Article

Economic Freedom and its Influence on Economic Growth and Human Development in Emerging Countries

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Abstract

The current study aims to analyze how the decisions governments make when applying a trade policy based on the economic freedom of emerging countries affect economic growth and human development because there is still no consensus on the most appropriate trade policy. This was achieved through panel data analysis that included information from 53 emerging countries in Latin America and Asia, corresponding to 2013 to 2022. It was found that economic freedom influences human development, but not significantly. However, this has a positive impact on economic growth. This study provides information to better explain political models focused on the free market and thus improve decision-making for governments regarding the quality and standard of living of emerging countries' populations. Based on institutional theory, this study generates new knowledge to understand how economic freedom and the human and economic development of emerging countries are related.

Keywords

Manufacturing SMEs, CSR, Organizational Performance, Mexico

Introduction

There are various studies on emerging countries and why poverty has not yet been reduced after applying a hegemonic economic policy focused on the free market since the 1990s (De la Dehesa, 2019). Some studies mention that there have been failures in the market (Stiglitz, 2018), where large corporations and other economic agents concentrate a large part of the capital, causing the disappearance of small producers and gaps in income, especially in the most vulnerable sectors. In turn, this results in the general population failing to develop on a human scale. Low wages and job insecurity coexist with economic growth and concentrate on a few people. This situation worsens income distribution, but the free market can significantly reduce this inequality in the long term, as explained by the inverted Kuznets curve (Huynh, 2022). The question is: For how long? Perhaps it will only be reflected in a higher rate of violence, generations without opportunities, and increased poverty (Caravaca, 2022).

It has been identified that an appropriate institutional framework is necessary to take advantage of the opportunities offered by any economic system (Varela & Ramírez, 2019). Therefore, there is a need to identify the best trade policy to support sustainable development. Some studies have shown that national policy focused on economic freedom influences human development (Jacimovic et al., 2013). Economic freedom is characterized by the incentives generated by property rights; increased government spending; development of strategies for opening and investing in new businesses; and labor, monetary, commercial, and investment freedom that have benefited employment (Jacimovic et al., 2013). Thus, it generates sustained growth (Haller, 2016; Egu & Aregbeshola, 2017). In addition, it generates the conditions for attracting foreign direct investment (FDI), which is initially attracted by the advantages of low costs and, in the medium term, by the conditions of the internal market, skilled labor, and infrastructure (Abbes et al., 2015).

This study identifies a theoretical model that shows how trade policy focused on the free market affects economic development, and therefore, sustainable human development. First, a theoretical debate is presented on how economic freedom is related to economic growth and sustainable human development so that empirical findings that support the premises proposed in this research can be presented.

The wealth of nations is seen as a consequence of an open and free business environment in which direct foreign investment, free flow of capital, exports, and imports prevail. The economic and health crisis generated in 2019 by the COVID-19 pandemic has created greater global tensions. This has made us wonder whether the free market benefits economic development (Aïssaoui & Fabian, 2021). This has generated greater concern about the true benefits it creates, such as employment (Jacimovic et al., 2013) and sustainable human development (Haller, 2016; Egu & Aregbeshola, 2017). This has increased populism, especially in Latin America, where corruption has dramatically increased. Populism and corruption in the free market provide the expected benefits for the at-risk population (Aïssaoui & Fabian, 2021).

Hence, institutions can create obstacles to human and economic development (Butzbach 2021). Dzionek-Kozlowska and Matera (2021) stated that national culture plays a crucial role in economic development. Human interactions are necessary for the industrialization process. In addition, certain rigid economic systems negatively affect economic freedom. It identifies with commercial openness, ease of investing and doing business, financial freedom, and monetary freedom. Different studies show that it is important to develop these variables because they encourage economic development in less developed countries (Arel-Bundock, 2017). However, economic freedom has also provided results regarding income inequality in the short term, whereas there has been a reduction in the long term. Therefore, it initiates economic growth, as explained by the curve-inverted Kuznets model applied in Asia (Huynh, 2022). This has generated an increase in countries with populist policies, but it has even been found that certain institutional changes focused on economic freedom are applied in some countries with this political aspect. They include the development of labor policies and tax incentives that encourage the creation of local businesses and, in turn, trigger economic development (Larnell, 2018). It has been found that during different economic crises, regulation of the capitalist system is required to achieve stability. Consequently, it is understood why changes generated in different democratic governments change to a model of greater control over capitalism (Ormaechea, 2021).

