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Well-being and economic freedom: Evidence from the States

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ABSTRACT

There is ample evidence that well-being, measured in various ways for a large number of countries, is positively related to the level of general intelligence. Pesta at al. (2010a) verify this close relationship between well-being and IQ across states. There also is evidence that well-being is positively related to economic freedom across countries. The purpose of this study is to determine whether economic freedom and well-being are related at the state level. Our regression analysis indicates that, across the 50 states, improvements in economic freedom lead to higher levels of well-being after controlling for other economic factors. We also find that the relationship between well-being and economic freedom differs significantly across regions in the United States.

1. Introduction and overview

The interest that social scientists have shown in studying the factors that increase well-being has increased markedly over the past few decades. Clark (2008) reported that, based on an ECONLIT search, between 1960 and 2006, over 600 articles with some combination of the words "happiness," "well-being," "life satisfaction," or "job-satisfaction" in the title have appeared in academic journals. Of these, almost 60% appeared after 2000.

This research agenda is wide-ranging, examining the potential links between economic success and well-being. It is reflective of the basic finding that economic success, measured by an individual's earnings, is directly linked to IQ (inter alia, Gottredson, 1997; Lynn & Vanhanen, 2002; McDaniel, 2006b). Higher IQ individuals, and apparently countries, also demonstrate greater patience and a willingness to save (Jones, 2012 and the references cited therein). The evidence (reviewed below) also points to a positive and robust correlation between a country's rate of economic growth and general intelligence. To that end, researchers have found that economically successful countries are characterized not only by higher levels of well-being, but also by greater economic freedom. Only recently (e.g., Rindermann, 2011; Rindermann & Thompson, 2011) have researchers begun exploring the link between general intelligence, economic freedom and economic success.

A prominent line of research has tested whether economic success is a factor that explains well-being or happiness. Easterlin's (1974, 1995) found that rising national incomes are not necessarily associated with increased national happiness. Veenhoven (1991), Diener, Diener, and Diener (1995), Easterly (1999), Lane (2000), and Blacnhflower and Oswald (2000), among others, refute Easterlin's claim, finding that improved economic conditions enhances subjective well-being. Others, such as Hagerty and Veenhoven (2003), Tella, MacCulloch, and Oswald (2003), and Ovaska and Takashima (2006), have explored the robustness of the link with conflicting results. Peiro (2006), for instance, finds that economic factors can have different quantitative effects depending on whether one is interested in happiness or well-being: they are not necessarily the same.

This research raises several important questions, such as "Is it happiness, satisfaction or well-being that is being

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captured?" Surveys of measuring well-being, such as Sharpe and Smith (2005), give perspective to the diversity of this concept. Kahneman, Krueger, Schkade, Schwarz, and Stone (2004) and Krueger, Kahneman, Schkade, Schwarz, and Stone (2008) are attempts to provide an economics-based, quantitative measure of well-being based on time allocation. Within their different disciplines' perspectives, Kahneman, Diener, and Schwarz (1999), Diener and Suh (2000), Frey and Stutzer (2002), Tella and MacCulloch (2006) attest to the unsettled issue of what exactly is meant by well-being.

Into this mix, a number of researchers have investigated the relationship between well-being and economic freedom. Economic freedom has long been championed as elemental in achieving economic success. Exemplified by Hayek's (1944) and Friedman's (1962, especially Chapter 1) noteworthy contributions to this line of thought, economic freedom—the ability to engage in exchange, to operate in an economy characterized by rule of law and protection of property rights, among others—is often viewed as the bedrock of economic success, and by extension economic well-being (Karabegovic & McMahon, 2005). If a greater degree of economic freedom enhances one's economic condition, and improved economic conditions are associated with higher levels of well-being, improved economic freedom should be associated with higher levels of well-being or happiness.

