

Executive Summary

Economic Freedom of the World

The index published in *Economic Freedom of the World* measures the degree to which the policies and institutions of countries are supportive of economic freedom. The cornerstones of economic freedom are personal choice, voluntary exchange, freedom to compete, and security of privately owned property. Thirty-eight data points are used to construct a summary index and to measure the degree of economic freedom in five areas: (1) size of government; (2) legal structure and security of property rights; (3) access to sound money; (4) freedom to trade internationally; and (5) regulation of credit, labour and business.

Economic freedom has grown considerably in recent decades

- ◆ The chain-linked summary index (exhibit 1.5) permits comparison over time. The average economic freedom score rose from 5.1 (out of 10) in 1980 to 6.5 in the most recent year for which data are available. Of the 102 nations with scores in 1980 and in the most recent index, 98 recorded improvements in their economic freedom score, four saw a decline.
- ◆ Of the five nations that have increased their score by more than 3 points since 1980, two are in Africa. The five nations in order of gain are Ghana, with the largest increase of 4.0 points, Israel, Uganda, Jamaica, and Hungary. These nations began at a low point of economic freedom and must continue to make progress to enjoy the full benefits of economic freedom. The nations that have registered losses in economic freedom since 1980 are Venezuela, with the largest fall of 2.6 points, Zimbabwe, Myanmar, and the Republic of Congo.
- ◆ In this year's index, Hong Kong retains the highest rating for economic freedom, 8.7 out of 10, followed by Singapore at 8.5. New Zealand, Switzerland, and the United States tied for third with ratings of 8.2. Ireland and the United Kingdom are tied for 6th at 8.1. Canada ranked 8th with a rating of 8.0. Iceland and Luxembourg are tied for 9th at 7.9. The rankings of other large economies are Germany, 17; Japan, 19; France, 24; Italy, 45; India, 53; Mexico, 60; Brazil, 88; China, 95; and Russia, 102. (Exhibit 1.2)
- ◆ The majority of nations ranked in the bottom fifth are African, with the most of the remainder from Latin American and former communist states. Botswana's ranking of 35 is the best among continental sub-Saharan African nations. Chile, at 20, has the best record in Latin America. The bottom 10 nations are Zimbabwe, Myanmar, the Republic of Congo, the Democratic Republic of Congo, Venezuela, Guinea-Bissau, Algeria, Burundi, Rwanda, and the Central African Republic. However, a number of other nations for which data are not available, such as North Korea and Cuba, may have even less economic freedom.

Nations that are economically free out-perform non-free nations in indicators of well-being

- ◆ Nations in the top quartile of economic freedom have an average per-capita GDP of US\$24,402, compared to US\$2,998 for those nations in the bottom quartile. (Exhibit 1.6)
- ◆ The top quartile has an average per-capita economic growth rate of 2.1%, compared to minus 0.2% for the bottom quartile. (Exhibit 1.7)

- ◆ Unemployment in the top quartile averages 5.9%, compared to 12.7% in the bottom quartile. (Exhibit 1.8)
- ◆ Life expectancy is 77.8 years in the top quartile compared to 55.0 years in the bottom quartile. (Exhibit 1.9)
- ◆ In nations of the top quartile, only 0.3% of children are in the labor force, compared to 19.3% in the least economically free nations. (Exhibit 1.11)
- ◆ In nations of the top quartile, the average income of the poorest 10% of the population is US\$6,519, compared to \$826 for those in the bottom quartile. (Exhibit 1.14)
- ◆ Nations in the top quartile of economic freedom, have an average score of 1.8 for political rights on a scale of 1 to 7, where 1 marks the highest level of freedom and 7, the lowest level. The bottom quartile has an average score of 4.6. (Exhibit 1.16)

Freedom versus Collectivism in Foreign Aid

The United Nations and other bodies have called for more foreign aid to help lift developing nations out of poverty. These groups believe increased aid is necessary to meet the United Nations Millennium Development goals, which include promoting growth, providing universal education, reducing the spread of HIV/AIDS, and halving extreme poverty. Yet, the demand for foreign aid is typically made in the absence of any empirical evidence that it leads to benefits for recipient nations and without asking whether there are better approaches to poverty reduction for the international community to support. In Chapter 2, William Easterly of New York University examines these issues.

- ◆ A key argument for increased foreign aid invokes the “poverty trap.” Proponents argue that a lack of capital and an inability to acquire capital because of desperate poverty prevents even those nations with good policy from advancing. A “Big Push” is required by outside donors.
- ◆ Foreign aid has no positive impact (and possibly a negative impact) on economic growth in the poorest nations (Table 3). This indicates that the “push” from foreign aid is ineffective in breaking the “poverty trap.”
- ◆ On the other hand, economic freedom has a strong and positive impact on prosperity in general (Table 1) and on helping lift nations out of poverty (Table 3).
- ◆ Easterly shows that, once economic freedom is taken into account, poor nations, far from being caught in a “poverty trap,” grow faster than rich nations.” Moreover, the results suggest that foreign aid may hinder growth, though Prof. Easterly cautions that further research is required to investigate this result.
- ◆ A key component of the success created by economic freedom is the ability to experiment, find economically successful areas of production, and prune those that do not succeed so that resources may be transferred to where they are most productive.

Data Available to Researchers

The full data-set, including all of the data published in this report as well as data omitted due to limited space, can be freely downloaded at <<http://www.freetheworld.com>>. If you are using the data across time periods, it would be better to use the chain-link series presented in Chapter 1, Exhibit 1.5, and available at the website, for reasons outlined in that chapter. If you have any difficulties downloading the data, please feel free to contact us via e-mail to freetheworld@fraserinstitute.ca or via telephone at +1.604.714.4563.