economic freedom to influence subjective well-being.

Hypothesis 1: Economic Freedom increases personal functioning.

In contrast to personal functioning, social functioning is related to the quality and quantity of relationships individuals form. Like personal functioning, social functioning is broken down into several components which are categorized as thick relationships, thin relationships, and civic engagement. Social functioning is a crucial element of subjective well-being because people are naturally social and therefore need a well-developed social network to thrive. Even in societies where individuals report high levels of personal functioning, citizens might still not have high levels of well-being if social functioning is lacking. Social functioning leads to happiness, satisfaction, health, and productivity (Putnam, 2000; Helliwell & Putnam, 2005).

Thick relationships focus on closer, more prominent relationships to the individual. These thick relationships can be thought of as “bonding ties” such as connections to family and friends. Thick relationships provide sources of support which is measured by the extent to which people feel they have others who support them emotionally. Feeling appreciated is another sub-component of thick relationships and measures the extent to which people feel they are valued, recognized, respected, and acknowledged by close family and friend. Thick relationships help to combat loneliness, which is a leading cause of depression. The last sub-component of thick

relationships is reciprocity in social exchange, which measures the balance between giving and receiving in close social relationships.

Whereas thick relationships are bonding ties with people close to the individual, thin social relationships are “bridging ties” to people who are less close to the individual. Thin relationships are broader but less deep than thick relationships. Examples of thin relationships include work acquaintances, distant friendships, or others that have infrequent contact. One key element of thin relationships is social trust, which measures how much fairness an individual perceives from other people. Other sub-components include the perception that others will treat you with respect, the frequency of social contact, a sense of local belonging, and the perception that an individual’s local area will offer sufficient support.

The third element of social functioning is civic engagement, which refers to the frequency that an individual participates in formal volunteering. Participating in the community is strong predictor of well-being (Stoll, Michaelson, and Seaford 2012). Community involvement is important in free markets as a way to give back to society and smooth income inequalities. In lieu of government social programs, volunteering is a way to benefit the lower tiers of society, but it also lends to improving the well-being of the volunteer. Not only are large government social programs costly in a financial sense, but they also eliminate opportunities for social volunteering that are beneficial for level of well-being.

Theoretically, economic freedom should increase social functioning. Economic freedom increases trust among citizens through promoting voluntary transactions and interactions among friends and strangers alike. The strong rule of law and monetary freedoms provided by free economies incentivize numerous interactions and inspire trust throughout the population (Berggren & Jordahl, 2005). More time spent in the workforce increases opportunities for

earning respect, feeling a social belonging, while simultaneously decreasing loneliness. Combined with the free market's promotion of civic engagement, tests should show a positive correlation between social functioning and economic freedom. Another avenue for economic freedom to increase social functioning is through the positive impact economic freedom has on gender equality (Stroup, 2008; Weichselbaumer & Winter-Ebner, 2007; and Zweimuller, 2008). Gender equality allows for both women and men to experience greater quality of their relationships through the notion that women should not be limited to domestic duties.

In combination, bonding, bridging ties, and civic engagement make up the main components of social functioning (Keyes, 1998; Ryan & Deci, 2000; Ryff & Singer, 1998; Seligman, 2012). Social functioning has a strong influence over subjective well-being, which suggests that it mediates the relationship between economic freedom and subjective well-being.

Hypothesis 2: Economic Freedom leads to higher social functioning.

There are some 400 known articles that cite specifically the Economic Freedom Index of the World as a primary variable, either dependant or independent. Of these 400 articles, a vast majority find economic freedom to be correlated in some beneficial way with other variables, while a small minority found a negative outcome (Hall & Lawson, 2014). These articles report all kinds of findings using a wide variety of other variables, including macroeconomic variables, financial variables, and human rights among others. Interesting findings reveal economic freedom is significantly positively correlated with income growth (Fria & Montesinos, 2009), gender equality (Stroup, 2008), and civil peace (see Soysa & Fjelde, 2010), but that it is also correlated with the Gini Coefficient (Carter, 2017).

