THE INFLUENCE OF GOVERNMENTAL INSTITUTIONS ON THE LIKELIHOOD OF AN INDIVIDUAL BECOMING AN ENTREPRENEUR (INTERACTIVE PAPER)

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INTERACTIVE PAPER

THE INFLUENCE OF GOVERNMENTAL INSTITUTIONS ON THE LIKELIHOOD OF AN INDIVIDUAL BECOMING AN ENTREPRENEUR

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Principal Topic

Although the decision to become an entrepreneur is an individual one, institutional factors are likely to influence the decision of an individual concerning whether or not to become an entrepreneur. It has been argued that increasing levels of economic freedom is an effective means to promote productive entrepreneurial activity (Gwartney and Lawson, 2002). In market-based economies with high levels of economic freedom, entrepreneurs may pursue economic profit by addressing consumer desires. Conversely, economies with high taxes, heavy regulations, trade restrictions, and a lack of property rights raise the cost of doing business, making pursuing such opportunities less attractive. In economies lacking economic freedom, opportunities for rent-seeking could yield higher returns than value-creating entrepreneurial opportunities (Kreft and Sobel, 2005), and higher levels of rent-seeking activities are likely to be observed. However, economies with high levels of economic freedom are more likely to have individuals engaging in productive entrepreneurship instead. In this paper, we investigate the following research question: How does economic freedom impact the level of self-employment in an economy?

Methods

To answer this question, we collect self-employment, unemployment, and per capita GDP data from 34 OECD countries. This data is matched with the Fraser Institute Economic Freedom of the World index. OLS regression is used using the self-employment rate as the dependent variable, with per capita GDP, unemployment rate, and the various components of the Fraser Institute Economic Freedom of the World index as the independent variables. Country and year fixed effects are included as well.

Results and Implications

Our preliminary results show that several components of economic freedom are significantly related to the level of self-employment. Small government size, sound money, freedom to trade internationally, property rights, and low levels of employment regulation were positively associated with the level of self-employment in an economy. This research highlights the important influence that institutions can have on many aspects of an economy, including the level of self-employment.

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