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. 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: Expenditures, Taxes, and Enterprises;
2. Legal Structure and Security of Property Rights;
3. Access to Sound Money;
4. Freedom to Trade Internationally;
5. Regulation of Credit, Labor, and Business.

Economic freedom has suffered its first setback in decades

- The chain-linked summary index (exhibit 1.4) permits comparisons over time. The average economic-freedom score rose from 5.53 (out of 10) in 1980 to 6.74 in 2007, but fell back to 6.67 in 2008, the most recent year for which data are available. This is the first retreat for global economic freedom in decades. (See chapter 1 for a discussion.)

- In this year's index, Hong Kong retains the highest rating for economic freedom, 9.05 out of 10. The other top 10 nations are: Singapore (8.70), New Zealand (8.27), Switzerland (8.08), Chile (8.03), United States (7.96), Canada (7.95), Australia (7.90), Mauritius (7.82), and the United Kingdom (7.81).

- The rankings (and scores) of other large economies are Germany, 24 (7.46), Japan 24 (7.46), France 35 (7.32), Italy 66 (6.90), Mexico 69 (6.89), Russia 84 (6.62), China 82 (6.65), India 87 (6.51), and Brazil 102 (6.18).

- The bottom ten nations are: Zimbabwe (3.57), Myanmar (3.81), Angola (3.89), Venezuela (4.33), Congo, Republic of (4.75), Congo, Democratic Republic (4.93), Central African Republic (4.77), Guinea-Bissau (4.82), Burundi (4.91), and Algeria (5.00).

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

- Nations in the top quartile of economic freedom had an average per-capita GDP of $32,744 in 2007, compared to $3,858 for those nations in the bottom quartile in constant 2005 international dollars (exh. 1.6).

- In the most-free quartile, the average income of the poorest 10% of the population was $8,474 compared to $910 for those in the least-free quartile, in constant 2005 international dollars (exh. 1.9). Interestingly, the average income of the poorest 10% in the most economically free nations is more than double the overall average income in the least free nations.

- Life expectancy is 79.3 years in the most-free quartile but 59.9 years in the least-free quartile (exh 1.10).
- People in nations in the most-free quartile report a life satisfaction of 7.5 out of 10 while those in the least-free quartile report a life satisfaction of 4.7 (exh. 1.11).
- Nations in the most-free quartile have an average score of 7.4 for corruption on a scale of 10, while those in the least-free quartile have an average score of 2.6 (exh. 1.12).
- Nations in the top quartile have an average score of 1.6 for political rights and civil freedoms on a scale of 1 to 7, where 1 marks the highest level, while those in the bottom quartile have an average score of 4.3 (exh. 1.13).

Chapter 1: Economic Freedom of the World, 2008

The principal authors of the report, James Gwartney (Florida State University), Robert Lawson (Auburn University), and Joshua Hall (Beloit College), review the causes of the financial crisis and the recession. They also discuss the policy responses and the political processes out of which those responses grew, and how these processes may favor government intervention and a reduction in economic freedom, which perversely is likely to extend the recession. They warn that this path over the longer term would lead to loss of economic growth and vibrancy. This highlights the importance of an objective economic freedom measure to bring accountability to the debate. The authors also review the history of the economic freedom project and describe the construction of the index.

Chapter 2: Country Data Tables

Detailed historical information is provided for each of the 141 countries and territories in the index.

Chapter 3: How Are Institutions Related?

Christopher Coyne (George Mason University) and Russell Sobel (West Virginia University) analyze the nature of institutional reform using data on different measures of each country's many economic and political institutions. They ask both whether some institutions are easier to permanently change than others, and whether sets of institutions must be reformed simultaneously for the changes to become permanent. The main results are: (1) that most formal, economic institutions (e.g., tax and regulatory structures) can be permanently reformed but that legal and rights-based informal institutions (e.g., civil rights or Area 2: Legal Structure and Security of Property Rights) tend to resist permanent change; and (2) that economic institutions are cointegrated and therefore must move together to obtain permanent change—some institutions simply cannot be changed in isolation. In terms of policy, this implies that over the long term, reforms to one set of institutions are more likely to become permanent if reforms to other institutions are also undertaken. To achieve meaningful advances in economic freedom, countries must undertake simultaneous reform to the different areas of the index, rather than trying to change one at a time. Changes to one area in isolation tend to decay back to prior levels unless accompanied by changes in other areas.

