

Economic Freedom:
Toward a Theory of Measurement

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Economic Freedom: Toward a Theory of Measurement

Proceedings of an International Symposium

Edited by Walter E. Block

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The Fraser Institute
Vancouver, British Columbia, Canada

Proceedings of an International Symposium on Measuring Economic Freedom, held July 28-30, 1988, in Vancouver, British Columbia. This event is part of the programme of Liberty Fund Inc., under the direction of its President, Dr. W.W. Hill. This Symposium was managed by The Fraser Institute and organized by Senior Research Fellow Dr. Walter E. Block.

Canadian Cataloguing in Publication Data

Main Entry under title:

Economic Freedom

Symposium held July 28-30, 1988 in Vancouver, BC

Includes bibliographical references.

ISBN 0-88975-129-3

1. Free enterprise—Congresses. 2. Liberty—Congresses.
3. Comparative economics—Congresses.
4. Economics—Methodology—Congresses. I. Block, Walter, 1941-
II. Fraser Institute (Vancouver, BC)

HB95.E36 1990 330.12'2 C90-091722-9

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Printed in Canada.

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PREFACE

This is the second book in the Fraser Institute's liberty project. It is based on the proceedings of a colloquium held in Vancouver, in July 1988. The first book, *Economic Freedom, Democracy and Welfare*, is similarly based on the proceedings of a conference that took place in Napa Valley, California, in October 1986.

The connection between the books in this series is more intimate than usual. Each tome builds on the groundwork set by its predecessors and serves as a foundation for its successors. The Fraser Institute has published other multi-volume series: on housing, health, and anti-combines legislation, the Reaction series, and most recently, the Service Sector Project. In all of publications, each work is connected to the larger study, yet each can stand entirely on its own.

This, however, is not true in the present case. So strong is the link between the first two products of the liberty project that the entire first section of *Economic Freedom: Toward a Theory of Measurement* is based on a discussion of *Freedom, Democracy and Economic Welfare*. Dr. Michael Walker, editor of the latter volume and director of the Fraser Institute, begins chapter 1 of this book with an overview of its predecessor. In his discussion Walker touches on how the liberty project was begun, and explains some of the underlying techniques for and the importance of a system of rating economic freedom. In short, the liberty project is an attempt to do no less for economic freedom than what Freedom House does for political freedom: to calculate the amount that exists in the various nations of the world. In addition, Walker summarizes how governments of all five continents are encroaching upon the ability of the citizenry to engage in economic activity and to keep the fruits of their efforts. The remainder of chapter 1 is a spirited discussion of these concepts with the distinguished panel of conference participants.

Chapter 2 presents the philosophical aspects of Alvin Rabushka's monumental study of economic liberty. This Hoover Institution scholar, an expert in taxation and the economics of countries in the Asian Pacific, begins his analysis right where it belongs: with the philosophical roots of economic liberty. He surveys the writings of some of the most influential and visionary contributors to this tradition, starting with the work of John Locke, an originator of the private property basis of free enterprise philosophy. Although somewhat suspicious of Locke's reliance on majoritarian democracy, Rabushka focuses on

his important contributions to government limitations and homesteading as the source of private property rights.

Next comes Milton Friedman, who Rabushka characterizes as a “modern-day John Locke.” He focuses particularly on the Friedmans’ book *Free to Choose* which makes the case that economic freedom is a necessary but not sufficient condition for political freedom—the departure point of the Fraser Institute’s entire liberty project. Milton and Rose Friedman respond in discussing the proper limited role of government, forcefully maintaining that when the public sector exceeds these bounds, it violates an economic “bill of rights.”

Rabushka concludes his discussion with the work of Murray N. Rothbard, who has been called the father of libertarianism, in order to present what some consider “the cleanest, purest exposition of the principle of economic freedom.” Rabushka presents this natural rights, free market, anarchist position not because he goes along with the view that literally all government activity should be privatized, but in order to establish an end point to the free market continuum. With this provocation, the ensuing discussion was wide ranging and high spirited. Some topics covered in greater depth were utilitarianism, alternative definitions of economic freedom and property rights, the plight of Hong Kong, the restructuring of socialism, libertarian theory, Rothbardianism, the conceptual difficulties of measuring freedom, noise and air pollution, and institutional stability.

Chapter 3 is devoted to Alvin Rabushka’s analysis of the Freedom House survey of economic freedom. Although primarily associated with rating political liberty, this organization has recently concerned itself with economics. But the experiment has not proven successful to date, according to Rabushka and the panel’s participants. The major criticism is that Freedom House conflates economic freedom and democracy. For example, if a polity votes for rent control, minimum wages, and tariffs in an open and free election, then according to Freedom House calculations, these laws, which would otherwise have been considered paradigm cases of the denial of economic freedom, somehow become freedom-enhancing. Particularly unsatisfactory in this regard is the linkage between unionism and economic freedom.

In chapter 4 a preliminary definition of economic freedom is attempted. Based on Rabushka’s analysis and the consensus of the conference participants, the following definition emerged: at the core of economic freedom is an appreciation of the institution of private property, whether in human or physical capital, and the right to trade. It applies pre-eminently to individuals, not to political or other groups or majorities. It is consistent with the necessarily coercive role of the state, but only if government actions, and the taxes imposed in order to accomplish them, are severely and strictly limited. Economic regulation and public ownership of economic activity are therefore highly dangerous to a regime grounded in economic liberty. The discussion focused on

seven critical categories: private property, the rule of law, taxation, government spending, regulation of business and labour, monetary policy, and free trade. Among the most disputatious issues were the role of government in the provision of money, anti-trust legislation, “voluntary” taxation, the regulation of externalities such as air and water pollution, and food and drug and occupational safety legislation. As well, there was the highly controversial methodological issue of whether economic freedom is “out there” just waiting to be measured, or whether it is a concept that can help us explain and understand economic reality better.

Chapter 5, written by Zane Spindler and Laurie Still, is our first attempt to quantify the analysis. They create an index of economic freedom that encompasses such criteria as conscription, privatization, public sector involvement, profit repatriation, import restrictions, foreign ownership, infrastructure, licensing, taxes, banking regulations, military conflict, government stability, trade barriers, investment incentives, bureaucracy, labour relations, deregulation, and price and exchange controls. Then they apply this index to 145 countries, where a rating of 1 indicates a high degree of freedom, and 5 a low degree. On this basis, countries such as Cayman Islands (1.25), Costa Rica (1.00), Australia (1.62), Austria (1.60), Belgium (1.71), Denmark (1.87), Fiji (1.50), Great Britain (1.33), Hong Kong (1.14), Liechtenstein (1.25), Singapore (1.37), St. Lucia (1.33), Swaziland (1.25), and the U.S. (1.81) are amongst the freest in the world, while Afghanistan (4.14), Albania (4.20), Bulgaria (4.30), Cuba (4.75), Czechoslovakia (5.00), East Germany (4.50), Iran (4.60), Iraq (4.28), North Korea (5.00), Laos (4.33), Rumania (4.00), Vietnam (4.20), and Yugoslavia (4.00) are the least free.

The critical discussion that greeted these findings ranged far and wide. Several of the criteria used in the index were questioned, such as the claim that the freedom to form restrictive associations impinges on the rights of others to free access. There was consensus, however, on Milton Friedman’s point that at bottom, civil liberties can be reduced to economic liberties.

The Fraser Institute has had a deep and long abiding interest in the analysis of economic freedom. By publishing this volume we hope to encourage wider discussion of this topic and move toward that day when the economic liberties of the nations of the world may be more meaningfully measured. However, the authors and contributors to this volume have conducted their research independently, and the views they express may or may not conform singly or collectively with those of the members of the Fraser Institute.

Chapter 1

Setting the Scene: A Discussion of *Freedom, Democracy and Economic Welfare: Proceedings of an International Symposium*

Michael Walker

This discussion is the second in what shall be a series of five symposia on rating economic freedom. Let me give you a little background on this project. I was asked to participate in the 1984 meetings of the Mont Pèlerin Society at Cambridge, England, and to comment on “1984—A False Alarm,” a paper by journalist and historian Paul Johnson which claimed that George Orwell’s predictions for the demise of democracy had proved to be too pessimistic. In commenting on Johnson’s paper, I raised a number of points that I thought demonstrated the accuracy of Orwell’s analysis, even if he had been wrong in the extent to which the totalitarian forces would exert themselves by 1984.

For example, the increase in the aggregate tax rate borne by citizens in Western democracies is closely connected to the decline of their ability to individually control their economic destinies. The use of social insurance numbers to trace every financial transaction in which individuals engage has increasingly exposed private affairs to the potential scrutiny of the state. The fact that one economic transaction subject to scrutiny is contributions to political parties led me to note that this intrusiveness of the state might eventually challenge the political freedom that, in Western democracies, we take for granted. Ultimately, it is the wide dispersal and availability of financial resources that enable citizens to challenge the political power of governments. In other words, I opined that there are connections between the extent of economic freedom, the dispersal of economic purchasing power, and the extent of political freedom enjoyed by people.

2 Michael Walker

In support of that comment, I naturally referred to the famous passage in *Capitalism and Freedom*, written by Milton Friedman with Rose Friedman, in which the authors note that

historical evidence speaks with a single voice on the relation between political freedom and a free market. I know of no example in time or place of a society that has been marked by a large measure of political freedom, and that has not also used something comparable to a free market to organize the bulk of economic activity.

At the meeting in Cambridge, there then ensued a discussion about the relationship between economic and political freedom. It became clear during the course of this discussion that while Milton and Rose Friedman's comment had been extant for more than several decades, there had been no serious attempt to explore the relationship between economic and political freedoms in a scholarly way. I decided at that time that such a discussion should be undertaken and was able to convince Rose and Milton Friedman to co-host a symposium to investigate these relationships. This event, the first in the series, was held in Napa Valley, California, in 1986. The proceedings were published in *Freedom, Democracy and Economic Welfare*, Vancouver: The Fraser Institute, 1988.

In discussion, it soon became clear that the focus of the symposium should be somewhat broader than economic and political freedoms. As Milton Friedman noted at the time, in some important cases it is civil freedoms and not political freedoms which are of most significant interest and concern. Hong Kong, which has a trivial amount of political freedom but enjoys civil and economic freedoms, is a case in point.

We were extremely fortunate to attract to that symposium some of the finest minds in the world, representing a broad cross-section of disciplines, including history, philosophy, political science, economics, and the law. Of course, the rest of the finest minds in the world are present at this meeting. [laughter]

I don't think there is any easy way to summarize those discussions other than to give you a sampling, a flavour of what was in each of the papers. A historical paper by Douglass North provided fascinating insights into the role that institutional developments and cultural heritage play in the evolution of democratic process. By comparing and contrasting the evolution of Britain and Spain, North cast into sharper relief the factors that have been important in the evolution of liberal institutions and economic growth in the Western world. This paper was followed by excerpts from Milton and Rose Friedman's *Capitalism and Freedom*, which provided the catalyst of the gathering. The relationship between economic and political freedom considered in these excerpts gave a timeless exploration of the subject, which was evident from the ensuing discussion led by Professor Gordon Tullock. It was noted that economic and civil freedoms have in common the fact that they are freedom from coercion by

others, whereas political freedom can be viewed as a process whereby people relinquish their rights in a collective majoritarian decision-making process. According to some participants, if civil and economic freedoms are guaranteed, then participation in the political process is almost irrelevant in this sense.

While the direction of causation was not established, evidence introduced in the course of conversation led to the definite impression that there is a correlation between the level of affluence and the likelihood that a nation will be politically tolerant and respectful of democratic institutions. Professor Alvin Rabushka, referring to earlier work, noted that he had correlated levels of incomes with political freedom indices produced by Raymond Gastil and also reproduced in our volume. These are the famous Freedom House measurements. The unmistakable conclusion from Rabushka's work is that countries that have a high rate of growth and a high level of income are also likely to have political freedoms. But a high rate of growth is difficult to achieve without civil and economic freedoms, suggesting that political freedom and stability may derive from civil and economic liberalism.

Fortunately, an examination of the global record seems to strongly suggest that the existence of political freedom is not a prerequisite of the existence of civil and economic freedoms. Singled out for particular consideration by the participants was the fact that most people tend to associate political freedom with the existence of some sort of majority rule. That is to say, legislation is determined by a simple majority of the populace and all have the opportunity to participate in the electoral process. It was determined by the consideration of a number of examples that majority rule by itself has no particular virtues, especially if the majority decides to abuse the rights of minorities.

In fact, considerable sympathy was expressed during the last deliberations for the unanimity principle, and for the reduction of political choices to those that were amenable to resolution by the unanimity principle. There was a lot of support for the notion that if we are going to speak of political freedoms, then we can only speak of that meaningfully in terms of the unanimity principle.

The discussion then went on from a general consideration of the prospects to particular case studies. In the book there is a collection of case studies in which countries from different parts of the world and existing in different cultural and environmental contexts are analysed to discern how economic, political, and civil freedoms co-exist. The first paper by Alvin Rabushka dealt with the two city-states of Hong Kong and Singapore. Those papers, and the subsequent discussion, confirmed the impression that both countries have done remarkably well in protecting economic and civil freedoms without utilizing political freedoms in the ordinary sense.

Not only did our discussions conclude that countries have been able to prosper in spite of having no political institutions but the judgement was that they have prospered because there have been no political institutions! Much of the discussion centred on the unfortunate proclivity of the political system to be

used for what Gordon Tullock has described as and Anne Kruger has dubbed “rent-seeking behaviour.”

While enjoying substantial amounts of economic freedom, neither Hong Kong nor Singapore are completely free of government intervention. This is particularly true of Singapore, which has a long tradition of governmental activism in such famous institutions as the Central Provident Fund and other social engineering policies. And though Hong Kong is subject to some economic regulation, in comparison with any other developing country it is undoubtedly the most economically free in the world. The lack of political institutions has been an important ingredient in Hong Kong’s past economic success, but as the end of colonial status approaches and the beginning of the People’s Republic of China hegemony becomes important after 1997, the conclusion is that political institutions may be the only thing that can act as a buffer between the P.R.C. and Hong Kong’s economic and civil freedoms.

As we attempted to become more precise in our discussion of different countries, there was much deliberation about how laws which were operated in one kind of context and by one sort of attitude could be completely changed when activated by a different set of attitudes. For example, in Hong Kong there are laws regarding the freedom of the press that can, in fact, be used by the colonial administrators to simply remove that freedom. But because the administrators of Hong Kong are subject to the second-guessing of the parliamentary traditions of Whitehall, there is no proclivity to use that particular law. When the mandarins of the P.R.C. come to operate that same law, it may produce an entirely different prospect and negatively impact civil freedoms. This is something to remember when characterizing countries on the basis of their laws and not the attitudes that may have formed them.

Lord Peter Bauer examined the interaction of economic growth, political sovereignty, and freedom in black Africa. He noted that the colonial managers of black African states left an administrative residue that has subsequently become the “ready-made framework of economic totalitarianism,” which underlines the point I have just made about Hong Kong in the P.R.C. era. One very interesting comment that emerged from the discussion about the black African situation was, as Isaiah Berlin noted in 1958, that the notion of liberty is a concept of such porosity that there is practically no interpretation it is capable of resisting.

During the course of discussion, there were no firm conclusions but there was a kind of consensus that Africa does provide many examples of misuse of government power, and this points to the crucial role that the protection of civil and economic rights have for economic development and political stability. The resounding message from Africa is that those who are seriously interested in freedom must not be misled to believe that political freedom, in the sense of freedom to cast votes in an election, can in any sense guarantee freedom that is meaningful for citizenry, and in particular, civil rights and freedom from capricious violence administered by the state. The economic success stories of

Africa occur in those jurisdictions where civil rights are preserved and a measure of economic freedom is ensured.

The paper by Ramon Diaz on South America was very insightful. He dealt with the puzzle of economic, political, and civil freedoms in South America and tried to explain why this continent, which had such promise in its early years, could have lapsed into the economic and political difficulties that are now endemic to the region. Diaz hypothesizes, and the subsequent discussion confirmed that, in part, the difference between South and North America is that the former was inspired by a Rousseauist concept of the appropriate role of government, whereas in the latter the Lockean notion of limited government was more prevalent. Cultural differences, a number of which were raised by Doug North in his paper as being a very important part of institutional evolution, were also mentioned by Diaz as having proved important and, indeed, decisive. This is particularly true of the pervasive impact of mythological thought and romanticism in Latin society.

The paper by Ingemar Stahl noted that many of the discussions about the relationship between rights and freedoms are often marred by a lack of precision in the terminology used. I can say that if there was one conclusion that emerged from that three-day session it was that terminological inexactitude is the main plague of these kinds of discussions. To try to remedy that, Stahl proposed an approach to the discussion about freedoms and civil rights that relates the contractual relationships between individuals and between individuals and the state. Freedoms in this sense are bundles of rights which will be more or less extensive in different states, depending on the regime pursued. This was found to be a quite useful classification system and it sharpened the nature of the discussion. The discussion itself concentrated more on the extent to which the relations between the state and the individual are really voluntary in the modern welfare state and, in particular, focused on the issue of Sweden's economic performance in light of the fact that it is a highly redistributive state.