In order to further develop the findings from the first two hypotheses, it is important to know exactly how economic freedom impacts psychological functioning. To do that, we must track the pathways through which economic freedom can affect psychological functioning. I propose the following channels through which economic freedom improves psychological functioning: economic development, unemployment, inflation, individualism, democracy, and income inequality. Evidence clearly supports the overwhelmingly positive influence of economic freedom on economic development factors such as growth and income (Faria & Montesinos, 2009) and its tendency to lower unemployment, especially with women and young people (Feldman, 2007). Elements consistent with economic freedom principles work to minimize inflation (Mafi-Kreft, 2003). Beyond just macroeconomic variables, socio-political variables are at play as well. Data indicate economic freedom leads to a higher level of individualism among a society as evidenced by the increases to entrepreneurship in free economies (McMullen, Bagby, & Palich 2008). It is easy to see how democracy, which is in essence political freedom, could be correlated with economic freedom. Research backs up this link, which confirms democracy's positive relationship to economic freedom (De Haan & Sturm, 2003). The final channel through which economic freedom could affect psychological functioning is income inequality. As previously mentioned, income inequality is one of the frequent complaints with economic freedom (Pickett and Wilkinson, 2015). Evidence shows that economic freedom is moderately significantly related to income inequality with low elasticity and also that income inequality is negatively correlated to happiness (Carter, 2007; Oishi & Diener 2011). This paper hypothesizes that despite potential issues with income inequality, economic freedom might still positively relate to psychological functioning through the channels of economic growth, democracy, innovation, unemployment, and inflation.

Hypotheses 3: There is an indirect path from economic freedom to psychological functioning through the channels of economic growth, social capital, innovation, and income inequality.

CHAPTER FOUR

Data & Methods

Data for this study came from the sixth wave of the European Social Survey (ESS). The ESS provides detailed accounts of well-being by conducting face-to-face interviews with individuals all across Europe. The sixth iteration includes a special well-being model that focuses on subjective well-being and psychological functioning components that are good indicators of eudaimonic well-being. Overall, over 50,000 individual observations are included from 29 European countries. For this study, I use the 29 countries with available data from the European Social Survey because of the quality and accessibility of the data. Data for economic freedom come from the Heritage Foundation's Economic Freedom Index of the World. This index ranks countries on: (1) Size of government, (2) Legal System and Property Rights, (3) Sound Money, (4) Freedom to Trade Internationally, and (5) Regulation. The index provides data on 140+ countries, which include the 29 European nations from the European Social Survey.

Consistent with the aforementioned theoretical framework, I derive each country's aggregated mean score for economic freedom by compiling their respective scores on each of the following categories: (1) Size of government, (2) Legal System and Property Rights, (3) Sound Money, (4) Freedom to Trade Internationally, and (5) Regulation according to the Economic Freedom of the World Index. Consistent with Carol Ryff's psychological functioning model, I use data from the European Social Survey to compile an aggregate score for each country's respective personal functioning factors: (1) resilience, (2) meaning & purpose, (3) autonomy,

(4) engagement, (5) competence, and (6) self-acceptance. Similarly, to derive each country's social functioning score, I use European Social Survey data on the following factors: (1) thick relationships (strong ties), (2) thin relationships (weak ties), and (3) civic involvement.

With each of the 29 nations having scores in economic freedom, personal functioning, social functioning, and psychological functioning, I can use Stata 15 to create a linear regression model, indicating relationships between the variable scores. I run a regression for each of personal functioning and social functioning against economic freedom.

Since the data used in this study focuses on observations at the country level, I control for a handful of macroeconomic variables. The variables I control for are population size, GDP growth rate, unemployment, and inflation. Studies indicate that these variables could affect both economic freedom and psychological functioning at the same time. Scholars have claimed that economic freedom could lead to greater population growth, which could also impact psychological functioning through increased competition for limited resources (Norton, 2002). Evidence shows that economic freedom is an important determinant in GDP growth, which also affects well-being (Carlsson & Lundstrom, 2002). Unemployment and inflation are both variables that play a role in both economic freedom and well-being (Mafi-Kreft, 2003; Feldman, 2007).