There is evidence to support this assertion. Esposito and Zaleski (1999) used a sample of countries and found that increased economic freedom is associated with a better quality of life, measured as longer life expectancy and higher literacy rates. Ovaska and Takashima (2006) concluded that economic freedom and improved health are positively related. These are, they note, important findings since health is a robust predictor of well-being at the individual and aggregate levels. Welsch (2003) also reported that greater economic freedom is causally prior to income: the direction of influence flows from improved freedom then to income to happiness. This causal interpretation was disputed by Dawson (2003), though the freedom-happiness correlation was not disputed. Stroup's (2007) analysis led him to conclude that economic freedom helps explain economic well-being conditioned on the country's level of democracy. Gropper, Lawson, and Thorne (2011) concluded that there is a significant positive relationship between economic freedom, measured using several indices, and happiness across countries. Inglehart, Foa, Peterson, and Welzel (2008) reported that increased happiness is positively correlated with improvements in economic choice in countries with higher levels of economic security. Bjornskov, Dreher, and Fischer (2010) took a similar tack and found that changes in freedom and institutional quality affect happiness differently across countries depending on their level of economic development. And Wilkinson (2007) refuted the argument by Lane (2000) that happiness erodes in market economies.

A common feature of much of this research is reliance on international data to compare well-being, economic freedom, and economic outcomes, such as greater income per capita. What is lacking, and the void that this study attempts to fill, is to see how robust these links are using sub-national level. We know that state IQ and economic success, measured as the level of real income per capita, are positively related (McDaniel, 2006b; Pesta, McDaniel, & Bertsch, 2010a and the papers cited therein). What we do not know is whether greater economic freedom increases well-being at the state level.

We address that issue using state-based indices of well-being and economic freedom. The well-being index comes from the recent work of Pesta et al. (2010a). The economic freedom measure is published by the Fraser Institute. In the next section we briefly describe the index of well-being and the Fraser economic freedom measure. Following that discussion, our empirical methodology is presented in Section 3, our results are found in Section 4, followed by conclusions in Section 5.

2. Well-being and economic freedom

2.1. Well-being

Measures of well-being span many disciplines, including psychology, economics, sociology, criminology and public policy. The well-being index generated by Pesta et al. (2010a) is an important development because it allows social scientists to analyze observed geographical differences in well-being across states. Such information lends itself to investigation by applied psychologists, economists and sociologists to gauge the efficacy of the different states' public policies.

This well-being index also fits within the research agenda aimed at more completely understanding the so-called *g* nexus. A number of studies in psychology and economics have found (see references in Pesta, McDaniel, and Bertsch (2010a) that general intelligence is a robust predictor of individual educational success, higher income, health and longevity. A growing body of work in economics finds that countries with higher levels of general intelligence also tend to experience higher rates of economic growth. Jones and Schneider (2006), for example, found that Lynn and Vanhanen's (2002) IQ measure is an extremely robust predictor of economic growth even after accounting for a wide variety of other possible factors, including health and educational attainment. With a well-being index that reliably overlaps with the *g* nexus, Pesta et al. (2010a) provide a valuable data set that allows researchers to analyze how alternative institutional arrangements—government policies, legal structures, social conditions—affect well-being.

Well-being generally is measured in one of two ways.[2] One is based on subjective assessments, compiled from survey responses to questions related to factors such as life satisfaction, happiness, and quality of life. Another approach used in constructing the well-being index accounts for the attainment of physical needs, such as food and shelter, along with measures of psychological health. Pesta et al. (2010a) employ this latter approach, arguing that improved psychological health stems in part from the ability to deal with the demands of life (competence), the ability to establish and work toward goals (aspiration) and others. One important objective in constructing their well-being index was to construct an empirical measure that interconnects it with the *g* nexus.

[2] It is beyond the scope of our study (and our expertise) to weigh-in on the controversy surrounding the use of self-perceived measures (responses to surveys) or the objective type typified by Pesta et al. (2010a). Reviews and discussion can be found in, among others, Diener (2000), Anger (2005, 2009), and Pesta et al. (2010a).