The previous economic trend could be explained by relying on new institutional economics to understand social changes, interdependencies, structural tensions, and the balances in the economic systems of developing countries that affect their growth (Nouira & Saafi, 2022).

In this sense, there is little adoption of formal institutional structures, but they will be systematically adopted by the interrelation of domestic politics and transnational mechanisms, as well as international competition. Therefore, institutional economics could explain the ease of doing business and, in turn, identify the potential for economic development (Urbano et al., 2020).

They are affected by environmental factors, such as the climate for doing business and the dynamism of the ecosystem, while psychological factors include risk aversion, desire for autonomy, and self-satisfaction (Porfirio et al. 2018). In addition, it has been revealed that entrepreneurship has an important relationship with economic growth, since the speed of such growth depends on the initiatives to conduct business. It is necessary to adopt policies that stimulate greater business performance and promote the entry of new ventures into the national market (Rusu et al., 2022). At the same time, the development of strategies for financial inclusion, such as banking digitization, is required (Zuo et al., 2021).

New entrepreneurs require more efficient and inexpensive capital (Esubalew & Raghurama, 2020) to turn them into true agents of change that trigger the development of a country. The following model (Figure 1) shows that the development of an open trade policy focused on globalization and economic freedom can achieve better human development supported by greater economic growth.

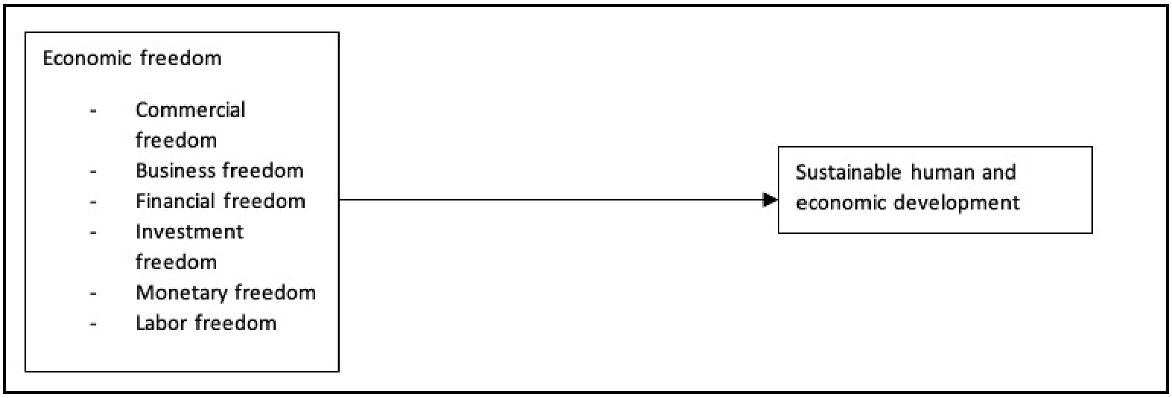

Figure 1. Research model

Source : Self made

Trade Policy and Human Development

Developed and developing countries apply different trade policies to attract FDI as the employment rate has improved in countries that have made major structural reforms by creating a more open market for foreign investment flows (Grahovac & Softić, 2017). However, they not only generate reforms, but also have financial and economic stability, a good level of security, and social equity.

Additionally, as previously mentioned, formal and informal institutions can generate difficulties in human and economic development (Butzbach, 2021). However, some studies show that an adequate institutional framework, such as a focused trade policy in the opening, stimulates economic development and triggers human development (Kowalewska et al., 2023), especially in less-developed countries (Arel-Bundock, 2017). This can be explained using the inverted Kuznets curve. It has been demonstrated that in Asian countries, there was inequality at the begining, but currently, it has been reduced substantially (Huynh, 2022). The quality of an institutional framework that regulates a business environment stimulates the quality of an institutional framework, regulates a business environment, stimulates entrepreneurship, and seeks to reduce uncertainty, which marks an important point in attracting foreign direct investment that triggers a spillover of knowledge about the economy (Aziz, 2019).