I create a Structural Equation Model to explore the mediation effects of income inequality, economic development, unemployment, inflation, democracy, and individualism for economic freedom's relationship to psychological functioning. Many of the variables are measured by common statistics that are easy to understand. One exception is income inequality, which is measured by the Corrado Gini's Gini coefficient. The Gini coefficient measures the

dispersion of wealth among a nation's residents and is one of the common measurements of income inequality (Gini, 1912).

Structural Equation Modeling shows the relationship between any mediating variables with the two primary variables in the study. In this case, the model shows the relationship between economic freedom and each of the aforementioned mediating variables, and then it shows the relationship between that respective mediating variable and psychological functioning. For example, if a variable is positively correlated with both economic freedom and psychological functioning, it follows that economic freedom increases that variable, which in turn increases psychological functioning, so therefore we can say economic freedom influences psychological functioning through the channel of that variable. Conversely, the rule of double negatives can be applied to mediating variables that display a negative relationship to both economic freedom and psychological functioning. This means that economic freedom is negatively correlated with the mediating variable, and because the mediating variable is also negatively correlated with psychological functioning, then economic freedom increases psychological functioning through decreasing the mediating variable. Finally, if economic freedom and psychological functioning do not share the same sign with the mediating variable, then economic freedom does not increase psychological functioning.

CHAPTER FIVE

Results

I begin the empirical analysis with some exploratory bi-variate plots. Figure 1 shows the relationship between the EFW index and personal functioning for a sample of 26 European countries. The figure implies that higher level of economic freedom increases personal functioning. Figure 2 shows the relationship with respect to social functioning. Once again, I find a strong positive correlation between EFW index and social functioning.

Figure 1: Economic Freedom and Personal Functioning

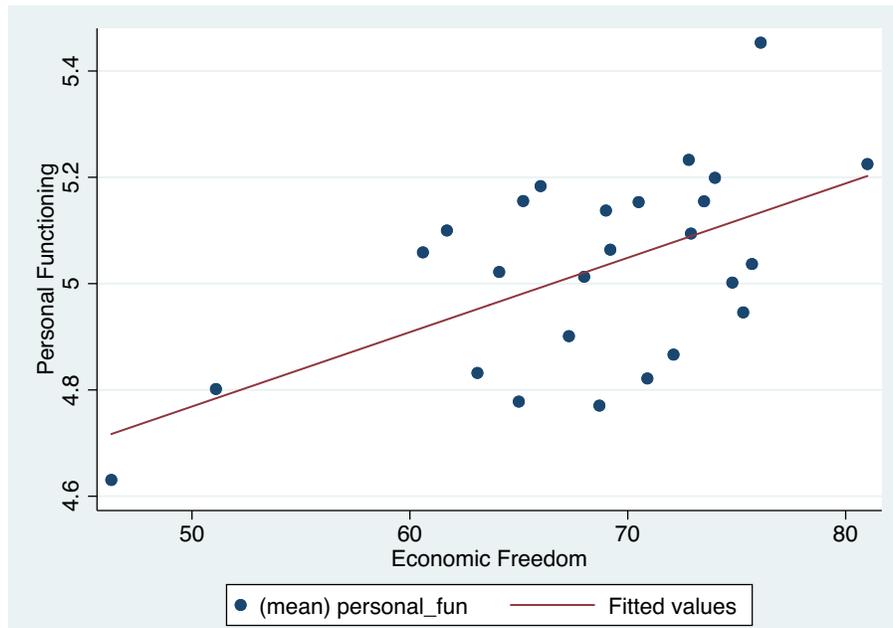
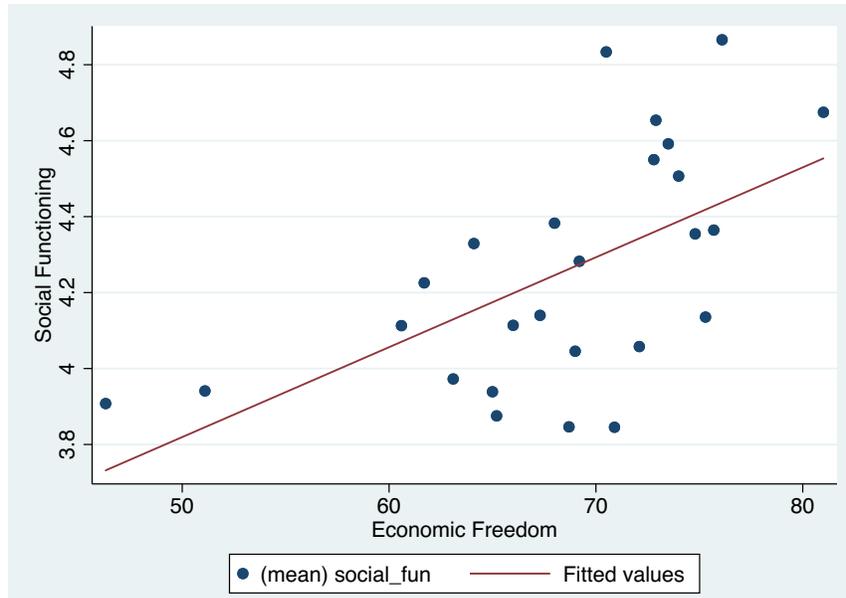