Chapter 4: Macroeconomic Volatility and Economic Freedom: A Preliminary Analysis

John Dawson (Appalachian State University) examines the empirical relationship between business-cycle volatility and economic freedom across countries. In a diverse sample of 85 countries, the results suggest a significantly negative relationship between volatility and a broad measure of freedom—even after controlling for other determinants of cross-country volatility and using an instrumental variables procedure to account for the likely endogeneity of economic

freedom. Among the underlying components of the freedom index, all but the size of government also have a significantly negative relationship with volatility; that is, in these areas, economic freedom reduces volatility. Size of government is found to have a significantly positive relationship with volatility. Measures of changes in freedom and the volatility of freedom are found to be statistically insignificant, suggesting that freedom is not among the shocks that cause business cycles. Rather, freedom appears to allow economies to better adjust to those shocks that drive business cycles.

Chapter 5: Economic Freedom and Unemployment

Horst Feldmann (University of Bath) examines the relationship between economic freedom and unemployment. According to his regression results, more economic freedom appears to reduce unemployment. The magnitude of the effect seems to be substantial, especially among young people. Given the large costs of unemployment and the enormous number of jobless people worldwide, particularly in the wake of the current financial and economic crisis, governments should consider increasing economic freedom as a means of reducing unemployment. To illustrate the magnitude of the effects, Feldmann compares the United States and Italy and finds that, if Italy had enjoyed the same degree of economic freedom as the United States, its unemployment rate might have been 1.7 percentage points lower among the total labor force and between 3.5 and 3.9 percentage points lower among youth, other factors being equal.

Chapter 6: The Relationship between Economic Freedom and Homicide

Edward Peter Stringham (Fayetteville State University) and John Levendis (Loyola University New Orleans) consider the question: Does economic freedom lead to more or less conflict? Numerous authors argue that markets create conflict, whereas many advocates of economic freedom from Adam Smith to Milton Friedman argued the opposite. Stringham and Levendis examine the various ideas about why economic freedom may reduce conflict and why government intervention might increase it. Then, they look at cross-national data to determine whether measures of markets and homicides are correlated and find that, in a cross section of countries, measures of economic freedom are significantly and negatively correlated with homicide rates. These results hold under various tests for robustness. Increases in economic freedom do appear to be associated with decreases in homicide rates.

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 downloaded for free at <http://www.freetheworld.com/release.html>. The data file available there contains the most up-to-date and accurate data for the Economic Freedom of the World index. Some variable names and data sources have evolved over the years since the first publication in 1996; users should consult earlier editions of the *Economic Freedom of the World* annual reports for details regarding sources and descriptions for those years. All editions of the report are available in PDF and can be downloaded for free at <http://www.freetheworld.com>. However, users are always strongly encouraged to use the data from this most recent data file as updates and corrections, even to earlier years' data, do occur. Users doing long-term or longitudinal studies are encouraged to use the chain-linked index as it is the most consistent through time. If you have problems downloading the data, please contact Jean-François Minardi via e-mail to <freetheworld@fraserinstitute.org> or via telephone +1.514.281.9550 ext. 306. If you have technical questions about the data itself, please contact Robert Lawson (e-mail: <rlawson@auburn.edu>; telephone: +1.334.844.3007) or Joshua Hall (e-mail: <joshua.c.hall@gmail.com>; telephone: +1.608.363.2376). Please cite the data set as:

> Authors: James D. Gwartney, Joshua C. Hall, and Robert Lawson
> Title: 2010 Economic Freedom Dataset, published in *Economic Freedom of the World: 2010 Annual Report*
> Publisher: Fraser Institute
> Year: 2010
> URL: <http://www.freetheworld.com/release.html>