

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 support economic freedom. The cornerstones of economic freedom are personal choice, voluntary exchange, freedom to compete, and security of privately owned property. Forty-two data points are used to construct a summary index and to measure the degree of economic freedom in five broad 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, labor and business. This year's index includes a number of new components based on the World Bank's *Doing Business* ratings.

In the past year, more data has become available and, so, 11 new jurisdictions have been added to the 130 jurisdictions in last year's index. They are: Angola, Bosnia and Herzegovina, Burkina Faso, Ethiopia, Kazakhstan, Kyrgyz Republic, Lesotho, Mauritania, Moldova, Montenegro, and Serbia.

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 5.4 (out of 10) in 1980 to 6.6 in 2005, the most recent year for which data are available.
- ◆ Of the 102 jurisdictions with scores in the chain-link index in 1980 and in the most recent index, 90 had increases in score, nine had decreases in scores, and three had the same score, when changes are rounded to one decimal point.
- ◆ Five nations increased their score by more than three points since 1980: Hungary (3.0), Peru (3.0), Uganda (3.2), Ghana (3.6), and Israel (3.7). Only three nations decreased their score by more than one point: Zimbabwe (-1.7), Venezuela (-1.7) and Myanmar (-1.3). Other nations that saw reductions are: Nepal (-0.7), Bahrain (-0.3), Hong Kong (-0.2), Malaysia (-0.2), the Republic of Congo (-0.2), and Haiti (-0.1).
- ◆ In this year's main index, Hong Kong retains the highest rating for economic freedom, 8.9 out of 10. The other top scorers are: Singapore (8.8), New Zealand (8.5), Switzerland (8.3), Canada (8.1), United Kingdom (8.1), United States (8.1), Estonia (8.0), Australia (7.9), and Ireland (7.9).
- ◆ The rankings of other large economies are Germany, 18 (7.6); Japan, 22 (7.5); Mexico, 44 (7.1); France, 52 (7.0); Italy, 52 (7.0); India, 69 (6.6); China, 86 (6.3); Brazil, 101 (6.0); and Russia, 112 (5.8).
- ◆ The majority of nations ranked in the bottom fifth are African and all the nations in the bottom 10 are African, with the exceptions of Venezuela and Myanmar. They are: Zimbabwe (2.9), Myanmar (3.8), the Democratic Republic of the Congo, (4.0), Angola (4.2), the Republic of the Congo, (4.3), Central Africa Republic, (4.6), Venezuela (4.9), Burundi (5.0), Chad (5.1), and Niger (5.1). Botswana's ranking, tied for 39th with a score of 7.2, is the best among continental sub-Saharan African nations.

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\$26,013, compared to US\$3,305 for those nations in the bottom quartile (exhibit 1.6).
- ◆ The top quartile has an average per-capita economic growth rate of 2.25%, compared to 0.35% for the bottom quartile (exhibit 1.7).
- ◆ In nations of the top quartile, the average income of the poorest 10% of the population is US\$7,334, compared to \$905 for those in the bottom quartile (exhibit 1.10).
- ◆ Life expectancy is 78.7 years in the top quartile but 56.7 years in the bottom quartile (exhibit 1.11).
- ◆ 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, while those in the bottom quartile have an average score of 4.4 (exhibit 1.18).
- ◆ Nations in the top quartile of economic freedom have an average score of 1.7 for civil liberties on a scale of 1 to 7, where 1 marks the highest level, while those in the bottom quartile have an average score of 4.1 (exhibit 1.18).
- ◆ Nations in the top quartile of economic freedom have an average score of 81.0 (out of 100) for environmental performance, while those in the bottom quartile have an average score of 58.9 (exhibit 1.19).

The Spread of Global Economic Freedom

Global foreign policy has been strongly grounded in the idea that freedom, including economic freedom, spreads among countries. Russell S. Sobel and Peter T. Leeson, in Chapter 2, search for spatial dependence in economic freedom between geographic neighbors and trade partners using a panel of more than 100 countries between 1985 and 2000. Their results confirm that economic freedom does indeed spread through both geography and trade: both a country's levels of economic freedom and changes in its economic freedom are affected by levels and changes in neighbouring countries and its trading partners.

- ◆ Both levels of economic freedom and changes in it spread at about the same rate through both geography and trade. Countries “catch” about 20% of their average geographic neighbors’ and trading partners’ levels of, and changes in, economic freedom. This result is remarkably robust to alternative specifications and estimation techniques.
- ◆ Although these results provide strong evidence that freedom spreads, they also suggest freedom does not spread as strongly as suggested by the “domino theory” that underpinned American and Soviet foreign relations during the Cold War. The idea that reforms within a few key nations would substantially alter the state of economic freedom in the rest of a region does not appear to be correct.

Policy implications

While it is important to be cautious in drawing policy implications from the analysis, the results suggest significant conclusions.

- ◆ While changes in the economic freedom in one country have only a modest impact on neighboring countries, when multiple neighbors experience simultaneous changes in economic freedom, the impact is much greater. Thus broad regional changes in freedom can and do have significant impacts on surrounding countries.

- ◆ By liberalizing their trade with foreign nations, economically free countries can exert at least a modest positive impact on economic freedom in less free nations. While the effect of trade liberalization with any one country is relatively small in terms of the broader impact on other neighbors, free-trade agreements that allow a number of nations to simultaneously coordinate trade liberalization could have a sizeable influence on spreading economic freedom.

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.