Figure 2: Economic Freedom and Social Functioning



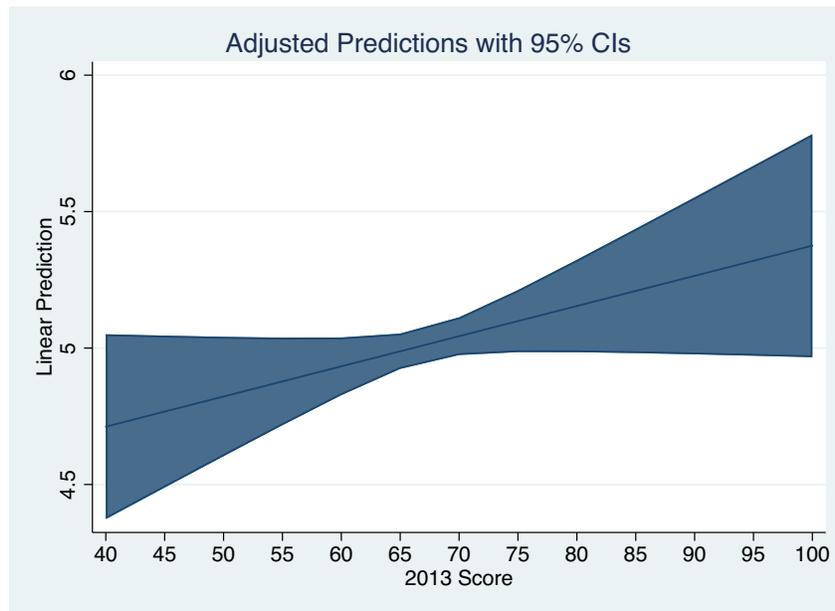
Linear Regressions

In order to account for omitted variable bias, I next estimate the relationship using a multi-variate linear regression model. Table 1 summarizes the results with respect to personal functioning and includes controls for population, GDP growth rate, unemployment, and inflation. The estimations in Table 1 suggest that the EFW index is positively correlated to personal functioning, although the relationship is only marginally significant ($p < 0.075$). To ease interpretation of the results, Figure 3 shows predictive margins with 95% confidence interval, holding all other variables in the model at their sample means. The clear upwards slope of the predicted line shows clearly the positive relationship between the EFW index and personal functioning and is consistent with the results in Figure 1. The R-squared of 0.4823 shows that 48% of the change in personal functioning is due to the change in economic freedom.

Table 1: Economic Freedom and Personal Functioning

| Personal Functioning | Coef. | Std. Err. | t | P>t | [95% Conf. Interval] |
|---------------------------------|------------|-----------|-------|-------|----------------------|
| Economic Freedom | 0.0110536 | 0.0058936 | 1.88 | 0.075 | -0.0012402 0.0233473 |
| Population (in millions) | 0.0010892 | 0.0006942 | 1.57 | 0.132 | -0.000359 0.0025373 |
| GDP Growth Rate | -0.0115297 | 0.0167705 | -0.69 | 0.500 | -0.0465124 0.0234531 |
| Unemployment | -0.0088359 | 0.0047063 | -1.88 | 0.075 | -0.0186531 0.0009814 |
| Inflation | -0.0277803 | 0.0255449 | -1.09 | 0.29 | -0.0810661 0.0255054 |
| _cons | 4.447021 | 0.4405165 | 10.1 | 0 | 3.52812 5.365922 |
| R Squared | 0.4823 | | | | |
| Number of Observations | 26 | | | | |