When analyzing a positive business environment, the human capital structure improves. This has a tangible effect on economic development. They conducted a study in 30 provinces of China and confirmed that the business environment and human capital structure create high-quality economic growth. Another important point in achieving human development is access to the national financial system, mainly through a public policy that encourages savings and access to credit to the most vulnerable sectors of the population. Provide purchasing power to those who can pay for quality education, medical care, etc. (Ababio et al., 2018).

Therefore, an increase in labor policies and tax incentives helps generate new businesses, both new and foreign direct investment (FDI), when multinational companies invest abroad in activities that create value. This activity has been proven to positively impact poverty reduction, productivity, human capital, and physical capital, generating capital flows in poor countries and positively affecting the balance of payments (Amir & Mehmood, 2012; Nikolov, 2016).

It also contributes to strengthening institutions that fight corruption (Topalli et al., 2021); consequently, sustained economic growth is achieved. Therefore, developing countries take advantage of the positive effects of trade opening and benefit from FDI flows and must have a specialized and qualified labor force to make them attractive to multinational companies (Barzotto et al. 2016). Countries that invest in human capital are attractive to FDI and, in turn, grow economically (Hamoudi and Aimer, 2017). It is worth mentioning that economic freedom variables such as investment, business, and financial freedom benefit society as a whole (Korle et al., 2020). Therefore, we propose the followinghypothesis:

H1 A commercial policy focused on the free market, such as commercial freedom, business freedom, financial freedom, investment freedom, monetary freedom, and labor freedom, generates greater human development.

Trade Policy and Human Development

The trade policy applied by countries since the 1990s has been characterized by privatization, democratization, and decentralization. Such policies have led to industrial reconfiguration. This was supposed to encourage not only the establishment of relevant institutions but also to reward citizens to accept certain initial losses, which inevitably came with the introduction of a new economic system (initial drop in income, rise in the unemployment rate, the growth of inequality, and the phenomenon of evident poverty). The development of institutions in countries with little tradition in their development was negatively affected by the strengthening of individuals and interest groups that made up political and economic powers, abusing the mechanisms of the democratic system to appropriate economic power and even more political. In such circumstances, the elements of acceptance of an authoritarian system with clear preferences regarding economic development, improvement of living standards, and reduction of poverty and inequality were produced as socially acceptable and preferred by the population (Praščević, 2013). However, it has been seen that in emerging countries where formal institutional policies of economic freedom were applied, they generate a positive impact on the generation of businesses that contribute to economic growth and reduce unemployment rates, as is the case of the BRICs (Udimal et al., 2020).

On the other hand, the globalization process is intrinsic to the result of multinational companies' activities given using foreign investment, exports, and imports and, in itself, all commercial relations with the exterior. Considering this, the market takes advantage of its advantages and obtains goods of acceptable quality at very low prices (Haller, 2016). It is possible to understand the role of international companies in the growth of domestic consumption and their ability to stimulate the competitiveness of export processes for all countries that participate in this environment. Thus, emerging markets, mainly manufacturing markets, benefit the most from this environment (Jacimovic et al., 2013). Therefore, the globalization process is essential for the system. Companies generate specialized skills for participation in specific sectors, as well as the use of technologies and management skills, in such a way that they obtain competitive advantages that cause sustained growth (Egu & Aregbeshola, 2017).

Governments have been concerned with regulating the imbalances caused by these production models through macroeconomic policies. The tax burden has favored the recovery of produced capital and prevented a significant reduction in productive resources, thereby strengthening the national economy, contributing to the improvement of inflationary processes, the growth of aggregate demand, and the premium of downside risk (Grubišić & Marčetić, 2013). Although it seems that taxes would hurt the development of companies, the reality is that their impact is minimal compared to their benefits. Net Present Value has generated a direct compensation rate that produces a change that could be positive in the long run; however, investors have the last word to make their investment based on this understanding (Hove & Chidoko, 2012).

The contribution of these policies to emerging and weakly developed markets has been "the growth";' pros and cons cannot be denied. When argued correctly, they could find adherents. Therefore, it is accepted that the processes imposed by globalization in emerging markets improve competitiveness and economies (Haller, 2016). Developing countries have expanded beyond their traditional participation in international production as recipients of FDI. In addition, we examine the impact of FDI in the countries of origin. In addition, emerging countries are large suppliers of inputs and finished products that generate foreign exchange and trigger economic growth.

