

# Economic policy and the level of self-perceived well-being: An international comparison

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## Abstract

The focus of macroeconomic inquiry has traditionally been on studying economic growth. The success or failure of any government initiated expenditure, revenue, or regulatory policy is commonly judged by the rate of the ensuing economic growth. This study focuses on whether economic variables that figure prominently in current policy discussions, such as economic growth and economic freedom, are related to the self-reported levels of well-being of individuals. The econometric analysis attempts to uncover those economic factors that appear to be the most highly correlated with a country's success or failure in promoting its citizens' well-being. The cross-country sample includes 68 countries of diverse characteristics and uses averaged data for the 1990s.

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## 1. Introduction

There are few things more precious to people in life than happiness and well-being. The 1776 Declaration of Independence of the Thirteen U.S. Colonies famously noted that “We hold these truths to be self-evident, that all men are created equal, that they are endowed by their Creator with certain unalienable rights, that among these are life, liberty and the pursuit of happiness.” The Soviet constitution of 1977 is no different in stressing the desire to create a society where “[. . .] the well-being of the people is constantly rising, and more and more favorable conditions are being

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provided for the all-round development of the individual.” The new European Union constitution signed in the Fall 2004 also notes that “The Union’s aim is to promote peace, its values and the well-being of its peoples.” That happiness and well-being are so prominently displayed in the founding documents of such a diverse set of societies is a reflection of their universal importance to people.

The focus of macroeconomic inquiry has traditionally been on studying factors behind the gross domestic product, i.e., societies’ ability to produce and consume more goods and services. What has made this approach very attractive to modern economists in particular is its amenability to measurement, whereas happiness is harder to pin down. As evidence of economic growth’s importance in the current mainstream thinking in modern societies, we can observe that governments very rarely omit higher economic growth as one of the main targets of public policies. Indeed, the success or failure of any government initiated expenditure, revenue, or regulatory policy is commonly judged by the rate of the ensuing economic growth.

Nonetheless, using income to measure the success of public policies is problematic. Very few people would concur with the statement that what makes them content with life is solely a function of the consumption of goods and services, or saving. Indeed, particularly in wealthy countries, changes in income may represent only a small fraction of overall happiness. Good personal relationships, economic and political freedom, health, education, income distribution, and many other factors may be equally important or more important, yet their value is not explicitly measured by the market place. That the marketplace and capitalism in general are deficient in fulfilling people’s needs is an age-old argument. For instance, Karl Marx and Friedrich Engels argued that the materialistic desires of the dominant class – the bourgeoisie – were changing the whole nature of society towards an untenable state.<sup>1</sup> The important question is which are the factors that affect people’s well-being? How important are the economic factors in people’s happiness and life satisfaction? Such questions are not only important for individuals but also crucial ones for policy makers to assess the efficacy of public policy.

Researchers have striven to come up with the measurement for well-being. Interestingly, even if economic growth figures prominently in current policy discussions, in the past 30 years there has been no lack of proposals for alternative measures of well-being, and for new ways to evaluate the effectiveness of public policies. Nordhaus and Tobin (1972), Estes (1988) and Daly and Cobb (1989) are examples of calls for broader approaches in measuring the success of government policies. The most commonly used of the alternative quality of life measures, the human development index (HDI) of the United Nations Development Program already has data going back 30 years. However, HDI is comprised of only three characteristics of society – life expectancy, educational attainment and GNP per capita – and does not reflect well-being comprehensively. Alternatively, researchers have recently taken advantage of increasing availability of survey data of self-perceived well-being. The data has been made available recently over longer time periods and across more countries.

This study utilizes this most updated and comprehensive survey data of well-being to find important determinants of well-being. More specifically, the paper explores how standard economic variables, such as income, economic growth, unemployment, inflation, foreign trading and

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<sup>1</sup> According to the early criticism by (Marx and Engels (1964, [1848]), the class arrangements under capitalism have “[. . .] resolved personal worth into exchange value, [. . .] torn away from the family its sentimental veil, and has reduced the family relation to a mere money relation. [This] constant revolutionizing of production, [has led to] uninterrupted disturbance of all social conditions, everlasting uncertainty [. . .]. All that is solid melts into air, all that is holy is profaned [. . .].”

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