Another point that rose in the discussion was the very important question of the extent to which the modern welfare state apparatus is coercive. If citizens believe that other citizens are bearing the cost of the programmes that they themselves subscribe to, then they are, in effect, voluntarily concurring with arrangements that are not in their interest, but *seem* to be in their interest because the costs associated with the actions are not clearly visible. Discussion of the Swedish case revealed that there are many lapses and many imperfections in the conceptual framework that economists and political scientists bring to the analysis of the relationship between economic, political, and civil freedoms.

The final paper, by Svetozar Pejovich, dealt with innovation in economic systems. While at first blush it seemed to be unconnected to the rest of the papers, it in fact initiated a discussion that neatly enveloped much of the discussion that had preceded. Innovation—the introduction of something new—occurs in economic, political, scientific, and all other aspects of human existence. In its

broad sense, the amount of innovation that can occur in a society depends on the relationships between individuals and the relationship between the individual and the state. The point emerged that when people are free to make contracts between themselves on how they will treat each other, they increase their freedom by increasing the choices that they have—and this is true even if the contracts involve restrictions. It was noted, for example, that contracts between inventors and those given the rights to use their inventions, while often quite demanding, in effect are intended to provide the user with sufficient latitude to use the innovation in a creative and potentially novel way while protecting the rights of the inventor. The only way the inventor will be inclined to encourage this to happen is if there is some equitable sharing, from the inventor's point of view, of the fruits of that arrangement.

One kind of innovation that can occur in a society where people are free to contract, re-contract, and make choices is the development of new institutions. Elections are a process whereby people change governments, and the freedom to do that is the freedom to innovate in the political area. Freedom of speech is the freedom to bring new ideas or new perspectives on old ideas to a society, while the range of civil rights which are often the concern of civil libertarians are the rights to be innovative in personal behaviour as long as that behaviour doesn't violate the rights of others. From the point of view of society's economic growth and development, the most important right is the right to innovate: to bring new products, new methods of production, and new pricing information to individual interactions.

That's a review of what I believe to be the salient points of our book *Freedom, Democracy and Economic Welfare*. But most importantly, a resolve emerged from the discussion (which ultimately became that book) that this was only a beginning of the process, not a culmination. At the suggestion of my colleague Walter Block we decided to enlarge our involvement into a series of five conferences, in co-operation with the Liberty Fund, of which the present gathering is the second.

It is our hope that out of this series will emerge a methodology for rating economic liberty. Then, with the basics under our belt, we will be in a position to publish an annual rating of economic freedom around the world—in much the same manner as Freedom House now rates political liberty.

Two final points need consideration in order for us to become more precise in our measurement of economic freedom. First, if there is one criticism to be made of the discussions during the last session it is that the dialogue was often frustrated by a lack of precision in our speech. As Al Harberger put it at one point, the discussion often floated away on a cloud of terminological inexactitude. Hopefully, we can avoid that fate, if we can agree on some taxonomy that we will find useful.

Secondly, as a public policy institute, the intent and the interests of the Fraser Institute are pragmatic. My hope is that from the process in which we are

engaged we will produce a measuring technique that can eventually become as much a part of common political parlance as the unemployment rate and the consumer price index. We have had some experience at the Fraser Institute in trying to raise important political and policy issues in the form of measurements which subsequently have become commonly accepted. For example, our Consumer Tax Index* is a measurement that generates considerable interest and activity in Canada every year we release it. In fact, it generates about 4,000 column inches of newspaper coverage which in comparable American terms would be about 40,000 column inches, to give you an idea of some of the impact it has.

I would like to see regular reference made to reports that freedom took a nasty turn last week owing to a cloud of interventionism emanating from Ottawa. I would like to see people eventually talk about freedom indices in comparing different provinces and different jurisdictions. While that may be an impractical hope, getting back to my original point, I think that if there is a chance to do it, it will come out of this series of discussions. I look forward very much to the discussion today and to the ones that will ensue in the coming years.

* See Isabella Horry, Sally Pipes, and Michael Walker, *Tax Facts Seven*, Vancouver: The Fraser Institute, 1990.

Discussion (Chapter 1)

David Friedman When I was reading one of the papers it occurred to me that we need to distinguish between the amount of freedom and the value of freedom. There are ways in which one may be free, and yet that particular freedom is of no use. We think of freedom in terms of how many choices are available, but there are lots of choices we don't want to make. We are freer for being able to make them, yet that particular freedom is not of much value to us compared with the freedom to make choices we want to make.

I am not arguing for identifying freedom with utility or wealth, or with how rich or powerful one is. What I am suggesting is that an index of the cost to me of restrictions on my freedom would be the ratio of the utility I actually have to the utility I would have in an entirely free society.

This definition does not require that perfectly free societies be possible. That is, I am thinking of an absolute in a sense in which every penny of taxation is a restriction on my freedom. It might be that in a society that had zero taxation, my freedom would be violated by countries across the border coming in and enslaving me. Fine. All that tells me is that there may be no stable society whose amount of freedom in this sense is 100 percent.

What I want to get away from is saying "this country is rich, therefore by definition it is free." I want to say instead "the average utility of people in this country, or the GNP per capita, which we may think of as a very crude measure of average utility, is 50. If you had the same country, the same resources, the same people, but no restrictions at all on freedom, the number would be 93. So the amount of restriction on freedom is 50/93." Of course, actually measuring that would be a horrendous problem, but it is easier to think about the actual solution if you at least have a solution in principle.

Voice Suppose it was 40 instead of 93?

David Friedman Oh, that's possible. Clearly this doesn't automatically assume that more freedom makes you happier. It does indicate the possibility that restrictions of freedom might make you happier by providing freedom somewhere else. But it might be that in a perfectly free society there would be a lot of heroin addicts, and in a slightly less free society where heroin was illegal, those people might not be addicted and might be happier. If so, then the value of that additional freedom would be negative. The definition does not automatically assume that freedom is valuable, although obviously it usually is.

Ellen Paul I would like to ask for further clarification on the pragmatic uses to which Mike would put this economic calculation. It is too narrow if we just hope to influence democratic societies that are already at the top of whatever scale we come up with. It is fine if we try to influence these societies to be more free

market and less interventionist than they are already. But if that is our sole objective, it is really unnecessarily restrictive. We would thereby ignore possibilities around the world for economic change, possibilities that did not exist a few years ago. What I am thinking of particularly is the situation in Eastern Europe and some other communist countries where there is tremendous change on the horizon, more change than any of their leaders anticipated. Once these forces are unleashed they have a dynamic of their own that is really hard to check. But if registering a six or a seven—low scores—on a scale of economic freedom does not make any difference to the leaders of some Eastern European countries, it may be useful to promote this scale in those countries anyway.

What I have in mind is the unintended effects of the Helsinki Accords. When they were first signed, it just seemed like an act of Western cravenness in validating the Soviet conquests of the Second World War. But it turned out to be useful, as was the Soviet signature on the human rights component of that accord: dissidents could say, “aha, you are violating the rights you agreed to in this Accord.” In other words, if this measure were promoted in Eastern Europe, dissidents might find it very useful as a check on their own governments. It is really a question of whether you intend to influence those countries registering sixes or sevens with any scale that we might devise.

Michael Walker There is certainly that possibility, and I hope that it would be used for that purpose. But there is also a more pragmatic, and from our point of view, more immediate interest: we have to think in terms of a freedom possibility frontier—of what is possible in our own context. If we don’t think in terms of what is possible, if we don’t relate it to the amount of resources, for example, that we have in North America, then we can get a horrible misreading of the state of affairs. Because we have such a huge resource endowment in North America, we have been able to finance all kinds of intrusions and inefficiencies that result from taking away peoples’ economic and civil freedoms without feeling adverse consequences. We are, to some extent, marching along with great confidence, because our losses in freedom are not evident. But our current standard of living is being financed by the depletion of our endowment. If we do have a shock, we will find ourselves in a much less desirable position than we currently think we are.

Ellen Paul I am not denigrating the importance of such an effort. I am certainly concerned with encouraging free enterprise in market societies. I just think that if you look at Eastern Europe you’ll find such tremendous opportunity. I know a couple of scholars, colleagues of mine, who have been holding conferences in Poland. One of them comes back every year and says, “it’s wonderful going to Poland and delivering a paper in defence of capitalism. There are no Marxists in the crowd. Even with the presence of the secret police sitting there in the audience at the University of Warsaw, I still get a much better reception than I do

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at Cambridge or Oxford.” There is a whole generation of intellectuals who disagree with Marx, who loathe the communist system, and who understand it. These people are just craving contact with the West, and this enterprise would be a tremendous opportunity to give them ammunition.

Richard McKenzie I am a bit confused about the objective of this endeavour. It seems to me that Mike is too. I’ll raise my concerns in terms of questions. Do we want to come up with a measure of freedom that reveals the truth about countries on a comparative basis? Or do we want to measure what has instrumental value? That is, do we want to manipulate the process of research agendas? If it is the latter objective and we actually want to manipulate the process, then we must begin to ask, what is it that the media want? What do we want to feed them? How can we get them interested? What is it about the political process that makes such a number important? And we work backwards. I would like to think that a true measure, if in fact we can come up with one, would indeed be very useful to manipulate the process.

James Ahiakpor Consider the notion that if we found tax revenues were enough to pay for social programmes, then this would indicate the community’s willingness to support social programmes. My feeling is that if we calculated the incidence of the cost of social programmes and compared it with the benefits, we would find that these are not equal. Social programmes may well be an avenue for those who pay very little tax or no taxes at all to exact spending on their behalf from those who pay taxes. It seems to me that if we do not find a way of capturing the incidence of benefits and costs of these programmes, we will be giving up some latitude in calculating the amount of freedom that exists.

Milton Friedman I would like to continue along the lines of Dick McKenzie’s story and go back to Mike Walker’s comment about the purpose of this research. I sympathize with the use of this research for propaganda, but I must say I personally find that very uninteresting. Or at any rate, how to use it for that purpose is an issue that economists, philosophers, and so forth don’t have much to say about. We’re not good at that. If you want to do that you ought to hire some public relations people. It seems to me our interests are scientific, and from a scientific point of view, I believe that the implicit assumption in much of this discussion is upside down. People are talking as if something called economic freedom is there in the same sense as a mountain is. We know the mountain is there, it exists, we know exactly what it is and we have some instruments and we are going to go off and measure it. But that’s not the way science works. That’s not the way a concept like economic freedom gets refined and improved and specified.

The fact is, we don’t know what economic freedom consists of. We have very intuitive ideas and we would like to do two things, as I see it. We would like

to use a process of exploring various dimensions of economic freedom and of trying to attach numbers to it as a device for approaching a more sophisticated understanding of what we really mean by economic freedom. What is the most useful definition of economic freedom? You cannot define a measure without knowing what the purpose of the measure is. What are you going to use it for? For one purpose you measure length, linearly. For another you measure it by the reciprocal. For another you measure it by the log. There is no one answer as to how you measure length. And that's an easy case because length is in a certain sense more objective, though not strictly objective.

I remember well a marvellous seminar at the University of Chicago that Hayek conducted on methodology. At one particularly memorable session, Enrico Fermi, the famous physicist, spoke about the meaning of measurement. He gave a very simple definition. He said, "measurement is the making of distinctions, precise measurement is making sharp distinctions." He said that the statement, "this is a dog and this is a cat" is a primitive form of measurement. And he said, "the concept of length that we use on Earth would be useless on the surface of the sun where the temperature is so high that there are no rigid objects. You would have to develop wholly different concepts."

The same goes here. One reason I am interested in trying to develop a measurement is that it is a way of gaining a more sophisticated understanding of what I mean by economic freedom. A second reason is to find a way of exploring the consequences of one or another dimension of economic freedom.

The approach, for example, taken in Zane's paper that somehow or other GNP is a measure of freedom seems to me to be upside down. That may be a result. We all know it isn't a measure. There is nobody in this room who would say that the fact that Saudi Arabia has the highest average per capita income in the world is a result of its having an economically free system. So what we know is that GNP, or any such thing, is a complicated result of a great many sources. That is what David was trying to get at by talking about the maximum potential from the present resources. What we would like to do is to understand what the sources of high GNP are. We believe that one of those components is freedom. I say, "is freedom" as if we knew what it is. We don't. But we have certain intuitive ideas. We are trying to refine them. Unless we can view this effort as having a scientific purpose, we don't have anything to hang onto. Otherwise it is purely arbitrary. You like tomato. I like potato. What do we do? I would like to see us try to concentrate, at least for a time, on turning upside down Mike's specification of the purpose of this research. He already knows what he wants to achieve. And I agree with him. I want to change Canadian and U.S. policy in certain well-specified directions that we both know. I have no doubt that the results of a scientific investigation would sharpen the concepts of economic freedom and would help in persuading people to make such changes. But let's turn it upside down and ask, what are we doing this for? How will it help us, as

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scientists trying to understand the world, to form our own philosophies, to go through this numerical process?

Henry Manne That's a hard act to follow. All I can try to do at this point is give some additional reasons why Milton has put his finger on the major problem here, although I have one semantic disagreement.

The notion of economic freedom is very peculiar. If you don't have an instrumental view of it, that is, if you don't have an idea that it can be measured in some way, by GNP, rates of production, or something of the sort, it gets very shadowy and confused with other kinds of freedom. It begins to look like the political freedoms that you are trying to distinguish it from in this exercise.

Part of the problem is that there is already some confusion that was bound to occur. There was this nice idea that it would be great if our side could get the kind of publicity that Freedom House does for political freedom. That would sharpen people's sensitivity and so forth. What happened as a result of thinking of that good public relations idea was that we got carried away. We began to think of that as having some real objective intellectual content, and I don't think that it does. As Milton says, maybe it would be a good idea to get some good publicists to do that sort of thing, but this doesn't seem a proper exercise for us.

Already this morning's discussion has shown some of the great difficulties involved. For instance, Ellen's comments raise the difficulties of distinguishing between a country's economic freedom, which is a collective notion, and individual freedom. If you take the idea that greater wealth gives some greater freedom to individuals—I don't think anyone disagrees with that notion—then I might quibble a bit with Milton's point that GNP is not a measure of freedom. It is the best measurement we can get at the moment. That is, the higher GNP or the higher total wealth, the more freedom in aggregate the individuals who own that wealth enjoy. The kind of political system doesn't matter. You can have a great deal of individual freedom, and the country's freedom can be very low. Take Milton's example of Saudi Arabia where some people have a great deal of freedom, can buy and sell huge parts of the world, and yet the national economy of Saudi Arabia is not a particularly free one. So that is one kind of difficulty with this.

Another difficulty is related if you go along with the notion that wealth is a measure of the individual's freedom. If you set up an index along that line, then immediately, and I think not incorrectly, the U.S. and one or two other countries become so dominant because of their total and per capita wealth, that countries that are just coming on line, even though they may have a very free political system and don't regulate or restrain property rights at all, are going to look very bad on that scale. You want to use wealth as a measure of freedom, and yet you don't for political purposes because then your index wouldn't have the desired effect.

This raises the question of how to rate Hong Kong, circa 1947. It was very poor. The average income was certainly very low. And yet we didn't know any rate of discount to use to say that the present value is very high because they have put in a lot of freedoms and they are going to do very well. We cannot do that in politics. Consequently, as long as we have no basis for determining the present value of economic freedoms that are simply in the process of developing, there is no such thing as measureableness. That is, until you have some scientific way of predicting political change. I don't think anyone here would suggest we do, so you really can't do the exercise you have set up.

Robert Poole There is a fundamental problem with what Henry is saying in terms of different perceptions of what economic freedom means. The choices that wealth gives is something that we value, but that is not at all what we are talking about when we speak of economic freedom as analogous to civil freedom and the absence of coercive constraint on choices that we would make.

We need to decide what the whole point of the conference is, in terms of what kind of freedom we are talking about. Picking up on Ellen's point about Eastern Europe, it is exactly this kind of terminological confusion which is imbedded in existing measures such as the UN's Universal Declaration of Human Rights. That document's conception of rights is, in large part, couched in terms of positive rights and entitlement rights. We risk getting into the same kind of terminological confusion by talking about freedom as the economic power to have lots of options, to make choices—as opposed to the negative-liberty conception of what economic freedom is all about. We have to really get clear on that before we spend two days on this.

Henry Manne If you have confidence that a full private property system without restraints will give you maximum wealth and production, as individuals will view it subjectively, then there really isn't any difference in these two things and to invent some amorphous notion sitting off there called economic freedom is just a way of confusing it.

Milton Friedman Where do you get that?

Henry Manne I want to know where you get the confidence that a notion of absence of constraint is in and of itself a good. Is that simply a given? You see, I find that in absence of constraint people will act as classical economics tells us they will. They will act in their own self-interest to maximize their own wealth as they evaluate it. And there isn't anything else.

Milton Friedman All I am saying is that it seems to me we can't take it for granted that we know what you think we know. We are trying to understand these things and we are very much aware that power in the sense of availability of

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goods and services is not the same thing as freedom as in the case of Saudi Arabia. Consider a dozen isolated islands with one person on each. Some are rich islands, some are poor. Are you going to say the rich islands are freer? Well, if they are, that is one dimension of freedom. It is a different dimension of freedom than the freedom from coercion by individuals and the question is, does it make any sense to distinguish between these different concepts?