Therefore, foreign direct investment (FDI) can be made attractive by developing a policy based on economic freedom. At first sight, this would seem beneficial for the country's macroeconomic development. Still, some studies demonstrate that investments have mostly been in manufacturing and service sector activities. This is due to cheap labor and raw materials (Bose, 2012), but not so much in research, development, and innovation (R+D+i). It has been proven that R + D + I can generate sustainable development. Its absence means that it does not have sufficient sophistication (Forte 2013). It is important to develop adequate conditions in developing countries: environmental factors such as the climate for doing business, the dynamism of the ecosystem, psychological factors such as risk aversion, the desire for autonomy and self-satisfaction, and the ease of doing business (Porfirio et al. 2018), as well as attractive costs. Therefore, it has been found that entrepreneurship has an important relationship with economic growth, since the speed of such growth depends on the initiatives of doing business, so it is necessary to adopt policies that stimulate the creation of greater performance that promotes the entry of new ventures into the national market (Rusu et al., 2022).

Developing countries have greater chances of absorbing investments from different countries in the short term, thus generating the right environment for economic development and increasing value in the long term (Grubišić & Marčetić, 2013). Evidence indicates that developing countries that apply free investment policies detonate their economic development. This is the source of transformation (Abbes et al. 2015). Emerging countries have made efforts to develop strategies to reduce political risk and improve institutions (Arel-Bundock, 2017), in addition to improving infrastructure, economic stability, reducing corruption, and the development of the internal market (Bose, 2012; Assunção et al., 2013).

It has been proven that emerging countries have achieved great changes, which have led to attracting foreign capital, which has translated into profits for foreign transnationals (Budiartha, 2018). It has also favored the creation and strengthening of transnationals in developing countries that have managed to expand into the world's richest regions. For this reason, lines of research have been generated on foreign direct investment (OFDI) abroad and the increase in the competitiveness of local companies. This logic between FDI and competitiveness creates links to the transfer of resources and technologies from international markets to the national economy. In addition, it transforms the production structure by acquiring large-scale resources, assets, and technologies to develop technology-intensive industries. It helps increase the competitiveness of local companies and, at the same time, establish new links to transmit resources and technologies from the global to the domestic market, in addition to developing distribution and value channels abroad (Caseiro & Masiero, 2014; Maciągowska & Kołtuniak, 2016; Knoerich, 2017; Egu & Aregbeshola, 2017; Noor et al. 2016; Nwaolisa & Francis, 2018), the following hypothesis is proposed.

H2: An economic policy focused on the free market, such as commercial, business, financial, investment, monetary, and labor freedom, generates greater economic growth.

Methodology

Data Source and Variables

To verify the previously proposed hypotheses, it was decided to develop an explanatory scope design, with information from the Index of Economic Freedom (IEF) published by The Heritage
Foundation and the Human Development Index (HDI) developed by the United Nations Development Program (UNDP) in a period from 2013 to 2021 and taking 53 emerging countries in Asia and Latin America. The regression technique with panel data with fixed effects (FE) regressions was used, and the Hausman test was developed to choose FE. In addition, it was found that there was heteroskedasticity and serial autocorrelation with the Wald and Wooldridge tests, 465 observations were obtained.

Measurement of Variables

The following variables: business freedom, labor freedom, monetary freedom, commercial freedom, investment freedom, financial freedom and foreign direct investment were analyzed. They were measured according to the IEF indicators of The Heritage Foundation in 2021, which measures the market opening of the countries, which are described below:

• Business freedom (BF), where the IEF takes the Doing Business index, which measures the ease with which a company can open a business from a regulatory and infrastructure point of view based on the 13 subfactors determined by the World Bank.

• Labor Freedom (LF), also taken from the IEF, measures the regulatory framework of the countries' labor market and includes regulations related to wages, laws that prohibit dismissals, compensation regulations, hiring, and hours at work.

• Monetary freedom (MF), which combines inflation with a series of government activities where they control market prices, such as subsidies. 0

• Commercial freedom (CF) seeks to measure the scope of tariff and non-tariff barriers that influence exports and imports of goods and services; it has two indicators; the weighted average tariff rate and a qualitative assessment of non-tariff barriers.

• Investment freedom (IF), which measures that there are no restrictions on investment flows, means that capital resources can be moved within and outside the country in specific activities within the financial system of a country.