Figure 3: Economic Freedom and Personal Functioning, Predictive Margins



Next, I replicate the analysis with respect to social functioning. Table 2 summarizes the results again controlling for population, GDP growth rate, unemployment, and inflation. Once again, I find a significant positive relationship between economic freedom and social functioning ($p < 0.07$). Similarly, Figure 2 shows predictive margins with 95% confidence interval with

respect to social functioning and suggests a positive relationship between the EFW index and social functioning. Overall, the empirical results suggest that even after controlling for a number of relevant controls, economic freedom is positively correlated with personal and social psychological functioning. The R-Squared of 0.5267 indicates that much of the marginal change in social functioning is due to changes in economic freedom.

Table 2: Economic Freedom and Social Functioning

| Social Functioning | Coef. | Std. Err. | t | P>t | [95% Conf. | Interval] |
|---------------------------------|--------------|------------------|----------|---------------|-------------------|------------------|
| Economic Freedom | 0.017714 | 0.009245 | 1.92 | 0.07 | -0.0015708 | 0.036998 8 |
| Population (in millions) | 0.0028374 | 0.0011666 | 2.43 | 0.025 | 0.000404 | 0.005270 8 |
| GDP Growth Rate | 0.0028102 | 0.0229607 | 0.12 | 0.904 | -0.045085 | 0.050705 4 |
| Unemployment | -0.0150861 | 0.0126463 | -1.19 | 0.247 | -0.0414659 | 0.011293 6 |
| Inflation | -0.0689193 | 0.0408579 | -1.69 | 0.107 | -0.1541475 | 0.016308 8 |
| _cons | 3.341507 | 0.731319 | 4.57 | 0 | 1.816002 | 4.867011 |
| R Squared | 0.5267 | | | | | |
| Number of Observations | 26 | | | | | |