Henry Manne You are assuming my measurement of the Saudi Arabian economy. If one person has all the wealth, there may very well be diminishing marginal returns of wealth for individuals.

Milton Friedman How do I know what all that means?

Henry Manne You don't. And that's why I say if the GNP of one island is greater, then yes, it is freer.

David Friedman It seems to me Henry is missing the point of the Saudi Arabian example. Saudi Arabia could be very equal in the distribution of wealth. Their high real income would still be the result of a number of different things. One is having lots of petroleum under the ground. Another is how free their institutions are in our sense. If you believe that freedom in Bob Poole's sense—absence of coercion by others—is one of the things that makes people wealthy, then freedom is not the same thing as wealth and you had better distinguish it from wealth if you want to test your belief that the two are related.

Ellen Paul I would like to comment on Milton's point that economic freedom is a complicated concept. I don't see that it is all that complex a notion. Why is it so difficult to know what it is? It seems a simple notion to me; of course, if you have lots of participants of diverse ideological persuasions it might become more complicated, even become the opposite of what it ought to be. But at least in this gathering, economic freedom has a rather obvious significance; it means that people should own, control, dispose of, trade, and exchange their property without government intervention and without threats of force or fraud from others. Government will not engage in regulating the economy. It won't offer subsidies and monopolies. I think that what is difficult is devising comparative measurements. How much freedom did you have in 1970? How much do you have in 1988? Is there more economic freedom in the United States than in Canada? That's difficult, but knowing what economic freedom is doesn't seem to be all that problematic.

Milton Friedman In a sense I agree with you. The abstract concept of economic freedom is very simple. I wouldn't put it in your terms at all, which seem to me much too complicated. I would say that economic freedom is the

ability of any two individuals to make any arrangements among themselves, wherever they are, whatever their sex, whatever their colour, providing it doesn't hurt a third person. That's where you have a real problem with your definition. You may need some of these governmental restrictions to prevent what two people do alone from hurting a third party. Almost all the difficulties of going from this highly abstract concept of economic freedom to the institutional arrangements that are most appropriate arise out of the complexities that are concealed by the simple statement that two people are free to do anything they want provided they don't interfere with a third party.

Ellen Paul Well, let's take an example. A factory produces an environmental pollutant. Let us say that the government mandates that the factory be closed. It says: you can't produce in this way. We'll dictate what kind of production mechanism you should use. Or, alternatively, the government provides courts in which private parties injured by the pollutant can come to attain an injunction or sue to recover damages. Which system is more free?

Milton Friedman I don't know which is more or less free. That depends on the transaction costs.

Ellen Paul I want the liberty to dispose freely of my property; you are worried about transaction costs?

Milton Friedman They are the same thing.

Ellen Paul Well, I don't buy that.

Milton Friedman If there were no transaction costs, the whole third party problem would disappear, as Ronald Coase showed in his famous paper. Since there are, and we are talking about the real world, not an abstract world, we have a very difficult problem.

Ellen Paul If one is looking at governments and their economic policies, it is relatively easy to say which government policies are promoting economic freedom. If you look at the extreme example of communist countries where governments own everything and attempt to dictate all economic behaviour, and people are tied to their jobs, it is obvious that these people have no economic freedom; they are slaves of the state. The situation is quite different in the United States, even if that government exercises quite a lot of control over economic relationships.

Milton Friedman You don't make progress in understanding things by looking at easy problems. It is the fringes that illuminate the difficulties.

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Ellen Paul The fringe cases may be fun to play around with, but these “life boat” cases are intellectual ploys, and they often serve to obscure the larger issues.

Milton Friedman We are talking about two different worlds. We are supposed to be intellectuals and thinkers and scientists. We are not here as public relations people. I hope.

Ellen Paul I’m not saying that we are mere public relations flacks. I just don’t think the problem is all that difficult. There are genuinely difficult questions of philosophy. This doesn’t happen to be one of them.

Milton Friedman As long as you just talk in generalized terms there is no difficulty, I agree. You don’t realize how difficult the problem is. You don’t realize the complexities that are covered up by the abstract definition. And you will when you try to be more precise about this; as Fermi says, precise measurement is the making of precise distinctions.

Ellen Paul I would agree with you if you were coming up with a measure that said Rumania is a 5.03 and Czechoslovakia is a 5.76. But we’re not doing that. The numbers offered by Freedom House are not of this order of specificity, and they are amalgamated into seven general categories.

Milton Friedman They are largely fallacious and contribute very little to our problem. The defects of the Freedom House measures were shown in the discussion last year. It turned out that if you held civil liberties constant, there was a zero correlation between political liberties and income. Political liberties had nothing to do with income. So those measures alone were illuminating in bringing out a relationship we didn’t have very clear evidence of before.

Zane Spindler I want to address one issue that Ellen Paul and Milton Friedman raised with respect to the Freedom House measures. These just give gross ratings that are not useful for making fine distinctions of freedom between or within various countries.

Suppose we had finer measures. One could imagine a presidential news conference where some reporter like Sam Donaldson gets up and says, “Mr. President, you have sworn to uphold the Constitution. What are you going to do about this 0.1 fall in the freedom rating?” That might make freedom ratings at least as valuable as the unemployment rate.

Another point I would like to focus on is one that Richard McKenzie raised, but not in the way that he raised it. He tried to distinguish between a measure that gives a truth versus one that gives us political value. I don’t think we can separate these. In order for a measure to have political value it has to have truth value. It

has to be something that is ultimately very difficult for opponents of freedom to challenge, otherwise it is not going to work.

Finally, David Friedman said that there were really two concepts of freedom that we should keep straight, and I agree. We have to differentiate between freedom and the value of freedom. The problem I find in this is that freedom per se has a number of dimensions that are incommensurable and for which there are no obvious trade-offs. How are we going to get an aggregate measure of economic freedom unless we have some way of establishing trade-offs? It may be ultimately more useful if we look at the value of freedom because that measure at least has implicit trade-offs, established by those people who really value it, that is, by those people in the market.

Antonio Martino This discussion reminds me of something that Joan Robinson said in her horrendous little book *Economic Philosophy*. She made this distinction between a point and an elephant: you can define a point as something that has position but no magnitude, but you cannot see a point; you cannot define an elephant, but, of course, you can see an elephant.

The concept of freedom is closer to the elephant than it is to the point. It is a very large concept. From this point of view, I entirely agree with what Professor Friedman said. From the scientific point of view, I also agree that the concept of freedom is too large. You cannot have an exact measurement. You can have a measurement that would be narrow and inaccurate and instrumental. We would be doing violence to the concept of measurement.

On the other hand, this is also true for political freedom, and we don't even know what political freedom is. The propaganda value, however, of Freedom House in this instance is very high. As defenders of economic freedom, whatever that means, we must follow the same strategy for economic freedom as we do for political freedom.

William Hammett I am caught between Milton and Ellen here. It might be that there is more ambiguity about Fraser House than Freedom House. Take occupation licensure; we all agree this is an intrusion. However, right now in California cosmeticians are causing blindness with their make-up applications. There is some movement for a new law to restrict them. A lot of individuals would consider that an infringement on their economic freedom because they enter into what we would see as a voluntary arrangement...to get blinded. There are third party effects and externalities. One definition of economic freedom is not to have harmful substances thrust at you in a market transaction. It seems like that's where some confusion arises. It depends on your level of sophistication and that's what makes it difficult.

James Ahiakpor Sometimes you can tell a great deal about what you are trying to get at by considering what the opposite is. With regard to freedom, my concept

of freedom is non-interference with a voluntary exchange. It is not a third party problem. Rather, it is whether or not individuals gave their consent to an act. If they did, then we can say an exchange is consistent with freedom. Thus, we may think of coercion as the opposite of freedom.

Gerard Radnitzky I wish to attend to what Milton Friedman said. But first a sort of apology. I am one of the few in this company who is not an economist. My teachers were theoreticians of physics, philosophers of science, and logicians, and only late in life I discovered that, for me, economics is more fascinating than those other fields. In view of my limitations it may be advisable to limit myself to methodological comments—but I know I will not have the moral strength to be so cautious.

I take Milton's remarks as a warning against essentialism. Essentialism is the view that something can have an essential property by virtue of a definition. The gist of his warning is that we should not attempt to formulate the correct definition of the concept of "economic freedom." That would be an impossible task. Rather, we should attempt to improve the intellectual instruments with the help of which we can describe certain aspects of social systems. The concept of "freedom" is one such instrument. Milton also reminded us that measuring is but a special sort of describing. In order to describe things we need as a conceptual instrument a descriptive system. We can classify such systems as classificatory, comparative, typological, and quantitative. "Measurement" is often used metaphorically. At any rate, first we must know what objects we wish to measure with respect to what relational or quantitative properties.

With regard to the task at hand, the methodological concept of explication is useful. An explication is basically a proposal, in certain contexts, to replace an intuitive or less refined concept, the explicandum, by another concept, the explicatum. The new concept is supposed to have "sufficient" similarity to the old one and to be a better intellectual instrument for the task at hand, e.g., enabling us to formulate law-like hypotheses that cannot be formulated with the old concept. To give a simple example: the intuitive concepts of "hot," "cold," "warmer than," etc., are replaced first by the concept of "temperature"—which must not be confused with the various methods of measuring temperature. That concept is then replaced by a concept defined in terms of thermodynamics and then by a concept in terms of statistical mechanics, roughly as the average kinetic energy of molecules and atoms. This example shows that an explication, the improvement of a concept, is a spin-off of the improvement of a theory, i.e., the replacement of a theory by a successor that has more explanatory and predictive power.

Alvin Rabushka's papers are fine examples of explications. In chapter 1 he makes an inventory of what the literature has to offer with respect to concepts of "freedom." In chapter 2 he focuses on a recent proposal of an explicatum of "freedom," i.e., that given by Freedom House, and he criticizes that explicatum.

In chapter 3 he proposes an explicatum of his own: a descriptive system based on the seven dimensions that he mentions. Such a descriptive system—which explicates the idea of “economic freedom”—can then guide the construction of indicators of the absence or presence of certain aspects of “economic freedom,” now taken in the sense of the explicatum. The explicatum, in turn, guides methods of comparing countries with respect to the degree in which a particular aspect of “economic freedom” is exemplified in each of two or more countries that are being compared. Eventually, it might guide a quantitative description in the full sense of “measurement.”

It is imperative that we distinguish between concept and definition on the one hand and methods of ascertaining the presence or absence of the property signified by the concept on the other. Otherwise, conceptual confusion is unavoidable. Take for instance the concept of truth, roughly defined as correspondence with facts—an absolute concept of truth. It must be clearly distinguished from the procedures or methods of ascertaining the truth value of a particular descriptive statement; these methods are in principle fallible. Confusing concepts and procedures for ascertaining the presence or absence of the property designated by the concept leads to what in methodology is called the “operationalist fallacy,” the view that a concept can be identified by stating methods of measuring the property designated by the concept. This fallacy leads to the pseudo-problem of the “sameness” of concepts that guide different methods of measurement, e.g., temperature as measured by various thermometric methods like thermal expansion, thermo-couple, resistance, and radiation types, etc. Alvin does not commit that fallacy.

Rose Friedman This whole discussion of measurement reminds me of Frank Knight’s comment when he looked at the quotation carried on a social science building that read, “Nothing is scientific unless you can measure it.” Knight said, “and if you can’t measure it, measure it anyway.”

That is essentially what we are talking about. Why not forget the idea of a numerical measurement and instead discuss what economic freedom really consists of. If you ever get to the point where you really can define the elements of economic freedom, the measurement will be very unimportant in a sense and will be very simple. So I suggest that we just forget about the sum total and go to the ingredients.

Milton Friedman The quote Rose refers to is from Lord Kelvin and it says, “Nothing is scientific unless you can measure it.” I believe that Knight’s comment is wrong. I disagree with Rose on this one.

Michael Walker The main purpose of having these kinds of discussions is to strive for a more precise way of approaching the problem of measuring freedom. Having gotten this more clear and more precise understanding, we can use those

measures for public relations purposes. The notion that using research for public relations purposes renders it scientifically inaccurate is a myth. Our experience is that if you take the trouble to do your scholarly work first, when you use the instrument for public policy, you have a great deal more effect. If you don't take this trouble, it will have no effect, or its effects will be harmful. The Fraser Institute has had this experience with the tax rate. Our statistical agency, Statistics Canada, criticized the Fraser Institute for 12 years for using a certain methodology for calculation, even though we are using the most scholarly and accurate way of doing it. Then, in the thirteenth year, they approached us and asked how exactly did we do this, because they want to create a measure of this kind.

Now for a few particular points that were raised. Jim Gwartney mentioned the idea that we could define economic freedom as freedom from having to seek collective approval for individual contracts. In the last symposium Ingemar Stahl reminded us that there may be collective contracts in which people may voluntarily contract away some of their freedoms. Jim Buchanan noted that at the constitutional formulation stage individuals may, in fact, contract away some of their freedoms out of the belief, maybe illusory, that this will reduce the riskiness of their existence in the post-constitutional phase. That is, behind the veil of ignorance they may contract away some of their freedoms because they believe it would reduce the risk of living when they don't know which lot they will draw in the lottery of life.

Two last points on measurement. The kinds of measurement that will come out of our deliberations will always be relative ones. David Friedman mentioned the notion of the freedom possibility frontier, a kind of total choice set that we might have available to us. This touches upon an illustration that may be useful to make my point. Conceive of a country in which 15 percent of total income is needed to maintain a subsistence level of consumption. Then a 50 percent tax rate, an elimination of 50 percent of the choice set that is available to the people in that country, may not be oppressive.

Now consider another situation in which 95 percent of the available income is needed for subsistence. Then a 10 percent tax rate in that environment would be totally oppressive in the sense that it would reduce peoples' level of consumption to a point below subsistence.

The final point, and in some ways contradictory to the one I've just made, is that in our discussion this morning, there has been a confusion between the freedom to choose and the consequences of having the freedom to choose and particularly the notion that there are values to freedoms. We have implicitly said that because people are free to choose they will therefore have a greater income set, and that situation is preferred to the one where they have less choice and a lower income set. But suppose an increase in the freedom set leads to a reduction in economic outcomes. Then how would we evaluate it? It seems to me that we should not identify the value of freedom to choose and freedom to choose itself

in our deliberations. We have to isolate the freedoms, and then in a subsequent phase try to relate those freedoms to the values that may emerge from having the freedom to choose.

Chapter 2

Philosophical Aspects of Economic Freedom

Alvin Rabushka

“The tide is turning” in favour of economic freedom, as Milton and Rose Friedman wrote in 1980 in *Free to Choose*. Perhaps even they dared not envisage the dramatic gains that have taken place during the 1980s: a world-wide trend to lower tax rates, the spread of capitalism in the Third World, privatizing state-owned enterprises in both advanced and developing countries, and deregulation of industry. Economic freedom has fuelled a rising trend of prosperity around the globe. Market forces have even invaded the socialist countries of Eastern Europe and Southeast Asia as central planners look to jump-start moribund economies.

Most of us have an intuitive or common-sense notion of the meaning of economic freedom. A smattering of definitions or attributes includes free markets, private enterprise, voluntary exchange, capitalism, limited government, laissez-faire, free trade, low taxes, free movement of capital, and other dimensions of economic life. To say that one country enjoys more economic freedom than another means that it has more and higher doses of the above dimensions of economic life. For example, it is relatively easy to agree with the claim that Hong Kong enjoys a greater measure of economic freedom than mainland China, or South Korea than North Korea, or the Federal Republic of Germany than the German Democratic Republic. It is equally easy to see if any given country has more economic freedom than it did last year or a decade ago as, for example, in mainland China, which has undergone a decade-long spate of liberal economic reforms under the tutelage of twice-rehabilitated Deng Xiaoping.

These comparisons lack quantitative precision. Assume, for the moment, a scale of economic freedom ranging from zero (no economic freedom) to 100 (complete economic freedom). On that scale, where would we rank Hong Kong

in comparison with mainland China? How would we score mainland China in 1988 compared with the China of the Cultural Revolution during 1966-76? To date, all scholarly efforts to rate economic freedom have taken the form of qualitative measures or relied on casual empiricism. No formal, rigorous rating method yet exists.

This paper is the first stage in a long-run effort to elaborate the conceptual underpinnings of economic freedom for the ultimate objective of developing precise measures of the degree of economic freedom that exists in every country in the world. At a minimum, it is hoped that from this effort will come a basis for rating economic freedom that rivals the Freedom House treatment of political freedom, which has gained universal currency in the scholarly community. Ideally, it would be better still to develop a rating system that permits quantitative comparisons across nations and over time. A side benefit of a formal rating scheme that achieved acceptance and frequent usage is that it would sensitize scholars to the idea of economic freedom, and thus elevate it in stature to the much more frequently analysed topic of political freedom. That in itself would constitute an enormous pay off for this effort. Of course, there is no guarantee that scholarly acceptance of a scheme to rate economic freedom would insure agreement with the values of economic freedom or the goals of its proponents. Nonetheless, it would be nice if scholars around the globe, regardless of political persuasion, accepted the outcomes of a rating system as factually accurate.