• Financial Freedom (FF) measures how efficient the banking system is and its independence from government control, reducing competition and credit access.

• Foreign Direct Investment (FDI) is the flow of capital made by multinational companies in countries with activities that generate market value.

• Dependent variables. To analyze the effects of the opening of the market on economic development and human development, the following variables were taken:

• Per capita Gross Domestic Product (BFGDPPC), which measures the productivity of a country and was taken with data from the World Bank, to smooth the observations and adjust them to a normal distribution, the natural logarithm was applied.

• The Human Development Index (BFHDI) is the indicator of the United Nations Development Program (UNDP), which has three dimensions: life expectancy and health, knowledge, and decent standard of living; As in the case of the previous dependent variable, the variable to be generated was transformed with the natural logarithm.

Analysis of Data

For the data analysis and prior to it, the relevance of developing a data panel was established; first, an analysis of bivariate correlations was made (Table 1). The independent variables business freedom, labor freedom, commercial freedom, freedom investment, financial freedom, and foreign direct investment have a positive and significant relationship greater than 0.01 with economic growth. Monetary freedom is positively related, but it is only significant at 0.05. When analyzing the relationships of the Human Development Index, only labor freedom has a negative relationship with a significance level of 0.05. Investment freedom and monetary freedom fail to reach significance levels that can explain any relationship.

They began with estimating OLS and random effects, and the Lagrangian multiplier was obtained. and as Table 2 depicts, both in the models with the dependent variable of economic growth and in the Human Development Index, there is a level of 0.01, so it is concluded that there is unobserved heterogeneity, and it is recommended to use panel data models. Thus, the Pesaran test was also applied, resulting in levels of 0.01, which indicates that using the OLS estimation is not a viable option and confirms the need to use the panel data technique. That is why it was considered to continue the random effects since the Hausman test in the models of both dependent variables turned out to be significant: 0.01.

In addition, the results of the Wald test (Wooldridge, 1990) were obtained. They show the presence or absence of heteroscedasticity and autocorrelation, they turn out to be significant; therefore, the regressions had to be run with generalized least squares standard error corrections. (MSGLS) and self-correction of standard errors to exceed the estimates in heteroscedasticity and autocorrelation (Table 2).

Table 1: Correlations matrix

	LNGDPPC	BFFDI	BFHDI	BF	LF	MF	CF	IF	FF
BFGDPPC	1								
BFFDI	0.177***	1							
BFHDI	0.877***	0.272***	1						
BF	0.446***	0.0514	0.503***	1					
LF	0.308***	-.1203**	0.263***	0.433***	1				
MF	0.126**	0.022	0.092	0.421***	0.366***	1			
CF	0.282***	0.303***	0.269***	0.174***	0.0685	0.399***	1		
IF	0.240***	0.066	0.246***	0.322***	0.171***	0.581***	0.528***	1	
FF	0.366***	0.320***	0.391***	0.2987***	0.0898**	0.4537***	0.589***	0.648***	1

Source: Own elaboration. Nota: *, **, *** represents 0.1, 0.05, 0.01 significance levels.

From the results presented in Table 2, the following discoveries can be highlighted: models with Prais-Winsten estimation (Park & Mitchell, 1980) of random effects were developed to evaluate the linear trends to correct the autocorrelation (model 2), which shows that the variables Business Freedom with a significance level of 0.01, Labor Freedom with a significance level of 0.01, Financial Freedom with a significance level of 0.01 and Foreign Direct Investment with a significance of 0.10, create positive effects on human development. So, this model is the one that best explains, but it could not be assumed that hypothesis 1 is verified. This is because running the model with robust results with error correction standards cannot have significant variables.

On the other hand, when analyzing the economic development of emerging countries, it can be seen in Table 3 that in model 5, where the standard error corrections are presented, it can be seen that the variables with the greatest significance (0.01) are Freedom of business, labor freedom, investment freedom, financial freedom and Foreign Direct Investment (0.05 significance), and investment freedom without significance. It is worth noting that the monetary freedom variable has a negative effect, which suggests that there must be greater controls on central banks regarding their monetary policy.

To correct the heteroscedasticity and autocorrelation of the dependent variable model, a generalized least squares model (Model 6) was generated and the STATA command xtpcse was developed, where it turns out that monetary freedom negatively impacts economic development and commercial freedom is not significant with the generalized least squares model, while in the autocorrelation correction for standard errors, monetary freedom, commercial freedom and foreign direct investment are not significant; Therefore, hypothesis 2 is verified.