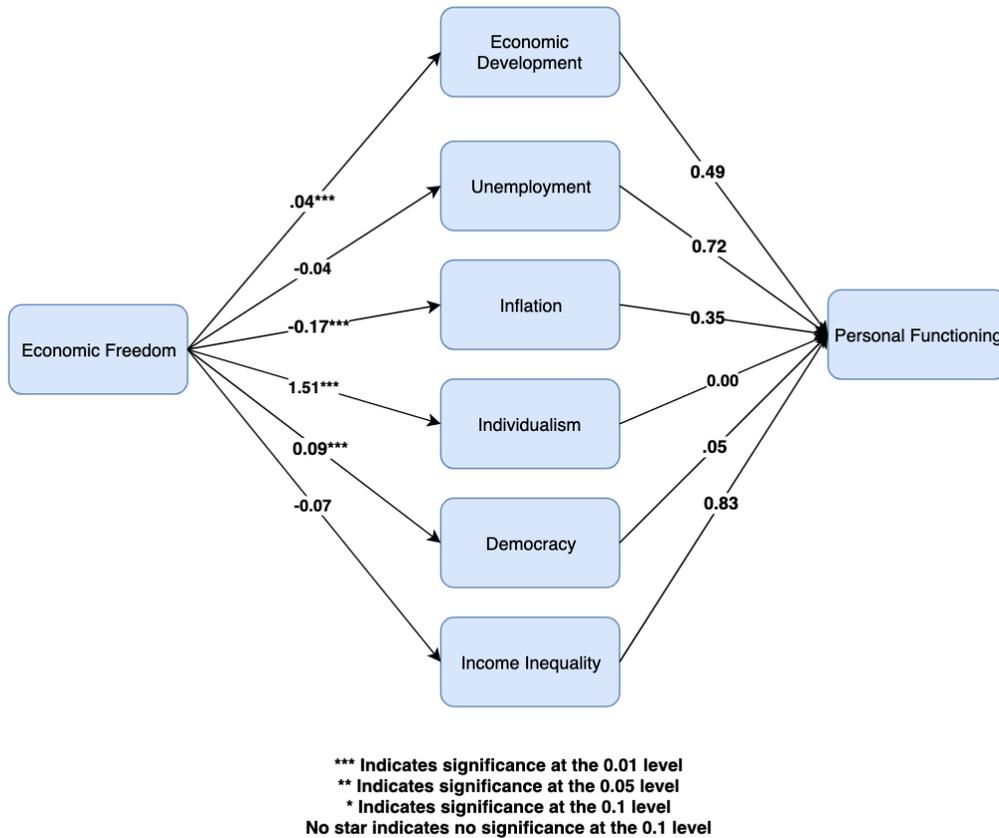
Structural Equation Modeling

In the previous section, I found a positive correlations between the EFW index and personal and social functioning even after controlling of a number of variabels such as unemployment, inflation and economic development. However, it is likely that economic freedom works through some of these channels. For example, economic freedom is strongly and positively correlated with economic development, which can increase both personal and social functioning. Similarly, more economically free societies are less likely to experience high levels of inflation and

unemployment, which can positively relate to people's personal and social functioning as well. Therefore, in this section, I examine the socio-economic paths of economic freedom on personal and social functioning using structural equation model (SEM).

Figure 3 shows a summary of the SEM model. I find that economic freedom is positively correlated to economic development, democracy, and individualism and negatively correlated to income inequality, unemployment, and inflation. The nature of each of these relationships are as I previously predicted in the paper, except for income inequality, which I predicted to have a positive relationship with economic freedom. In turn, economic development and individualism both display a positive relationship to personal functioning, while democracy, unemployment, income inequality, and inflation display a negative relationship. The positive relationship personal functioning shares with economic development and individualism as well as the negative relationship personal functioning shares with unemployment, inflation, and income inequality were predicted accurately. However, the negative relationship between democracy and personal functioning was unexpected. The correlations between economic freedom and economic development, inflation, individualism, and democracy are all significant at the 0.01 level. The other relationships are not statistically significant. Overall, these results indicate that economic freedom is positively correlated with personal functioning through the channels of economic development, individualism, unemployment, and inflation, although these findings are not statistically significant. Democracy is negatively correlated to personal functioning. Despite this negative relationship, the overall impact of economic freedom on personal functioning is still significantly positive, as indicated by Table 1 and Figure 1.

Figure 3: Structural Equation Model linking Economic Freedom and Personal Functioning