The organization of chapters 2, 3, and 4 are as follows: chapter 2 sets forth several historical and modern attempts to develop a philosophy or definition of economic freedom in order to identify common (as well as divergent) elements¹; chapter 3 critically assesses the most thorough attempt to measure economic freedom that now exists, which has been performed since 1982 by Freedom House in New York City as part of its Comparative Survey of Freedom; finally, chapter 4 represents a preliminary attempt to provide and elaborate on a checklist of the different dimensions of economic freedom that require consideration in the development of a comprehensive system to rate economic freedom.

If there was any need to justify the importance of focusing on the concept of economic freedom, a glance at the household dictionary would show how little emphasis it has received compared with its political cousin. *The American Heritage Dictionary* offers 11 different aspects of freedom, most of which concern political rights or civil liberties: 1) the condition of being free of restraints; 2) liberty of the person from slavery, oppression, or incarceration; 3a) political independence; 3b) possession of civil rights; immunity from the arbitrary exercise of authority; 4) exemption from unpleasant or onerous conditions; 5) the capacity to exercise choice; free will; 6) facility, as of motion; 7) originality of style or conception; 8) frankness; 9a) boldness; impertinence; 9b) an instance of improper boldness; a liberty; 10) unrestricted use of access; and 11) the right of enjoying all of the privileges of membership or citizenship.

Roget's Thesaurus is more generous to economic freedom than the dictionary. Synonyms of freedom include liberty, license, self-determination, free will, noninterference, laissez-faire, civil liberty and civil rights, freeman, unrestrained, uncoerced, unimpeded, and freeborn, among others. Thus, in common parlance economic freedom generally receives much less attention than political freedom.²

Political philosophers and social thinkers have explored the notion of freedom almost from the beginning of recorded history. For example, the first use of the word liberty is traceable to ancient Sumeria.³ Its use describes the good king, Urukagina, who freed his people from previous wartime taxes. The evidence consists of cuneiform writing on clay cones excavated at Lagash, in Sumeria, which contained the freedom laws of Urukagina that were promulgated to rid the land of tax collectors. One cone contained a proverb about taxes: "You can have a Lord, you can have a King, but the man to fear is the tax collector."

Ancient and medieval philosophers were primarily concerned with political freedom rather than economic freedom. To the Greeks, freedom described a fully independent polis that was not subject to the control of any outside power.⁴ Pericles typified the free man who, as an active citizen in the exercise of his political freedom, helped shape the laws and policies of the polis.⁵ The primary emphasis of the ancient conception of freedom was an entitlement to a voice in collective decision making. Political freedom meant self rule, or the absence of external control. It was not an idea that emphasized the rights of the individual to non-interference from the state or protection under the rule of law.⁶ The citizens of the ancient world had duties and obligations, not rights and privileges.

The liberal tradition in politics and economics dates largely from the seventeenth century.⁷ The modern notion of liberty or freedom signifies non-interference in the private affairs of individuals in a society governed under the rule of law. Freedom became synonymous with the protection of property, which derived from the feudal heritage of the Middle Ages. The Christian emphasis on the salvation of the individual also helped break down classical collectivist notions of society. The freedom to own a certain amount of property was seen as a necessary condition for being able to maintain personal independence. The development of property rights went hand in hand with long standing provisions of human rights that were proclaimed in the Magna Carta in 1215, in thousands of medieval charters in England and continental Europe, in statements and restatements on civil rights, and in the procedural safeguards of person and property that developed in the common law.⁸

Although the Spanish Jesuits of the School of Salamanca at the end of the medieval period anticipated some of the themes of classical liberalism, especially the notion that the market price was the just (correct) price of any commodity, economic freedom seriously developed into a coherent and powerful intellectual tradition with the publication of John Locke's *Second Treatise on Civil Government*, which emphasized freedom of association, private property,

and the sacrosanct nature of individual liberty, secured under the rule of law. David Hume reinforced Locke's emphasis on the right to property as the foundation of society and government, insisting that the stability of possession of property was essential to the establishment of human society and that fixing and observing this rule fosters harmony and concord. In so doing, each individual may peacefully enjoy what he has acquired by fortune and industry.⁹

Locke was followed nearly a century later by Adam Smith. In his *Inquiry into the Nature and Causes of the Wealth of Nations* (1776), Smith theorized a system of natural liberty in which each person possesses the greatest liberty compatible with liberty for every other person—a system of methodological individualism. A system of commercial liberty would also find its natural counterpart in a constitutional order that guaranteed civil and political liberties.

Finally, brief mention may be made of John Stuart Mill. In his famous essay "On Liberty," Mill insisted that the principle of liberty permits individuals to frame their life as they see fit without external interference so long as fellow creatures are not harmed, and that from the liberty of the individual follows the right to combine for collective action so long as the rights of others are not infringed.

Nineteenth-century England was governed by the principles of Locke and Smith. Free trade, laissez-faire, low taxes, low state expenditure, and a minimally interventionist government were its hallmarks.¹⁰ The state had little more than night watchman functions throughout most of the century.

Twentieth-century Britain brought forth a managed mixed economy resting upon socialist philosophy. Those who supported an activist state believed it would insure full employment and fought for the extension of the welfare state. Classical liberalism revived in 1944 with Friedrich A. Hayek's *The Road to Serfdom*, followed later by Sir Isaiah Berlin's *Two Concepts of Liberty*, which distinguished the negative idea of liberty as non-interference from the positive idea of liberty, which involved an entitlement to participate in collective decision making and the use of the state to extend rights through redistributing income and creating opportunities to enable individuals to achieve self-realization. Other major contributors to the modern revival include Ludwig von Mises, Milton Friedman, and James Buchanan. Beyond any doubt, John Locke's powerful statement on the primacy of private property earned for him first place in the economic freedom hall of fame.

John Locke

To begin with, virtually every proponent of economic freedom stipulates the need for a system of well-defined property rights, secured and enforced under the rule of law. On this point, each owes a large intellectual debt to John Locke. Locke provided the first coherent justification for private property as the foundation of a liberal social order. Private property was essential to preserve and expand the individual freedom that man enjoyed in the state of nature. Let's review Locke's contribution to the subject of economic freedom in some detail.

In his *Second Treatise on Civil Government*,¹¹ Locke argued for the merits and legitimacy of private property, and that the primary end of civil government is the defense of property.¹² Locke's deep sense of property also took root in America.¹³ He provided the intellectual foundation that underpinned the zenith of economic freedom and prosperity that developed in nineteenth-century Britain.¹⁴

John Locke belonged to a class of "social contract" philosophers. He broke ranks with statist classical and medieval philosophers by reposing rights in the individual, not in the state. He began with a concept of a state of nature, in which men are living as equal and separate units. "In the state of nature, all men are in a state of *perfect freedom* to order their actions, and dispose of their possessions and persons, as they think fit, within the bounds of the law of nature, without asking leave, or depending upon the will of any other man."¹⁵ The state of nature is not a Hobbesian state of license: it implies a law of nature, namely, that no one ought to harm another in his life, liberty, or possessions. Each person recognizes limitations on his own will, especially the limitation that every other person possesses a right to property¹⁶ and the right to punish transgressors of natural law to preserve the innocent and restrain offenders.¹⁷

The state of nature is a state of individual liberty, and can be surrendered to a collective power or the community only through consent. No man can be subject to the arbitrary will of another man, since freedom of nature is bound only by the law of nature.¹⁸

The bulk of the *Second Treatise* is devoted to the principle theme "Of Property." Locke's primary claim was that "every man has a *property* in his own *person*."¹⁹ Every man is duly entitled to the labour of his body and the work of his hands, as captured in his famous phrase that "Whatsoever he removes out of the state that nature hath provided and left it in, he hath mixed his labour with it, and joined to it something that is his own, and therefore makes it his property."²⁰ The application of labour gives the individual the right to remove the newly-created property from the common state found in nature, thereby separating and excluding it from the previously held common rights of other men.²¹ The application of labour thus converts resources found in the state of nature, where they belonged equally to all, into private property. Of critical importance is that the act does not require the consent of any other person.²² The authority to create private property

out of the common rights derives from God. Although God gave the world to men in common, it takes industrious and rational men to make it useful through the application of personal labour. The application of labour secures distinct titles for men from a world given to men in common.²³ Indeed, the creation of value derives almost entirely from the effects of labour. A fallow field in nature has far less value than a sown and nurtured plot of grain.²⁴

What are the limits to the private acquisition²⁵ of the natural fruits of the earth that previously belonged to all? One can fix as much property in one's labour as possible so long as it does not spoil (spoilage betrays the law of nature since it takes from others the right to resources found in the state of nature without adding to one's own useful property).²⁶ The invention of money, that lasting item that men might keep and accumulate without spoiling, permits men to accumulate wealth beyond the holding of products up to the point of spoilage.²⁷ By mutual consent,²⁸ men could take money (gold and silver) in exchange for perishable products.

Locke built his social contract upon the institution of private property. The civil society, to which each man consents to transfer the right of punishment he enjoys in the state of nature, was created primarily to preserve private property.²⁹

Locke was more pragmatic about the institutions of civil society than he was about the absolute rights of free men in the state of nature. When men consent with each other to make a civil society under one government, they put themselves under an obligation to their fellow citizens by submitting to the determination of the majority. The consent of the majority, in the form of concrete decisions, becomes the consent of every individual in the civil society. Unless the majority can act as one body, the society will be dissolved. Locke permitted the formation of a community by "any number greater than the majority."³⁰

To repeat, "The great and chief end of men's uniting into commonwealths, and putting themselves under government, is the preservation of their property; to which in the state of nature there are many things wanting."³¹ Government supplies a known law, which determines right and wrong and a basis for setting controversies;³² it supplies an impartial judge with authority to determine differences according to established law; and it supplies the power to enforce sentences.

Locke's contribution to the discussion of civil government is the very important notion of limited government. The government that men fashion by yielding the rights they enjoy in the state of nature cannot act arbitrarily over them nor dispossess them of those rights. The rules that legislators promulgate in civil society must correspond to the law of nature (the will of God). The government is obliged to govern by law, not by arbitrary, capricious dictates. The "true end of civil government" is the protection of private property under the rule of law.

Nor can government take from any man any part of his property without his consent.³³ The power to tax that enables government to fulfil its tasks of protecting men from harm and punishing transgressors rests on the consent of the governed, either directly or through representatives chosen by them. Payment should be based on the proportion of benefit each taxpayer derives from the maintenance of protection the state provides.³⁴ Taxation without consent “invades the fundamental law of property and subverts the end of government.”³⁵

Locke’s government was limited in practice as well as in principle. Since lawmaking is a relatively expedient activity “there is no need that the legislature should be always in being, not always having business to do.”³⁶ Moreover, to prevent the government from extending its power, Locke required legislators to be subject to the laws they themselves made.³⁷ He also called for the separation of legislative and executive powers.

Locke reserved in the people the right to remove or alter a legislature that acts contrary to its trust. The community remains sovereign; it cannot surrender its right of self-preservation. Through the executive it can convoke or dissolve the legislature. But the people retain the right both to refashion the executive and legislature if either violate their trust.³⁸

Locke’s world was grounded on the primacy of the individual. From his emphasis on the individual as the unit of action, Locke developed his conception of natural law in politics which established the natural rights of each individual. Locke transformed the statist character of traditional natural law theory, which placed good and virtuous action in the state, to a body of thought that subordinated the state to the individual. Locke’s individualist tradition influenced later American revolutionaries and laid the foundation for American constitutional government.

Milton Friedman

In many ways, Milton Friedman is a modern-day John Locke. He asserts the primacy of the individual as the ultimate entity in society. He recognizes the vital role that private property plays in fostering economic and political freedom, and economic prosperity. He is concerned with a variety of pragmatic political issues, such as decentralization of political power. Though separated by 272 years, they are intellectual kinsmen.

With the assistance of Rose Friedman, Milton Friedman set forth a coherent statement of economic freedom in 1962 in a collection of essays entitled *Capitalism and Freedom*.³⁹ The book explains the role of competitive capitalism as a system of economic freedom and shows that economic freedom is a necessary condition for political freedom. It also discusses the legitimate role of government in a free society, identifying those areas where government intervention in the private affairs of individuals is warranted, but also where intervention that

goes beyond the legitimate limited tasks of government harms both economic freedom and efficiency.⁴⁰

Invoking the language of classical liberalism and defining himself as a liberal, Friedman posits freedom as an ultimate goal and the individual as the ultimate entity in a society. How is freedom best secured? In the miracle of the market place, he says, which co-ordinates the economic activities of millions of people on the basis of voluntary co-operation. Co-operation between buyer and seller is achieved without coercion provided that both parties in every economic transaction benefit from it. Through effective freedom of exchange, the market prevents one person from interfering with another. Consumers have a choice of sellers and sellers have a choice of buyers. Similarly, employers and employees enjoy multiple choices, which protects both from coercion. The market accomplishes this impersonally and without centralized authority. To ensure that every transaction is strictly voluntary, economic exchange requires that individuals and enterprises be private (government officials and enterprises would enjoy the coercive powers of the state to enforce their wishes), and that individuals be free to enter or not to enter into any particular exchange. Friedman labels an economic system built on the principles of voluntary and unanimous exchange a free private enterprise exchange economy, or competitive capitalism.

In the spirit of Locke, whose free individuals in the state of nature contract with each other to form civil society for the preservation of private property and maintenance of the market (and the institution of private property on which market exchange takes place), Friedman's world requires certain collective or political institutional arrangements. "The basic requisite is the maintenance of law and order to prevent physical coercion of one individual by another and to enforce contracts voluntarily entered into, thus giving substance to 'private'."⁴¹ Other issues arise from monopoly and neighbourhood effects (or externalities).

"The need for government arises because absolute freedom is impossible." Government is essential as a forum for determining the "rules of the game" and for enforcing the rules decided on. Protection of the individual and the nation from coercion are two activities that prevent exclusive reliance on individual actions through the market. Friedman argues that to the extent that economic activity is removed from the control of political authority, the market eliminates coercive power.

Friedman stipulates the institutional arrangements upon which the market system of voluntary exchange rests. First is the maintenance of law and order to prevent the coercion of one individual by another; Locke also gave heavy weight to this objective. Second is the enforcement of contracts voluntarily entered into; Locke was silent on this point. Third is the definition and meaning of property rights; Locke claimed property rights were a precondition of civil society.⁴² Fourth is the provision of a monetary framework; Locke made no statement about the private or public provision of a monetary standard. In addition, govern-

ment must correct the effective inhibition of exchange brought about by monopoly and engage in activities to overcome neighbourhood effects.

Once government exceeds its legitimate duties, intervention is likely to bring more harm than good. Friedman points to the destructive economic effects of railroad regulation at the expense of the consumer, the damage of high marginal rates of income tax, waste of funds in federal agricultural programmes, housing policies that contribute to urban blight, the coexistence of rising welfare expenditures and rising welfare rolls, and other examples of counterproductive government economic intervention. In the process, an expanding governmental role threatens the preservation and expansion of individual freedom.

To preserve and expand individual freedom, in *Free to Choose* the Friedmans propose an economic bill of rights to complement the original Bill of Rights set forth in the United States Constitution. The specific rights in question encompass a tax or spending limitation of the fraction of national income the government is authorized to spend (thus limiting the size of government), a prohibition on imports or exports (thus achieving free trade), a ban on wage and price controls (thus insuring internal free trade), a ban on occupational licensure (thus assuring free entry into every line of production), a requirement for proportional taxation (thus preventing discrimination by one class of taxpayers against another), a limit on money supply growth, and an indexation provision to remove the incentive for government to inflate the currency. They propose the list in an exploratory spirit of stimulating thinking on specific measures to foster economic freedom. The list is an invaluable starting point in the design of any measure to rate economic freedom.

Murray Rothbard

Libertarians who reject any role for government in the economy look to Murray Rothbard for the cleanest, purest exposition of the principles of economic freedom. A prolific writer, in the 1960s he wrote at length on the virtues of the free market, the evils of coercive intervention, and the feasibility of a totally stateless (anarchistic) market economy. Unsatisfied with value-free analysis, Rothbard set out to develop a positive ethical system which would make the case for individual liberty in *The Ethics of Liberty*.⁴³

Rothbard grounds his political philosophy of liberty on a natural law foundation, especially John Locke's treatment of property and ownership. Rothbard's theory of liberty rests on the establishment of the rights of private property, which determines each individual's sphere of free action. The right of any man to do certain things means that it would be immoral for others to stop him by the use or threat of physical force. He defines crime as a violation or aggression against the just property or body of another individual. The theory of liberty thus becomes an analysis of what can be considered property rights and

what can be considered crimes. On this foundation, Rothbard examines a number of topics including the rights of children, the proper theory of contracts as transfers of property titles, and the questions of enforcement and punishment, among others. His objective is to develop a libertarian law code as a natural law theory.

Rothbard's free society or his society of pure liberty is based on free and voluntary exchanges. The free society is one where property titles are founded on the basic natural facts of man—each individual's ownership over his own person, his own labour, and the land resources that he finds and transforms (though the ultimate justification in Rothbard's natural law does not depend on God as it does in Locke). The natural alienability of tangible property and man's labour service make possible the network of free exchanges of ownership titles. The free market economy thus depends upon a free society with a certain pattern of property rights and ownership titles. The libertarian society—the regime of pure liberty—is a society where ownership titles are not involuntarily distributed.