Table 2. Human Development Index (HDI) Index

	Model 1	**Model 2**	**Model 3**
	Coef.	Coef.	Coef.
BF	0.0003576*	0.0013775***	-0.000133
LF	0.0003925**	0.0009208***	-0.0000288
MF	0.000822***	-0.0003454	0.0000636
CF	0.0006142***	0.000301	0.0001078
IF	0.0007407***	0.0002776	0.0000414
LF	0.0002504	0.0015138***	-0.0002662
BFFDI	0.0012921	0.0013617*	0.000294
Const	6.372626***	6.349169***	6.245876
chi^2	0.000	72.92***	
Breush & Pagan Lagrangian Multiplier test	1310.33***		
Wald test			
Wooldridge test	14.505***		
Hausman	1503***		
F			15.379***
Pesaran test	27.948***		
Observations	465	465	405

Source: Own elaboration. Note: *, **, *** represents 0.1, 0.05, 0.01 significance levels.

Table 3. Human Development Index (HDI) Index

	Model 4	Model 5	Model 6	Model 7
	Coef.	Coef.	Coef.	
BF	0.0056532*	0.0252466***	0.0256171***	0.0131287***
LF	0.0051752*	0.0138726***	0.0103326***	0.0078443***
MF	0.0035053	-0.0237425***	-0.0241665***	-0.0033394
CF	0.0065725**	0.0117392***	0.0021688	0.003689
IF	0.0106745***	0.0006596	0.0068906***	0.0025074
LF	0.0013268	0.013684***	0.0089245***	0.0121214***
BFFDI	-0.0048532	0.0242972**	0.0501688***	-0.0027729
Const	7.37133***	6.952549***	7.555564***	7.355881***
chi^2	47.1***	215.87***	606.83***	81.29***
Breush y Pagan Lagrangian multiplier test	50.697***			
Wald test	9927.38***			
Wooldridge test				
Hausman	15.03***			
Pesaran test				
Observations	465	465	465	465

Source: Own elaboration. Note: *, **, *** represents 0.1, 0.05, 0.01 significance levels.

Conclusions and Implications

This study focuses on the analysis of economic freedom as one of the variables comprising trade openness, ease of investing and doing business, financial freedom, monetary freedom, and labor freedom (Arel-Bundock, 2017), which could explain economic growth and, in turn, impact human development in developing countries (Arel-Bundock, 2017; Huynh, 2022; Amir & Mehmood, 2012; Nikolov, 2016). However, in this study, there was no evidence that these variables explain human development in a concrete way.

On the other hand, in the 1990s, several emerging countries underwent a process of economic transition; they went from having an authoritarian political system to one based on democracy and globalization, where, at first, it was thought that it was pertinent that the citizens of poor countries had lost their well-being to prop up growth in the medium- and long-term (Praščević, 2013). However, three decades have passed, and a large number of these countries are still waiting for development that is reflected in better jobs, education, health, infrastructure, and other factors that improve their quality of life. However, empirical evidence shows that some countries, especially in Asia, present more equitable growth explained by inverted Kuznets (Huynh, 2022).

This is not widespread in emerging countries; it can be accepted that globalization can improve the competitiveness of nations and, therefore, their economic development. There is a need to create the necessary conditions to attract foreign direct investment, improve the conditions for national investment, create open and equitable trade policies, and, in turn, have a modern financial and labor market since all this has been found. impacts productive activities and value creation from both economic and social points of view (Caseiro & Masiero, 2014; Maciągowska & Kołtuniak, 2016; Knoerich, 2017; Egu & Aregbeshola, 2017; Noor et al. 2016; Nwaolisa & Francis, 2018), but there is still a need to find a theoretical model that explains the phenomenon analyzed in the present investigation; therefore, in future investigations, it is proposed to add different variables such as corruption, spending government, and the quality and level of education of the population, among others, so it is necessary to seek greater theoretical support.

One limitation is that only the institutional framework is considered, and different theoretical approaches can explain the development of countries. Another element rarely mentioned in this document is the cultural environment, which would be important to study to understand what impacts national culture can have on the economic sphere.

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