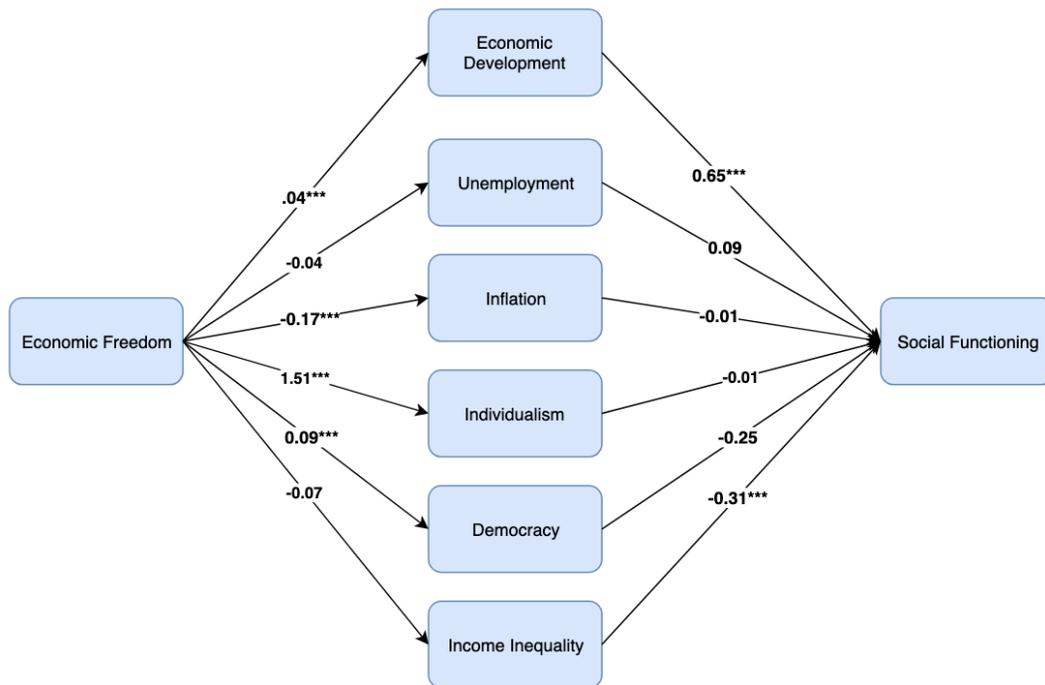


In Figure 4, we observe the effects of our mediating variables on economic freedom’s relationship with social functioning. Again, economic freedom is positively correlated to economic development, democracy, and individualism but it was negatively correlated to income inequality, unemployment, and inflation. These relationships all came out as expected, bar income inequality. In turn, economic development, individualism, and unemployment were positively correlated with social functioning, while democracy, income inequality, and inflation were negatively correlated with social functioning. I accurately predicted that social functioning would be positively correlated with economic development and individualism as well as that social functioning would be negatively correlated with income inequality and inflation.

However, I incorrectly predicted social functioning’s relationship to democracy and

unemployment. The relationships between economic development, inflation, individualism, and democracy are all significant at the 0.01 level. The relationships between social functioning and economic development and income inequality are also significant at the 0.01 level. None of the other relationships are statistically significant. These results indicate that overall, economic freedom is positively correlated with social functioning through the channels of economic development, income inequality, individualism, and inflation. Economic freedom does not positively correlate to social functioning through the channels of unemployment or democracy. These findings are not statistically significant at the 0.1 level. Despite unemployment and democracy being non-positive channels, the overall relationship between economic freedom and social functioning is still significantly positive as evidenced by Table 2 and Figure 2.

Figure 4: Structural Equation Model linking Economic Freedom and Social Functioning



*** Indicates significance at the 0.01 level
 ** Indicates significance at the 0.05 level
 * Indicates significance at the 0.1 level
 No star indicates no significance at the 0.1 level

CHAPTER SIX

Discussion & Conclusion

This study has several potential implications. First, this study connects economic freedom to psychological functioning, which differs from other notions of well-being. This study shows that economic freedom does not just improve the way people feel, but it also leads to citizens living a more flourishing life. A flourishing life is one that includes autonomy, control, competence, resilience, and the quality of social relationships (Ryff, 2013; Nikolaev). Previous literature states the importance of viewing overall well-being with both the hedonic and eudaimonic accounts in mind (Deci & Ryan 2001). This study adds to research on the often-overlooked side of eudaimonic well-being which is important to ensure we have a complete understanding of the effects of economic freedom. Furthermore, the results of this study indicate that governments interested in improving the well-being of citizens should consider implementing policy consistent with principles of economic freedom. Implementation of such policies have the ability to positively alter not only the hedonic well-being of citizens (Nikolaev and Bennett, 2017; Rode, 2013; Gehring 2012), but also the eudaimonic well-being of citizens as well.

This study is not without its limitations. The first limitation is that I have only observed 26 countries with suitable data available for eudaimonic well-being. All of these countries are European and therefore it is not necessarily indicative of global trends. The 26 countries observed do have 54,000 individual-level observations between them which somewhat

compensates for worries about sample size, but a dataset including countries from all over the world would be better. Another limitation is that this study is cross-sectional so we cannot follow how these relationships change over time. The dynamic nature of these relationships could be susceptible to change over time, but unfortunately I am presently unaware of any dataset that observes psychological functioning in continuous time. Also, my predictions for the Structural Equation Modeling were inconsistent. Although several relationships intuitively followed previous research, my data showed unfounded relationships involving income inequality, democracy, and unemployment. This could be due to aforementioned limitations regarding available data, or it could indicate limitations with previous research.

Overall, I conclude that economic freedom is positively correlated with both personal functioning and social functioning. Furthermore, macro-economic variables such as development, democracy, individualism, unemployment, inflation, and income inequality partially mediate the relationship between economic freedom and psychological functioning, although the significance of this mediation is low. These results show that perceived problems with economic freedom do not outweigh their benefits from a well-being perspective.

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