The universal status of the ethic of liberty, and of the natural right of person and property that obtains under such an ethic, can be covered by the basic rules: ownership of one's own self; ownership of previously unused resources that one has occupied and transformed; and ownership of all titles derived from that basic ownership either through voluntary exchange or voluntary gifts. Rothbard deems all current titles to property as valid except where the origin of any current title is criminal and the victim or his heirs can be identified and found, or the victim cannot be found but the current title-holder is the criminal in question.⁴⁴

Rothbard parts company with Friedman in the area of contracts. He argues that the right to contract is strictly derived from the right of private property, and therefore the only enforceable contracts should be those where the failure of one party to abide by the contract implies the theft of property from the other. This can be true only when title to property has already been transferred, and therefore where the failure to abide by the contract means that the other party's property is retained by the delinquent party without the consent of the former (implicit theft). Thus, the contract itself is not an absolute and need not be legally enforceable in a free society.⁴⁵ Put another way, promises are not the equivalent of a transfer of property title, and while it may be moral or responsible to keep one's promises, it is not the function of law (i.e., the legal application of coercion or violence) to enforce morality or the keeping of promises.

Rothbard further parts company with most treatments of the free market economy in his analysis of the proper role of government or the state in the economy (e.g., provision of a legal code, supply of police and fire-fighters, road building and maintenance, delivery of the mail, etc.). The crucial features of the state are its monopoly on the use of violence—the police, the armed services, and the courts—and its decision-making power in disputes over crimes and contracts. The key feature that distinguishes the state from private persons and groups is that the former obtains its revenue by coercion, known as taxation,

whereas the latter obtain their income voluntarily by selling goods and services to others or by voluntary gift. To Rothbard, taxation is theft, pure and simple.⁴⁶ If taxation is compulsory, and therefore indistinguishable from theft, the state is the most formidable criminal organization in history. How can the most formidable criminal organization in history enjoy the legitimate right to perform any task? To repeat, the use of coercive taxation to acquire revenue and the compulsory monopoly of force and ultimate decision-making power over a given territorial area on the part of the state constitute criminal aggression and depredation of the just rights of private property of its subjects. In addition to the state's inherent immorality, Rothbard contends that the services generally thought to require the state—from the coining of money to police protection to the development of law in the defense of property rights (all part of Friedman's legitimate role for government)—can be and have been supplied with greater efficiency and morality by private persons.⁴⁷

A Rothbardian rating of economic freedom would be the simplest measure to construct: it would rest solely on the extent to which all resources in any economy are held in the form of valid property titles and are subject to voluntary exchange with no interference by the state. Since every country in the world has some state interference in the economy, a rating scheme based on Rothbard's libertarian vision is more Utopian than practical. Every other philosopher of economic freedom, from John Locke to Adam Smith⁴⁸ to Milton Friedman to Robert Nozick, grants specific, if limited, powers to government or the state, including the power to tax, enforce laws, maintain order, and defend the nation. Rating schemes based on these alternative conceptions of economic freedom would permit larger measures of government activity. They would also take into account the real world activities of governments.

Notes

1. This review is not exhaustive due to space limitations. The main points, however, are fairly well covered in this brief selection of philosophers.
2. The 1981 Chinese-English edition of the dictionary issued by the People's Republic of China treats freedom in a wholly different vein. To the Communists in mainland China, "freedom" signifies the undesirable nature of "the petty bourgeoisie's individualistic aversion to discipline." Other illustrations of the use of the word freedom include "bourgeois ideas must not be allowed to spread unchecked" and "liberalism is extremely harmful in a revolutionary collective." All these aspects of individual freedom are anathema to China's Communist leaders. It should be noted that the word for freedom did not exist in the Chinese language until it was imported from the West in the nineteenth century and a suitable Chinese translation provided. Unfortunately, the characters that were chosen to translate freedom into Chinese remain mired in China's cultural context, in which individual economic activity is regarded as selfish and greedy. These meanings are reinforced by communist ideology.

In recent years, China has been experimenting with market reforms. The National People's Congress approved two constitutional amendments in April 1988 that authorize private enterprise and the transfer of land rights by private groups and individuals. Some American Marxist scholars are worried that Deng Xiaoping's liberal reforms may divert China from socialism down the capitalist road and they warn of the dangers that would result if private property is reconstituted. For this novel view see Cliff DuRand, "The Reconstitution of Private Property in the People's Republic of China: John Locke Revisited," *Social Theory and Practice*, vol. 12, no. 3 (Fall 1986), pp. 337-50.
3. The cuneiform symbol for "liberty" is found inside the binding of Liberty Fund, Inc. publications.
4. In *Politics* Aristotle injected one phrase suggesting that individuals should be free to pursue their own self-interest, but this one brief homage to the rights of the individual was swamped by the general notion that the purpose of political society was to foster the "good."
5. Carl J. Friedrich, *An Introduction to Political Theory* (New York: Harper and Row, 1967), ch. 1.
6. Sun Yat-sen, the founder of modern China and author of the *San Min Chu I* (*Three Principles of the People*), fell victim to the same error in interpreting Western principles of nationalism and democracy for China. Freedom, as he understood it, meant the freedom of the Chinese nation from foreign influence, not the freedom of individuals protected under the rule of law. Moreover, the practice of democracy was limited to the selection of leaders who, once installed in office, were relatively free from further constraints on their behaviour.
7. For a historical and philosophical treatment of classical liberalism, see John Gray, *Liberalism* (Milton Keynes, England: Open University Press, 1986).

8. Blackstone's *Commentaries on the Laws of England* illustrates these safeguards with an entire book devoted to the rights of persons and another to the rights of property.
9. David Hume's *Political Essays*. Edited, with an introduction by Charles W. Hendel (Indianapolis and New York: Bobbs-Merrill, 1953), pp. 25, 32-34. See the political essays entitled "Of the First Principles of Government" and "Of the Origin of Justice and Property."
10. See Alvin Rabushka, *From Adam Smith to the Wealth of America* (New Brunswick: Transaction Books, 1985), chs. 1-7. Historian A.J.P. Taylor vividly summarized the extent of economic freedom in nineteenth-century Britain as follows:

Until August 1914 a sensible, law-abiding Englishman could pass through life and hardly notice the existence of the state, beyond the post office and the policeman. He could live where he liked and as he liked. He had no official number or identity card. He could travel abroad or leave his country for ever without a passport or any sort of official permission. He could exchange his money for any other currency without restriction or limit. He could buy goods from any country in the world on the same terms as he bought goods at home...broadly speaking, the state acted only to help those who could not help themselves. It left the adult citizen alone.

See *English History 1914-1945* (New York and Oxford: Oxford University Press, 1965), p. 1.

11. The full title is *An Essay Concerning the True, Original, Extent and End of Civil Government*. Throughout I will be citing *Social Contract: Essays by Locke, Hume, and Rousseau* (New York: Oxford University Press, 1962), pp. 3-143.
12. One can't help but wonder how the history of China and other great civilizations might have differed had John Locke written for or been imported into those countries. China, in particular, failed to develop the institutions of private property and the rule of law, and thus remained mired in its Confucian heritage, which opposed the development of private mercantile and business activity. It is no surprise that the emergence of Chinese business and commercial interests took place largely in Southeast Asia primarily in British, but also in French and Dutch colonies, wherein the institutions of private property and the rule of law permitted enterprising Chinese to accumulate wealth without the fear of arbitrary confiscation by a hostile state.
13. Locke drafted a constitution for Carolina.
14. See Alvin Rabushka, *From Adam Smith to the Wealth of America*, chs. 1-7.
15. *An Essay*, para. 4, p. 4.
16. In arguing that the natural and inherent right of property existed before the community, and was not created by the recognition and guarantee of the community, Locke's assertion served the interests of the propertied classes among the Whigs. (Hobbes, in contrast, held that property was created by and therefore subject to the control of government.)

17. The law of nature would be in vain without a corresponding right to punish its transgressors. But with each man as his own judge and jury, the right of punishment is imperfect due to partial judgements, inadequate force for the execution of judgements, and variety in the judgements passed by men in similar cases. To remedy these imperfections, Locke proposes a judiciary to administer the law impartially, an executive to enforce the decisions of the judiciary, and a legislature to secure uniform rules of judgement. Imperfections in the right of punishment are thus resolved by consenting to make a community or government to which men transfer these rights of punishment.
 Locke goes on to describe the state of war, in which one man employs the use of force, or coercion, to set himself against another man's life. To avoid the state of war is one reason why men quit the state of nature and form a common society, thereby creating an authority that curtails and grants relief from the state of war.
18. In this view, a man cannot consent to enslave himself to any one, since slavery is a violation of the liberty of man found in the state of nature.
19. *An Essay*, para. 27, p. 17.
20. *Ibid.*
21. This contention forms the foundation of Murray Rothbard's libertarian society. See *The Ethics of Liberty* (Atlantic Highlands, N.J.: Humanities Press, 1982), pp. 21-24. Rothbard will be examined in more detail later.
22. *An Essay*, para. 29, pp. 18-19.
23. In 1690 Locke insisted that the world had land enough to provide for double its population. Thus, the application of labour by one man need not deprive others of similar rights to private appropriation.
24. Productive persons are clearly more valuable to society than the shiftless and idle.
25. A more accurate word might be usurpation or seizure.
26. "Nothing was made by God for man to spoil or destroy." *An Essay*, para. 31, p. 19.
27. This provision, in effect, allows and justifies the accumulation of fortunes and large landed estates.
28. Mutual consent in Locke corresponds to the features of voluntariness and unanimity found in market exchange described by modern writers.
29. *An Essay*, para. 85, pp. 49-50. It should be noted that Locke uses the term "property" to encompass life, liberty, and real estate.
30. *An Essay*, para. 19, p. 58. This phrase is the only application I can find of the principle of super-majority anywhere in the *Second Treatise*. Locke nowhere discussed the costs and benefits of requiring a decision rule other than a majority. He observed that the formation of political society is the consent of any number of freemen capable of a majority. It should be noted that the scope and size of government in his era, excluding periods of wartime, was so limited that Locke probably could not have fathomed simple majorities taxing and spending from one-third to one-half or more of the national income.
31. *Ibid.*, para. 124, p. 73.
32. The objective of law, and thus legislative power, is the protection of property.
33. *An Essay*, para. 138, p. 81.

34. On the basis of this wording it is possible to argue for either the merits of proportional or progressive taxation.
35. *An Essay*, para. 140, p. 83. Taxation without representation in colonial America was taxation without consent and thereby violated the rights of colonial settlers.
36. *Ibid.*, para. 143, p. 85.
37. The major political issue of the 1990s in the United States may well be the gradual inclusion of Members of Congress under those laws they have imposed on all residents in the United States except themselves (e.g., affirmative action, health and safety requirements, etc.). Locke's stipulation insures that laws will be made for the public good, not the private benefit of the legislators.
38. In short, Locke's individuals have an implied right of constitutional amendment.
39. Chicago and London: University of Chicago Press, 1962.
40. In *Free to Choose* the Friedmans enumerate a list of specific measures that, if enacted into the United States Constitution, would enhance individual economic freedom.
41. *Ibid.*, p. 14.
42. Friedman does not delve into the origin of property rights.
43. Atlantic Highlands, N.J.: Humanities Press, 1982.
44. *Ibid.*, p. 59.
45. *Ibid.*, p. 133.
46. *Ibid.*, p. 162. The only exception to the theft thesis of taxation is the unanimous voluntary payment of taxes by every person in a society.
47. *Ibid.*, p. 187. Rothbard refutes modern alternative theories of liberty in part IV of his book. This includes utilitarian free market economics, on the widely recognized grounds that utilities and costs are subjective and cannot be added or weighted to estimate social utility or cost. He challenges the unanimity principle as groundwork for a free market of voluntary and contractual agreements on the basis that the principle has nothing to say about the goodness of the existing status quo, only on changes from that situation. If the status quo represses liberty, the unanimity principle is a barrier to it. He faults Isaiah Berlin's treatment of negative liberty—the absence of interference with a person's sphere of action—with Berlin's later charge, stung by his critics, that unrestricted laissez-faire violated negative liberty by restricting free expression or association, and that personal liberty suffered during the reign of unfettered economic individualism by referring to children working in mines and mills, people in poverty and disease, etc. He parts with Hayek on the grounds that Hayek's government and its rule of law creates rights rather than ratifies or defends them. He devotes his lengthiest critique to Robert Nozick, attempting to show that Nozick failed in his demonstration of the need for a minimal state on ten separate counts, including issues of taxation, voting or democratic procedures, the prevention of the slippery slope from minimal to maximal state, and so forth.
48. Adam Smith believed in publicly-financed education, public works, and the Navigation Laws, among other legitimate activities of the state.

Discussion (Chapter 2)

Alvin Rabushka My interest in this general subject grows from a quarter century of first-hand observation of Hong Kong and its enormous amount of economic freedom. There is more economic freedom in Hong Kong than in virtually any other country in the world, even those that have considerably higher incomes per person.

The social science enterprise does a number of things: it develops concepts, tries to employ concepts and theories, seeks to explain reality, and tries to accomplish these tasks in qualitative, comparative, and quantitative ways. My interest is in doing these things in the most rigorous way possible over a period of time. I don't anticipate a resolution in two days. I'm not sure I anticipate a resolution in five years. But I am certain that there will be many who attempt to dismiss these ideas after two days as an insoluble task, and I am quite sure that in the course of human history, problems have been solved that have similarly been dismissed out of hand after an initial day or two of conversation. In the scientific spirit of being open minded in examining ideas, I am not prepared to sign by the end of tomorrow a statement saying that this is a fruitless and hopeless prospect. I can't guarantee how far we will get but I think over a period of years we will make some progress. However slow and however little it is, it still may be worthwhile in its own right and on its own merits.

As I thought about how to structure the subject, my first point was to get a handle on economic freedom. Before one can rate economic freedom, it is valuable to talk about its conceptual underpinnings. When one looks through the philosophy of economic liberty, it is clear that different people have taken different issues, have given different conceptual treatments of it, and have tried to define what they think economic freedom means by pointing to different sorts of minimum conditions.

I also believe there is some benefit to be gained by trying to move this concept forward out of the truly intuitive into something much more precise and conceptually more quantitative. The more attention that is focused on it, the more likely there will continue to be some incremental thinking about it. The more people who can be enlisted in this effort, the more likely contributions can be made to it.

Finally, it is desirable to get people to acknowledge that it is as valuable to talk about economic freedom as efficiency. I tried to put on the table what I felt some of the philosophical treatments were, some key people, and what they said. I found a greatly renewed admiration for John Locke. What comes out of John Locke is the critical issue of private property. John Locke takes us through his thinking, going back to the state of nature, the existence of God, the fact that men are equal in separate units in a state of nature, and that in the state of nature there isn't perfect freedom but there is the problem of punishing transgression. What do you do? You have to surrender some of your liberty into the collective to

protect it. I found it very worthwhile to go through property in John Locke and then Blackstone's commentaries—one of the four volumes he wrote is just on property, a very long account of all the intricacies of the law and how it protects property.

I was troubled with Locke. He went to simple majoritarian democracy as the vehicle that subsequently makes decisions on how one is going to protect the society one creates because of this problem of individual punishment. But he was also very clear that man does not surrender his freedom because he contracts it in a society; rather, man continues to have his freedom.

From Locke to Friedman, I have jumped several centuries. How do you secure individual freedom through the miracle of the marketplace? In looking through *Capitalism and Freedom* I found five points: the maintenance of law and order, the enforcement of contracts; the definition of property rights (that's a little bit different from Locke); and a monetary framework (that is completely different from Locke's concerns about monopolies and externalities).

In *Free to Choose* Friedman presents an economic bill of rights. I'd like to make an observation that isn't in my paper because something absolutely unique in modern constitutional history is occurring right now. The Chinese government is drafting a basic law or a mini-constitution for what will become the Hong Kong Special Administrative Region in 1997 when Hong Kong sovereignty reverts from Britain to China. Chapter 5 of this draft basic law is entitled, "Economy." In this there are lists of articles in very simple Chinese that translate into very simple English. These include such statements as, "Hong Kong shall continue to practise a low tax system." By that it means the government of Hong Kong, by constitutional requirement, shall not have a high tax share of GNP. "Hong Kong shall, taking one fiscal year with another over a series of years, run a balanced budget." Another point is that "the rate of growth of taxation and the rate of growth of expenditure shall not exceed, taking one year with another, the rate of growth of the economy," which is a tax or expenditure limitation. This is an explicit and concrete article.

There are other explicit and concrete articles which say that Hong Kong shall remain a duty-free port with no customs tariffs, and that it will maintain a policy of free trade save for safety and health regulations. There are provisions on commerce that require free entry and free exit. Unregulated prices are implied in all of this. There are also a series of precise and specific measures having to do with monetary policy, that is to say, "the Hong Kong government shall be required to make it a convertible currency." Therefore, there shall be a free market in money. It goes on to say that this convertible currency shall not under any circumstances be a fiat currency but must be 100 percent backed and that backing shall take the form of external convertible reserves such as U.S. dollars, deutsche marks, yen, gold, and other potential commodities.

Milton Friedman Who drafted this?

Alvin Rabushka There was a committee set up of sixty-odd persons of which about 60 percent were mainland Chinese and 40 percent were Hong Kong Chinese. By and large they tried to maintain the concept of one country, two systems, and guarantee that Hong Kong's capitalistic system would remain unchanged for 50 years after 1997, to give confidence to local and foreign investors in Hong Kong that the capitalist system will not be merged into the socialist system. They took the existing sense of economic institutions and policies and wrote them up as constitutional maxim.

What's intriguing is that if you take chapter 10 of *Free to Choose* and look at the seven amendments, I believe they are all there. I should go on also to state that earlier on in chapter 1 of this constitution there is a very clear statement about the definition of the maintenance and enforcement of private property rights. The very first statement is that Hong Kong people "shall enjoy the rights of private property, to buy, sell, exchange, and dispose of them as they see fit without government restriction." There is a whole series of statements about the judiciary. They, unfortunately, didn't carve those up and that is because the Chinese have a very peculiar notion of law which historically has been garbled.

I just wanted to indicate here that we are talking about a device being written by one of the most totalitarian communist countries on the face of the earth which no capitalist society has ever written—there is the occasional state in the United States which has to run a balance budget—but nowhere in the history of any national constitution can one find this activity. This is the first one, and it is quite ironic that a communist system has written of its intention to maintain a capitalist society. To the extent that constitutions work, that is, are honoured, enforced, and supported, we might be inclined to say the society will have a greater measure of economic freedom. The Chinese seem to believe that prosperity and good things flow from these provisions.

My last point. I also thought it worth mentioning Murray Rothbard because when one is talking about alternative philosophical conceptions of economic freedom one could say his is the simplest, imposes the least number of minimum conditions, and would be the easiest to derive and develop a measurement set for. All that he basically requires is a set of property rights growing out of a Lockean state of nature that ensures somebody doesn't steal illegitimately from someone else, and that ownership titles can be freely exchanged. He parts company from Locke, Friedman, and almost everyone else on the role of the state because a penny of taxation taken coercively makes the state a criminal organization in his view, and therefore there is no place for the state as there is among other schools of freedom. I would like to see a consensus develop about those core conditions or minimum requirements that we think make up the essence of economic freedom. From that we can begin to think in terms of breaking those into more refined and clearer notions until finally there is some empirical indication of what they are.

Henri LePage I'd like to make a few comments in line with the topic of this session. First, I was somewhat worried about the kind of utilitarian bias with which we started the previous session. For me liberty is mostly related to rights. Basically, it is an issue of individual rights. That's why I feel more comfortable with the philosophical approach.

I want to comment on an issue which has not been raised up to now. That is the fact that we distinguish between economic freedom and political freedom. I don't mean that we should not do this, but we must be very careful when we do, because once we start we implicitly introduce a kind of hierarchy, and end up by justifying economic freedom in terms of political freedom. For example, we often justify economic freedom because experience shows that we can have political freedom only when we also have economic freedom. So we justify economic freedom mostly in terms of consequences, in terms of political freedom. That means we introduce a hierarchy. By this means, I am afraid, we adopt the position of our opponents who usually put political freedom first and rate economic freedom a long distant second.

I think we have basically two theories of freedom. First is the classical liberal definition and second, the non-liberal definition. The classical liberal definition starts from the basic notion of self autonomy and non-interference. That means it starts from individual rights. From this you deduce a number of rights, but they all have the same status. And liberty is the sum of the bundle of rights. If you take only one right out of the bundle there is less liberty. In this definition, political liberties are just instruments, merely conditions needed to realize individual rights. They have a subordinate status.

In contrast, the non-liberal definition starts from a legal definition. You are free when nothing illegal is done to you. When you start with that definition you end up with political freedom as basic. Since everything depends on the legality of what is done, you have a vested interest in investing more and more into the political process in order not to be victimized. We end up with the present system where political freedom comes first and economic freedom comes last.

My third point is that liberty is defined in terms of property. It is the very same thing. It is not only constitutionally the same thing but historically it began the same way. Never forget that the concepts of individual liberty, free will, and private or individual property were developed in the Middle Ages out of the concept of dominion. They have the same conceptual rules. This gives us a clue as to the way to measure the presence or absence of liberty. It would be a negative measurement. We could devise an index adding up all that is infringing on individual property rights (using the Lockean definition). Then we would have a subsequent listing of positive rights enumerating only the political conditions that are necessary for the existence and conservation of individual rights.

Richard McKenzie I would like to try to add some clarity to what we have been doing here and also make a suggestion for the last session. It seems to me that the discussion is organized around three facts. One is that freedom has various meanings, as mentioned. The problem is that the meanings and dimensions are practically boundless. Secondly, we all have our own idea for a measure of freedom. Michael has his needs in terms of manipulating the government in Ottawa. Milton has his needs for econometrics, and I want to seek truth! (laughter) These needs are somewhat constrained by the fact that we are all Walter's friends. But we do have various needs.

Thirdly, I think we would agree that there are certain economies in proposing a common definition or measure of freedom. There are pressures to go ahead and come up with a measure to suit our own particular purposes. Really, what we seek here is some sort of reasonable compromise on that measurement. That is, what would go into it in order to take advantage of the economies that are there. I mean we are going to constrain the set; we are going to make compromises because they are advantageous. I know what I would do if I had a measure over time of economic freedom. Given my current research, I would try to assess the impact of capital mobility on economic freedom. I would predict that the growing capacity of capital to move internationally would lead to more freedom. And I might even be interested in the impact of economic freedom on tax rates. Here I would predict that tax rates would decline.

Maybe at the next meeting we might go around the table asking each person to indicate what would he or she include in the definition of freedom. Personally, I like Alvin's introductory remarks because I think he puts together a great list. Indeed, one might argue that the people he covers were more sincere in coming up with a definition than we could ever be around this table simply because they were dealing with a very small country that was open to the rest of the world. They wanted to keep the capital at home and they had some very private economic interests in coming up with a solid, confined set of components. My first impulse is to go down the list and determine how we can measure this, and this, and if nothing else, just add them up.

Ellen Paul Without getting too diverted from the main topic, I would like to pursue some of Alvin's remarks on the constitution proposed for Hong Kong by the Chinese Communists. I found his remarks fascinating. I think it will be a great study, whether this proposal for economic freedom can survive without political freedom. I wonder whether this constitution is something like the Stalin constitution of the late 1930s, which certainly didn't prevent him from killing some 20 million people despite professions much like the First Amendment liberties that we enjoy in the United States. Anyway, this proposal had a very soothing effect on the capital markets in Hong Kong. Things have proceeded with "business as usual."

Looking at the history of communist regimes, I just wonder whether a communist government can tolerate something like Hong Kong's free-wheeling capitalism in its midst. Such governments have to control everything. That has been the battle in China itself: they allow a bit of freedom and then a few months later they start denouncing the people who have taken advantage of it. The Communist Party starts feeling its grasp on power ebbing away when it is not controlling every activity of every individual in the country. That's a very frightening thing for the Communist Party. If this proposed constitution is good enough for Hong Kong, why isn't it good enough for the rest of China?

Alvin Rabushka There is the central question as to whether or not they will over a period of time honour this agreement, and this is designed to be a confidence-builder in the short run. There is no long-run guarantee. The emigration of skilled people suggests that maybe they can't be trusted to honour their agreement.

Remember, this is a very curious and perverse situation. You have a communist regime writing a set of free market principles into a territory that is going to be an adjunct of a communist system. What has been the reaction of the Hong Kong intellectuals to this particular chapter? This will be an astounding statement when I tell you that by and large they have rejected chapter 5 of this constitution as inappropriate for a constitutional instrument. That is to say, they complained that such a set of specific constitutional stipulations in economics ought not to be part of the generally westernized, bourgeois, liberal, democratic, social and political order. And that this will take away the flexibility of the government of Hong Kong to respond to changing circumstances whether it comes to changing the monetary system, taxing at higher rates, maybe affecting trade, and so forth. In fact, there should be some generalized principles in the preface to that effect: "just keep the capitalist system going, and we know what that is." There has been this rejection of this first attempt, even internally. Whereas the communists have felt that in order to maintain confidence, stability, and prosperity in the long run it was essential to put these kinds of conditions in. So you have a very curious, unique circumstance for the first ever national set of constitutional guarantees of economic rights.

Henry Manne What form did that rejection take? Was there a plebescite?

Alvin Rabushka Oh, no. Just open debate in the press and submissions. There are offices set up—you can put in written submissions. From what one can make out in the press about all the various interests groups in Hong Kong—big business, professors, labour, or whatever—the general view is that constitutions in the West do not contain specific economic conditions under which a government should operate. Therefore, it is inappropriate to include in a constitution specific policies rather than generalized decision-making rules. So

you have a people prospering under economic freedom quarrelling with the virtue of a totalitarian system, making it—assuming they honour the agreement—impossible for outside authorities to tamper with the way of life that has brought about that prosperity.

Richard McKenzie The fact that they may not honour the agreement is unimportant. In fact, I think that it is probably true that they will not. What is important is the framework within which that list was developed. That was a veil of ignorance, and you have a kind of veil with the Great Wall. What kind of principles can we come up with if we want to maximize the stability of the amount of wealth in Hong Kong right now? It seems to me that is what that list does.

Ellen Paul This gets more and more intriguing. The implication of it is that this chapter 5 is what the Communist Chinese believe the Hong Kong Chinese want, but they really don't. The mistake the Communist Party in China is making is assuming that the so-called capitalist countries really believe in capitalism, and they don't! I think the only people who believe and understand capitalism are on the other side. In Eastern Europe they read Hayek. They read Friedman. They think that these figures exemplify Western thought. During my brief stint at the United Nations, I had the occasion to discuss market economics with Chinese diplomats. They too were reading Hayek and Friedman, and they are getting a totally bizarre view of what intellectuals are like in the West.

Zane Spindler Who are the actual people being given play in the press? Are they, in fact, future politicians and rent-seekers, that is, proponents for special interests?

Alvin Rabushka There doesn't tend to be any support for this section from any specific group. The only comment on this section tends to be opposition. So far as I can make out, it includes all cross-sections of life from what would be the British colonial government in Hong Kong, Her Majesty's representatives in London, and local business and intellectual communities, that is, any articulate groups who have a stake or interest in this.

As I say in my book *The New China*, if some of them could have their way, and I am talking about those who are in the State Council or the System for Economic Restructuring, Reform—they would go immediately to completely unregulated prices. They would also move rapidly to private property, ownership, and markets. The raging debate in China now is whether one should move as quickly on price reform as on property rights reform, or move quickly on price reform and let property rights reform follow more slowly. I don't think there is any confusion in some circles that though they are writing this for Hong

Kong they wouldn't mind being able to write it for themselves. But it isn't that easy to write it for themselves and put it in overnight.

Milton Friedman I don't think there is anything surprising about their rejecting it. Unlike Hong Kong, to which Britain has given political freedom, other former colonies, almost without exception, I think, have chosen to become socialist welfare states. However, I don't think that means the people want to do that. As in so many cases you may, I'm not saying you do, have a silent majority, but the people who would naturally object to this are those who hope to have important political positions in the emerging society. They are the ones who will write the letters. They are the ones who will take the trouble to object.

Michael Walker Regarding Hong Kong, somebody, I've forgotten who, has noted that the framers of the American Constitution were largely slave-owners; what a comment on the usefulness of articulating the constitutional restraints on people.

I want to return to David Friedman's point. Just because something is not achievable, doesn't mean we can't use it as a bench-mark. I refer, in particular, to the libertarian notion of freedom.

It seems to me there is a paradox contained within the libertarian notion. Let's go back to Locke's notion of government. It is a co-operative notion. Government is, in effect, a contrivance to further individual ends. Buchanan makes this more precise by noting that individuals may contract to reduce their individual freedoms in order to reduce the riskiness of life. Friedman accepts the notion of some limitation without regarding that as a reduction in freedom since people contract into it or agree to it because they believe it will make their freedom greater in some sense.

Contrasted with those three views and the general stream of historical evolution, the Rothbardian view or the libertarian view, as I get it on a daily basis from Walter Block, is that any attempt, in effect, any departure from individual contracting on a free and unfettered basis is a reduction in freedom. This view seems to be suspended, however, in the case of co-operatives. Co-operatives are not included in this notion because they are conceived of as the contrivances of individuals to pursue their individual ends, although collectively. As long as the co-operative is voluntary, there is no reduction in freedom.

Walter frequently makes the distinction between voluntary socialism and coerced socialism or interventionist socialism. But why can't we conceive of a libertarian utopia for the purposes of our bench-mark measurement? It seems to me that if we are going to talk seriously about measurement, we have to come up with a bench-mark at some stage. We have to have some rule or some background calculus for our deliberations. Why can't we then conceive of a bench-mark that involves a certain amount of contracting into the coercive use of government which at the same time does not involve a reduction in freedoms? In

other words, the maximum choice set would somehow be achieved with some reduction of individual choices which are contracted to by the individuals who make up the policy.

David Friedman First, now that I know the source of Mike's information on libertarianism, I understand why he makes the common mistake of confusing libertarian and Rothbardian.

I think most of us would consider a system where coercion was the result of a voluntary contract as free. I think most of us would agree that if the government said to people, "if you are a drug addict and do not want to be one, you can, if you wish, sign an agreement with us saying, 'please arrest me if I use drugs,'" that would be consistent with a free society. But that is not what we observe in real-world societies. They all insist on imposing rules on people who have not requested them.

I want to try to make some further attempts at terminological clarification. The first is to point out that multi-dimensional does not mean unmeasurable. Freedom is multi-dimensional because there are many different things with regard to which you can be free, and there is no natural way of comparing them, of adding them up to give one number. So you have what mathematicians call a "partial ordering" of societies by how free they are. If country A has a certain amount of freedom in each dimension and country B has as much freedom in some dimensions and more in others, then we can say that B is freer than A. But if country B has more of some freedoms and less of others, then B and A are incomparable, and that will often be the case. You might still have a clear conceptual definition of freedom. The problem is that the freedom of a society is not a number but a vector, so you have only partial orderings among societies by how free they are.

So the first question is, if you think of freedom in that way, what are the problems in defining it? A later question would be, given the definition of freedom, how do you compare the freedom of different societies?

One issue involved in defining freedom is whether to include private restrictions as well as governmental restrictions. This takes us back to the argument between my father and Ellen Paul. Suppose the alternatives are government rules against pollution or a society without such rules. Further, suppose that in the latter case, even though individuals have a legal right to sue polluters for damages, the public good problem in litigation makes it impractical for them to do so; the result is that individuals pollute the air of other individuals. Which society is less free?

One way of looking at it is to say that in the first case we have a restriction of freedom because it is done by the government. In the second case, we may be worse off but there is no restriction of freedom. A different way of looking at it is to say that in the first case we have restriction of freedom by government and in the second case we have restriction of freedom by private polluters who succeed

in coercing us. So one question to ask ourselves is whether it is better to limit our inquiry to restrictions on economic freedom by governments, perhaps on the grounds that they are a lot easier to observe and measure, or whether we want to include all restrictions on economic freedom, private and governmental.

If you settle that question, there is then the conceptual issue: is “a restriction on freedom” well-defined? That takes us to the problem of whether there is a single natural set of property rights. Seen from one angle, a legal regime where I cannot pollute guarantees your freedom; seen from another angle it restricts mine. It may be that there is no way of defining property rights that entirely eliminates conflicts between rights, no definition that results in no third party effects. If so, one might argue that the idea of a perfectly free society is itself internally inconsistent.

The point I want to make is that even before we worry about a single scale for freedom, even if we accept the idea of a multi-dimensional definition, we still have the problem of whether that definition includes restrictions by other human beings who are not government. I think most of us agree that we should not include restrictions by nature because that is not a matter of freedom, but even given that, can we clearly define what we mean by restrictions on freedom? My instinct is to say we cannot do it clearly, but we can do it. My guess is that there is no well-defined “right” definition of property rights, but that most of the plausible definitions of property rights would have an overlap of 97 percent or so. But I do not claim that I can prove that.

I now want to get back to the point I raised in the beginning. If you have a definition of freedom, then even if you can’t calculate a single measure of the amount of freedom, you may still be able to determine a single measure of the value of freedom to people. That seems the most natural way of getting out of the problem of multi-dimensionality. Countries cannot be ordered by how much freedom they have, since freedom is multi-dimensional, but they can be ordered by how their citizens value the freedom they have, or the cost of their restrictions on freedom, since that is uni-dimensional. One could then ask how countries compare, and try to make some general list.

James Ahiakpor Alvin includes “defining rights” among the legitimate functions of government. That bothers me because if government has such a function it could define rights so as to impair them. I am saying this because I thought we could define rights from nature, that is, from natural rights. We would then get into a distinction between rights and privileges where privileges are concessions voluntarily made by people to allow others to perform those actions that otherwise would appear like infringements on their own property rights. If I give my keys to a friend to come to my room any time he wants, that’s a privilege which I can take away. Since we have Milton here, on whose authority Alvin partly bases his arguments (Alvin can also answer), perhaps we

can get an explanation of why government has a legitimate role in defining rights and not simply enforcing property rights?

Milton Friedman The answer is very simple. Because there is no unambiguous natural definition of property rights. My example is also very simple. It shows how the concept changes over time.

If an airplane flies over your house at 30,000 feet, is the pilot violating your property rights? What if he flies over at 50 feet? Did Locke think of that when he was defining property rights? It is arbitrary. What is important is that you have to have some way of determining what people's rights are when deciding disputes. The most effective way is somehow or other to have a mechanism for specifying what property rights are.

If I were re-writing this list today I think I would add one more thing that is left out of almost all the discussion here but is enormously important. I would add stability as one of the things defined as very valuable. Consider two different hypothetical definitions of property rights. Suppose we would all agree that in and of itself, one of them provides freedom. The other is less free. But the first one is changed every year and the other one is subject to no change over a 20-year period. I would say that there is a component or dimension of freedom preserved in the second. And somehow our freedom is less interfered with by a system of taxation than it is by having it changed every year. You have to ask, if you are not going to have a government, what mechanism do you propose for defining property rights, by which I mean for deciding controversies among people about what their rights are. Whether that means flying over your house has violated your property rights or not.

James Ahiakpor I think the definition of property rights is a philosophical issue which should not be determined by government, although the government may provide a means of enforcing the issue.

Milton Friedman What's enforce?

James Ahiakpor I think we can start from natural rights where they entail the facility or the ability to exercise, acquire, or enjoy something without the intervention of another person.

Milton Friedman You have a hi-fi system that you enjoy as your property and the man next door has his hi-fi at such a high volume that you can't sleep.

James Ahiakpor That is infringing on my right to quiet.

Henry Manne What level of noise should be allowed?

Milton Friedman What's his right to make noise?

James Ahiakpor We are getting to what I said...this is an extension of the philosophical debate over rights.

Milton Friedman How do you do it? You can't get out of this by saying you are not going to assign the defining of rights to government. Just tell me how you are going to do it.

James Ahiakpor This is what I said, that definition of property rights is something outside of the functions of government. It has to be decided through debate. Government can only provide a medium for enforcing what has come out of the debate.

Milton Friedman But nothing has come out. These two people differ. How does government know what to enforce unless there is some specification of what the rights are? Without this, government has no basis for enforcing anything.

Henri LePage I want to give a short reply to Michael by saying that contracting doesn't give you the rights he thinks it does. You can contract for yourself—but you cannot contract for somebody else, not even for your children. This is the main difference between government and the co-operative association; it is a gigantic difference, often overlooked. In a co-operative association you pledge yourself, you pledge nobody else. In government you pledge all your descendants plus all your fellow citizens, whether they agreed or not, into the coercive power of government. This is a very big difference.

Henry Manne David referred earlier to the matter of the value of freedom. It seemed to come down along the line of items that would be measured in this scheme we are discussing. I have great difficulty with this. I don't know how you can talk about the value of freedom if there is no efficient market...if nothing is being exchanged...if individuals aren't demonstrating the value they place on things. At the margin, all goods, political, economic, moral, whatever, can be substituted. That leads me back to the point I made earlier. Perhaps I didn't express it as well as I might; let me try again. Wealth, in the usual economic sense, is probably the best—I may have implied “only” before—measure of freedom. There isn't any other kind of metric you can come up with.

Alvin, I would vie for the honour of being first within two days to say that what you are trying to do is impossible. It seems to me it has already been demonstrated here.

What I don't understand is why there is resistance to the notion that wealth maximization is a proper surrogate for freedom maximization. Dick Posner

raised precisely this issue when he proposed wealth maximization as the proper utility function for judges in maximizing justice, as it were. Those of you who were at the San Vincent Mont Pèlerin meeting in 1987 will remember that he finally got that absolutely straight. It came very close to a libertarian notion...the earlier difficulties between a utilitarian and a non-instrumental view were pretty much ironed out and he realized that he was talking about the market minimizing transaction costs and protecting property rights. I think that is the same issue we are addressing here. If you want to do something politically practical, we should continue to do what we always did; and that is try to educate people that the free market is better for them than the government systems they seem to opt for.

James Gwartney I think the concept of personal freedom is very closely interwoven with property rights; this is true not just of economic freedom but of civil and political freedom as well. In a fascinating piece that I am sure some of you have read, *On Property Rights*, James Madison makes the point that individuals have property rights to their opinions. He then talks about non-intervention and those things which interfere with their freedom of property rights and their religious views. Property rights extend both to freedom of expression and to physical things. This discussion took place in the context of the debate about the Bill of Rights.

I guess I am a little troubled about separating too quickly the concepts of economic freedom and political and civil freedoms. This may lead to a kind of hierarchy of thinking about freedom, where political freedom is still at the top of the hierarchy. I think there is danger in the conceptualization of freedom.

If property rights are the key to understanding freedom, then it is important to determine who decides how the property is used. It is important to distinguish between (a) the individual who decides the use of property, or groups of individuals voluntarily entering into a contract and deciding the use of property, from (b) the requirement that in order to use property, you have to have collective approval—a sort of collectivism. The former is the heart and soul of freedom; the latter is antithetical to freedom. This is really the key distinction.

Whenever we talk about property, we must consider the third party effects. Of course, these are very troublesome issues. It is important that we make at least three distinctions with regard to actions that influence the value of another's property. Clearly, if I use my property in a way that physically invades someone else's property, or more generally, if I use my property in a way that changes the nature of the other individual's property, then I have violated their property rights.

One can also think of other cases where I may not change the nature of the property but nonetheless other individuals feel that they have been damaged. The clearest case of this is where I devise a better mousetrap so the guy who was previously selling mousetraps feels that he has been damaged. In this case I didn't change the nature of his property at all. His mousetrap production facility

is just like it previously was. Nonetheless, I still changed the value of his productive asset because I devised a better or cheaper method, which reduces his wealth.

A third way that I may damage another person is when I fail to change the nature of the individual's property but nonetheless do something that he doesn't like. Maybe I have certain religious views on drug use, homosexuality, or something of that sort that others find offensive. They are damaged by my behaviour but there has not been any change in the nature of any property that they own. The damages emanate from their subjective reaction to my action.

Building on the point that Rose made earlier, we have to tie down what we mean by this concept of freedom. I would encourage us, in terms of moving in that direction, to think about these three types of actions that damage somebody else. One is when our actions change the nature of the property that someone else owns and in which case we would say we violated their actions and, therefore, we are not free to use our property in that way. The other two are the competitive actions I referred to when our actions damage someone because they conflict with the other person's subjective preferences.

Ellen Paul Other things equal, it is better to have stability of institutions. But what if those institutions mandate that the state owns all property or that when small businessmen become too successful the state will nationalize their companies? Anytime revolutionary change is contemplated there are, undoubtedly, grave risks, but sometimes the oppression is so great that the risk is worth it.

But my main point is to dispute a kind of glib attack on the natural law that several people repeated, Dick included. If you look at the natural law theorists and read them, they are basically saying the same things. What are natural rights? What are the rights that people have? The Benthamite attack on the natural law school was simplistic, but it is still endlessly repeated. The advocates of natural law believe there are moral laws that ought to be obeyed in all times and at all places, and that we violate them at our peril. While there are some differences between theorists over details of the natural law, these deviations are remarkably slight, given the often great differences in culture and time in which the various writers wrote. They may differ, for example, over how one comes to own property—by first occupancy merely, or by mixing one's labour with the land. But they do not differ over the right of individuals to own property.

Henry Manne There is scarcity in nature. Scarcity leads to conflicts. We need in society some mechanism to resolve conflict. So the society that is freer is the one capable of resolving or preventing conflicts with fewer constraints. All rights have many aspects, and one aspect is that the tenure of a right, if not guaranteed, is worth less. Another aspect is its cost of enforceability. If I have an

individual right, but it is very costly to me to enforce it, then it is not worth much to me.

Michael Walker First, let me respond very briefly to Henri on the question of contracting for yourself but not for your children. It seems to me that fundamental contracts that restrain freedoms, such as those that restrain 51 percent of the population from imposing taxes or even worse kinds of rules on the 49 percent, are timeless inhibitions on the right to contract, and you would want to impose those both on yourself and your children in some fundamental way. This is not to say that they are not changeable with constitutional resolution.

Then you want to make a distinction between that and the kind of contracts we make that are framed in legislation, say, noise by-laws which state that we all agree that you shouldn't be able to run your stereo at 12 o'clock at night and impose unduly on somebody else's right to silence.

But the main point I want to make is to respond to Jim Gwartney about the difference between economic and civil rights and the distinction between those and political rights. It seems to me that economic and civil rights are negative rights. Freedom from coercion. Whereas what we call political rights are really an extension of the right of contract that results in surrendering economic and civil rights. Presumably we do so because of the perception that it will lead to a broader choice or freedom set. When we talk about political rights we are really talking about the right of individuals to opt for a contract that will provide them with less freedom, à la Buchanan; people will opt for a government that imposes taxes because they believe this will lead, in some ultimate sense, to a broader choice.

David Friedman I have one comment for James Ahiakpor and one for Jim Gwartney. The comment for James is that if the government is enforcing rights, then it is ultimately deciding what the rights are. It may do that by deciding which of several philosophers to believe. But if there is a government court where you can go to enforce a right, then that government court is going to decide whether you have the right. This means a government court is going to decide whether it believes philosopher A's version over philosopher B's. If you really want to get the government out of the business of defining rights, you must get the government out of the business of enforcing rights, which means you have to move all the way to an anarchist system.

The second comment is for Jim. I am very sympathetic to the way you want to distinguish different third party rights, but I would like to point out that it may be a harder problem than it seems. The basic problem is that what counts as your changing my property depends on my subjective tastes. The sharp division between my property and yours is an artifact of the way we are thinking. For

example, we all breath out. We therefore exhale carbon dioxide, which is a pollutant. We therefore all affect each other's property.

Suppose that I not only dislike homosexuals but dislike them so much that I regard breathing a molecule of carbon dioxide that has been breathed out by a homosexual as a dreadful thing to happen to me. That is a subjective belief; I have the right to have any subjective belief I want. I therefore enjoin everybody who is close enough to refrain from engaging in homosexual acts so that the exhaled carbon dioxide of homosexuals will not ultimately drift onto my property. And I claim I am doing so on strict libertarian grounds. Their acts have a measurable effect on my property, providing I am willing to go to the trouble of measuring the carbon dioxide level accurately enough. And that effect injures me. It injures me only because of my rather peculiar subjective tastes, but then I am entitled to have whatever subjective tastes I want.

In a way this is far flung example, yet it makes clear the problem with simply talking about my right not to have you affect my property. We cannot define property in a way such that your routine activity does not affect it, whether by your carbon dioxide molecules trespassing onto it, or by photons bouncing off of you and onto my property—as demonstrated by the fact that I can see you. Our normal working definition of property always involves, implicitly if not explicitly, some idea of what effects we can ignore because they are insignificant. That ultimately depends on what effects injure me and by how much, which depends on my values—which are subjective. That is an unfortunate complication. I am not sure how one deals with it but I want to point out that it is there.

James Gwartney I want to tread into some very dangerous waters because I am precariously close to finding myself in the position of not only being in conflict with Milton but also with David Friedman. This reminds me of a monetary theory class I took once. The lecture was given by John Floyd (a former student of Milton's), who stated that he had a point of conflict with Milton's position. He said, "Milton's wrong on this issue" and he proceeded to give his reasons why. Then at the end of his comments he said, "Of course, if Milton were here he would have me pinned to the side of the corner next to the blackboard explaining why I was wrong." So I sort of feel the same way that John Floyd felt that day.

It seems to me that this issue about the airplane—whether it has invaded someone else's property when it is flying at 30,000 or 40,000 feet—has to do with where you draw boundaries rather than the nature of property. It is an issue about the boundaries of property and not an issue about whether or not the property is going to be private or collective. Once you make some decision about where the boundary is going to be, you allow private decision making to determine how the property is used within that sphere. Whether or not violations have taken place at 5,000 feet or 30,000 feet, you are not going to have some collective authority determine this. I keep going back to this idea of collectivist

decisions determining how the property is going to be used. Once the boundaries are drawn, the usual criteria of English Common Law determines whether or not damages occur. If you can prove damages then you can go to the courts and collect for that damage.

Henri LePage Gerard talked about finding a mechanism to resolve conflicts with as few constraints as possible.

First, I believe that it is the Lockean approach to property rights which has the fewest constraints. But how can you apply transaction costs to the Lockean framework? You would need to measure transaction costs, and to compare them for different individuals. But this is something we cannot measure. It is purely subjective. With the transaction costs theory we end up with a total that is not operational. It is a very powerful analytical tool, but it is not operational. You end up with a kind of utilitarian approach, which leads to collectivism. I think the Lockean approach is in fact much more practical, because by definition, everything belongs to somebody in a Lockean framework. It belongs to the one who has appropriated it, by being the first to place value on something. This is a very practical definition. You can apply it everywhere. By definition, only one person, not several people, may own or may appropriate the same thing.

Then we come to the case of the airplane. By definition, a right exists only when you can petition for it. I think the notion of petitioning is very important. By this I mean you have the right only if you call on the existence of this right. Animals do not have rights because they cannot petition for them. We have rights because as human beings we have free will and we can petition for our rights. This means, for example, that with the air space nobody thought about before the invention of the airplane, no one was concerned with petitioning for the property rights of air thousands of feet up. The problem arose because somebody invented airplanes. I would venture to say that the inventors of the airplanes in effect petitioned for property rights in the air. And they got it because they were the first ones to put value on the air. If people are disturbed by this then they have to negotiate with the natural owner of the air above them.

Alvin Rabushka Coming out of what we would call the liberal tradition, both in a political and economic sense, when you ask what I think economic freedom means and how I would want to use it, I accept this notion of non-interference in the private affairs of individuals, with an emphasis on the protection of property and the rule of law. When one talks about economic freedom, one can talk about it at the level of institutions and rules and the notions of policies and practices.

For example, if you have private property but I have the right to levy a 90 percent wealth tax on it every year, your right doesn't amount to very much. One can't really talk about private property without also talking about what governments do. If you accept the classical liberal notion, you need some kind of civil order to standardize punishments for transgressions, and you need to have

revenues to finance this operation. You have philosophically empowered the collective order to tax, spend, and regulate to accomplish the primary objective of the preservation of property. When you talk about the rights to private property, you are talking about the freedom from coercion to enter into voluntary exchanges and to dispose of your property as you see fit with whomever you see fit. One wants to look at institutions of property, how extensive they are, how well defined they are, how separable, how transferrable, and how freely they enable you to do what you like with the property. On the other hand, one should also look at how encumbered property rights are and how the policies and practices of the collective order can impinge upon them. This is the background of how I let chapter 4 unfold.

When I think about the philosophical aspects of economic freedom, I am thinking about private property. I am thinking about, to the maximum extent possible, the notion of non-interference and predictability of the rule of law.

I want to point out a snag in the wealth maximizing notion by taking the extreme example of a relatively poor country with few resources, but one in which the individuals in that country have clear rights to property and are relatively free from the coercion of others or tyranny of government, and comparing that country to a society which is wealthy due to natural endowments, but is governed by an absolute dictator who is willing to redistribute a lot of his income. So, for example, the Sultan of Brunei has the capacity to enrich the ordinary citizens of Brunei at a level that makes their private consumption choices equal to that of the average American. But all property remains collectively owned, and you simply have a monumental consumption subsidy system.

In a classical liberal notion we would regard the residents of the poor society as having a higher measure of economic freedom than those in Brunei. I may be wrong, but I think Henry would regard the Bruneian as having a higher level of economic freedom. As I think back about the philosophy of science, in the end what constitutes truth and knowledge and understanding? Over a period of time it is the evolving consensus of the relative practitioners of the people studying it. Looking at the heads nodding here, the classical conception of the notion of freedom from coercion gets at it better than the notion of choices based on disposable personal income.

Chapter 4, the preliminary definition, is a kind of checklist or ratings scheme that follows from the way I look at the classical philosophical treatment of economic freedom which really begins with the institutions of private property and the rule of law. Then I look at all the things government does in its relationship to private individuals and those particular institutions, and try to decide what makes for greater and lesser freedom.

Chapter 3

Freedom House Survey of Economic Freedoms

Alvin Rabushka

In 1972 Freedom House originated its Comparative Survey of Freedom, which has become the standard universal measure of the degree of political rights and civil liberties that exists in every country in the world.¹ Each January Freedom House publishes its annual rating, along with a discussion of changes that have taken place during the past year country by country. A corollary purpose is to show the achievement and expansion of democracy throughout the world. The underlying value that pervades these ratings on political freedom is that political democracy is the best form of government because it gives each individual the opportunity to maximize his or her personal freedom.

Freedom House distinguishes between political rights and civil liberties. The former are rights to participate in the political process, including voting and competing for public office, with elected representatives having a decisive voice in public policies; the latter are rights to free expression, to organize or demonstrate, and such rights to personal autonomy as freedom of religion, education, travel, and so forth. Political rights are very much in the spirit of the ancient philosophers' approach to freedom, which emphasized participation in the political and decision-making processes of government. Civil liberties fall much more in the tradition of John Locke and John Stuart Mill.

The survey rates each country on a transitive seven-point scale for the two sets of rights. In each scale, a rating of 1 is most free and 7 is least free. The ratings are comparative in the sense that a state rated 1 is more free than another state rated 2. However, the ratings are not additive or multiplicative in a strict numerical sense; a rating of 7, for example, does not mean that a country is seven times worse off than a country with a rating of 1.

Political rights range from a fully competitive electoral process with those elected clearly ruling, to one-party states, and all the way down to wholly des-

potic regimes. A comprehensive checklist to determine the degree of political rights includes an elected chief executive and legislature, fair election laws, fair reflection of voter preference, two or more competitive political parties, peaceful transfer of power, significant opposition vote, freedom from military or foreign control, decentralized political power, and an informal consensus on the value of democratic practices and institutions. Most democracies fall into the higher rated categories while most communist states are classified into the seventh category.

The checklist of items that determines the rating on civil liberties includes an open media independent of the government, open public discussion, freedom of assembly and political organization, practice of the rule of law under an independent judiciary, freedom from torture or unjustified imprisonment, free trade unions, businesses, professional or other private organizations, and free religious institutions. Once again, high ratings for civil liberties are generally found in democracies. Movement down from ratings 2 through 7 involves a progressive loss of civil liberties. The lowest rating of 7 represents pervading fear, little independent expression even in private, a police-state environment, and swift imprisonment and execution.

Freedom House combines the two categories of political rights and civil liberties to generate an overall "status of freedom" measure for each country as "free," "partly free," and "not free." A great deal of diversity is obviously found within these three very broad categories. The lack of precision in this summary measure makes it less useful than the two separate scales on which it rests.

In reviewing annual gains and losses of freedom, Freedom House concludes that an advance of communism has typically gone hand in hand with a diminution of political rights and civil liberties; conversely, the spread of democracy has improved political and civil rights. In recent years significant gains in political freedom have materialized in Latin America. Such countries as Argentina, Bolivia, Brazil, Dominican Republic, Ecuador, Honduras, Peru, and Uruguay have re-established democratic institutions. In portions of Africa the process has reversed. The one-man, one-vote constitutions bequeathed by the French and British to numerous African states have resulted in exactly one election followed by military, autocratic, or dictatorial regimes. Whether or not one shares Freedom House's commitment to democratic institutions, it is important to note that the annual ratings have received widespread acceptance in the scholarly community as authoritative. Most data banks on democracy contain the Freedom House annual ratings.²

In 1982 Freedom House expanded the scope of its survey to include ratings on economic freedom to augment their traditional approach to political freedoms and relate those economic ratings to political freedom. Before I review the scope and limitations of the Freedom House analysis of economic freedom, it is important to observe that Freedom House does not consider individual economic freedom to be as important as political freedom as an objective of social organization. Moreover, political freedom, in the Freedom House scheme of val-

ues, is best served through the workings of democratic majorities in legislatures. It is not a doctrine designed to secure individual rights from the tyranny of the majority.

Politics dictates economics, thus turning economic determinism on its head. A political majority, exercising its freedom to participate in political decision making, has the right to establish or modify the nature of economic choice in any society. Majorities can expand or limit economic choices as they see fit. Freedom House naturally argues that it is prudent to maintain certain economic rights to protect individuals and groups against encroachment from the state. Nonetheless, the primacy of democratic majoritarianism in the Freedom House scheme means economic rights do not enjoy any status like the equivalent of constitutional protection. Economic rights can be altered at the will of the majority.

Raymond Gastil and Lindsay Wright utilize Alfred Kuhn's interpretation of government as a co-operative organization in which all citizens are both sponsors and recipients of government activities.³ Citizens pay the costs and receive the benefits of government. In this model, political rights represent the freedom of citizens to exercise their sponsor function by selecting leaders who decide policies while civil liberties limit the power of government to interfere with citizens either by altering their sponsor or recipient roles. Although government can also be conceived as an exploitative, profit-making model, such as dictatorships or oligarchies, only democracy satisfies the intuitively required humanistic concerns of Gastil and Wright. Only democracies give all adults the opportunities to be both sponsors and recipients of state organizations; only democracies provide both political rights (the inputs to collective decision making) and civil liberties (the outputs that provide the freedoms from state control). The fact that everyone is born to the state in which he or she lives gives him or her the right to influence its decisions and limit its powers.

This co-operative notion of democracy is underpinned by a principle of political equality, which assumes a continuing struggle to give each person equal influence in the determination of public policy. With this premise, each person should have an equal right to help determine how economic and other benefits shall be attained or divided, regardless of his or her contribution to the cost of providing those benefits. To summarize, existence implies citizenship rights, which in turn implies the right to make collective decisions over the individual economic activities and well-being of others—regardless of cost.

The Freedom House principle of democracy is value laden in terms of process but is relatively value free in terms of outcomes. Liberal voters (used in the modern sense of an expanding role of government) can legislate liberal outcomes and conservative voters can legislate conservative outcomes under identical democratic procedures. Either set of outcomes satisfy the Freedom House norms of participatory equality and democratic majority rule. Although Freedom House insists that minorities must retain the right to press for their own interests,

they forcefully contend that only the majority has the right to determine the public way of life for any society. The majority can forbid obscenity by intruding in the private affairs of individuals or it can decree that public funds be spent on a broad range of welfare benefits for segments of the population.

Aristotle, among others, worried that extreme democracy was a license for mob tyranny and therefore preferred a form of constitutional government known as polity, which combined the features of democracy and aristocracy. To prevent the tyranny of the mob, Gastil and Wright argue that all democracies must grant an arena of privacy to individuals in which they may live as they feel best. Their reasons are largely pragmatic rather than resting on philosophical first principles: privacy allows the autonomy necessary for creativity, and thus helps perpetuate functioning political rights for all. But they are not prepared to present a firm statement of the boundaries of the private arena into which the state cannot intrude. Nor do they point to either written or unwritten constitutions as effective constraints on the power of government.

Gastil and Wright contend that democracy cannot be equated with capitalism or socialism. Capitalist states can be democratic or autocratic and socialist states can range from democracies to autocratic systems of communist or one-party states. They observe that the state played a large economic role in the early development of such capitalist economies as Japan, Singapore, and Korea. Moreover, Taiwan and Korea have only recently grafted democracy onto their capitalist economies.

As previously mentioned, the voters in any democratic society are empowered to determine how much latitude individuals and private organizations can enjoy in pursuing economic activity. The majority's right to decide on any aspect of economic policy or government control is, as a practical matter, constrained only by the social consensus that exists at any point in time on limits to majority rule in the realm of private activity, not by any doctrine or document that professes the inherent or inalienable rights of individuals to privacy or liberty. The rights of the majority must prevail in considering the boundaries of the right to privacy. The majority has the decisive role in defining the nature of social life: defense, transportation, education, sanitation, and the allocation of property are among the areas in which it achieves this definition. The limits to majority rule consist of the subsequent rights and power of new majorities to change any given definition. The only presumption is that new majorities remain committed to democratic processes, regardless of outcomes. Majorities are free to legislate outcomes of their choice, but are not free to change the institutions of majority rule.

Overemphasis of the rights of minorities represents an undemocratic thwarting of the will of the majority by a minority. Unless the majority can use the law to control its social environment, its rights as the majority will be unduly restrained. A minority would be making decisions that would bind the majority.

Civil liberties provide the output in democracies that protect citizens from state control. But the principle of unrestrained majoritarianism is potentially in conflict with the principle that individuals and minorities are entitled to certain inherent protections from majority rule. Gastil and Wright have abandoned John Locke, along with the principles of checks and balances and separation of powers inserted into the U.S. Constitution for the purpose of protecting individual rights from a powerful central government. Gastil and Wright's obsession with participatory equality has rendered their conception of democracy into Aristotle's category of extreme democracy, in which individuals and minorities enjoy rights solely at the capricious whim of transient majorities. The rights of individuals and property in the state of nature have no place in the Freedom House obsession with the twentieth-century emphasis on majority rule.

Economic Freedoms⁴

In discussing economic freedom, Freedom House argues that there is a basic difference between the degree to which people are free individually and collectively to undertake economic activities. Individual economic freedom means the right of people to pursue their economic activities free from arbitrary control and interference by the state and other individuals. Collective economic freedom refers to the extent to which the economic system that controls choice reflects the expressed preferences of the majority of the citizenry rather than those of a ruling few. In other words, a society that enjoys collective economic freedom is one in which a democratic political majority has the legitimate right and power to determine the structure of the economy. "An economy that is responsive to the needs and desires of the people evolves by providing those who are affected by its activities an equal opportunity to establish and change economic priorities and goals, including the fundamental structure of the economy, through open debate and full expression of their preferences."⁵ Wright's definition of collective economic freedom is really a statement of democratic processes applied to economic institutions. It is not a statement about some collective economic right that exists apart from the sum of the rights enjoyed by all the individuals in any society. This concept of collective economic freedom has no foundation in the classical liberal tradition of John Locke and Adam Smith. It represents a complete departure from the premise of methodological individualism in favour of group action.

Wright recognizes that individual economic freedoms can exist despite restrictions on or the absence of popular participation in the economic and political decision-making processes. Those in power in non-democratic societies may grant their subjects valuable opportunities for making effective economic choices (e.g., South Korea and Taiwan from 1950 to 1980) even as they deprive

their subjects a voice in collective decision making. Indeed, Koreans and Taiwanese may enjoy a greater measure of individual economic freedom than Sweden's heavily-burdened taxpayers.⁶

Wright contends that there is a complementary relationship between economic freedoms and political/civil rights. "Without the alternative centers of power produced by freedom to associate for economic purposes, to have and control property, to change residences and employment, and to express economic preferences, there is little to check the expansion of the state's authority." The relationship is one of empirical regularity, not logical necessity. She simply notes that governments that fail to respect political freedom usually fail to protect economic freedom and vice versa.

Wright arrives at her peculiar notion of economic freedom, in which democratic political majorities determine individual economic rights, by considering and rejecting the definition of economic freedom that permeates either liberal capitalist or Marxist economic theory in favour of a so-called "human rights" approach. A human rights approach to economic freedom reflects the desires of individuals and groups in the real world to achieve or maintain control over their own lives through political means.⁷ She rejects the capitalist interpretation which emphasizes maximum economic efficiency and the distribution of goods and services based on the free play of market forces underpinned by a system of rigorously defined and secured private property rights. Although capitalism fosters the rights of people to engage in economic activity free from arbitrary interference of others, Wright contends that a democratic political structure is required to protect other non-economic fundamental freedoms. The preservation and advancement of economic rights in and of themselves are not sufficient goals of human action. Wright would endorse capitalism without reservation if and only if it always stood in conjunction with democratic institutions. On this basis, the capitalist systems of Singapore, Taiwan, Hong Kong, and Korea are seriously deficient in other non-economic freedoms. In other words, economic freedom cannot be a goal of social organization in its own right apart from the existence of the non-economic rights that are part and parcel of democracy. (She equally rejects the Marxist interpretation of economic freedom on the grounds that Marxism's focus on a critique of "bourgeois" property rights over the means of production overlooks the broader spectrum of non-work related economic freedoms of association, movement, and information. Nor does Marxist theory address the possibility of the abuse of power in the actual establishment and conduct of a socialist society.)

In developing its summary measure of economic freedom, Freedom House examines four dimensions of economic activity: freedom to have and control property, freedom of association, freedom of movement, and freedom of information. Wright does not justify the choice of these four dimensions, nor explain why other dimensions of freedom are excluded. The analysis is primarily qualitative, rather than statistical.

Freedom to Have Property

It is not surprising that the freedom to have property is the first dimension in the Freedom House survey of economic freedoms. It would be difficult to take seriously any measure of economic freedom that failed to include private property, given its importance in every scheme of classical liberal philosophy. Property refers to land, labour, capital used in production, income, personal possessions, and intellectual property. “The freedom to have property and control its use is fundamental to the ability of individuals and groups to make economic choices independent of arbitrary intervention by others.”⁸ Property freedoms help preserve the sovereignty of the individual vis-a-vis the state.

In sharp contrast with Locke and other classical liberals, Wright asserts that the freedom to have property can never be absolute. Majorities exercising their political rights have both the right and power to limit individual property ownership and to transfer rights of property to the public sector in exchange for making certain benefits available to all or to provide specific social goods and services.⁹ In an economy that reflects popular political participation, there is no “correct” distribution of property ownership between the public and private sectors. “If popular majorities freely choose the rules of ownership and opportunities to change them remain available to future majorities, then societies may legitimately define limits on both state and private property within a broad range.”¹⁰ Wright seems at least as concerned with the prevention of monopolistic, concentrated control of the means of production in private hands, which she fears will emerge in the pure capitalist model, as with the protection of private rights to own and exchange property free from government interference.

Wright injects taxation into her treatment of property. Taxation represents an involuntary extraction of property to finance public goods. She recognizes that taxes reduce the amount of net income available for personal use, thus limiting private consumption choices, and that in some countries taxes have become confiscatory. However, if a more equitable distribution of income becomes a publicly approved social goal, a system of progressive taxation can serve legitimately to narrow income gaps between rich and poor or between regions. Freedom House does not wrestle with the problem of what levels of taxation are compatible with personal economic freedom. Nor does Freedom House consider possible vehicles to limit taxation.

To summarize, the principle of economic freedom requires some private control and ownership of personal and productive property to preserve the ability of individuals and minorities to pursue their own wants and desires in consumption choices, to balance the power between individuals and the state, and to symbolize personal rights to be free from illegitimate government intervention in private life. But monopolistic concentration of property in the hands of private citizens is an abuse of property freedoms.¹¹ Democratic principles are the best means, and are enhanced if restrictions on property ownership and use through

taxation or regulation serve to promote economic freedom for all. Purely pragmatic concerns over excessive state power and economic waste, not any inherent virtue in private property or the economic rights of individuals, are the limiting factors on majority rule. Unfortunately, Freedom House does not offer any firm qualitative or quantitative guidelines on acceptable levels of taxation or regulation. Economic freedom depends solely on the moderation and good will of congresses and parliaments to restrain their intrusions in the private affairs of individuals.

Freedom of Association

Freedom of association takes two general forms. One is the ability of people to associate with each other to exchange goods and services. The other is to form and join such economic organizations as trade unions, commercial and non-commercial enterprises, and co-operatives without interference from others.

As might be anticipated, trade unions play an especially important role. Wright states that the right to form unions is critical for the majority of people in advanced industrial societies who are not self-employed and whose livelihoods depend on cash or in-kind payments in exchange for labour and services. Trade unions represent the democratic equivalent of political parties or interest groups in the workplace, giving workers some power to counter the generally stronger owners of capital. At the same time, Wright acknowledges that individuals should enjoy protection against compulsory association (i.e., forced membership) to insure that they can follow their own economic interests.

Freedom House grants majorities the ultimate say in the degree of freedom of economic association that is allowed to exist. Legislatures can dissolve or ban abusive trade unions. They can also legitimately control abuses of monopoly power by both business and labour. Majorities are restrained only by the pragmatic concern to allow private organizations to exist to provide a countervailing power against excessive state authority.

How does Freedom House balance the rights of trade unions, which must contend with “free rider” and “collective goods” problems, with the rights of individuals and groups to be free from compulsory association? Does the group or the individual enjoy the primary right? The answer is that majorities must balance the matched rights of minorities and majorities.

The closed shop agreement highlights the specific issue of the rights of the individual to control the use of his own labour. Those rights take the form of an individual’s right to choose his place and type of employment, to offer his services on a mutually agreeable basis, and to withhold his labour when legitimate grievances have not been addressed. Yet these individual rights can be overridden by a legislative majority. Collectively, the right to strike allows workers to

pool common economic interests to counter the economic power of private or public employers.

The right of private sector employees to strike in democracies is widely recognized. In contrast, the right of public sector employees to strike is more controversial, especially in security and health occupations.¹² Democracies also generally accord unions the freedom to participate in political activities, including lobbying legislators, supporting candidates, and so forth.

Forced labour, slavery, and debt bondage all violate the basic freedom of individuals to control the use of their own labour. These rights are so basic that they cannot be violated by majorities.¹³ However, temporary, voluntary, indentured servitude while learning a trade or acquiring shelter and food may be compatible with the principle of personal economic freedom.

Taxation also enters into Wright's treatment of freedom of association. Some philosophers consider taxation to be a form of forced labour inasmuch as each individual is obliged to work a certain portion of each day to pay for services to others. Wright resolves this issue through simple majoritarianism. To the extent that economic policies are legitimated through popular participation, the community, acting collectively, enjoys the right to set tax levels to achieve social goals. The right to set public policy is, in the Freedom House framework, as basic and fundamental a freedom as that of the individual to enjoy the exclusive fruits of his labour. To the extent that economic policies are set by fiat of a nonrepresentative or autocratic government, which reflects the interests of party elites rather than the public interest at large, the limits imposed on the freedom of labour are unjustifiable.¹⁴ Wright does not address the threshold over which an individual's right to the fruits of his own labour may be unjustifiably thwarted by democratic majorities. Surely total confiscation of all income, even if approved by three-quarters of any representative elected body, would be a violation of any worker's economic freedom. Yet Wright can object to 100 percent tax burdens solely on pragmatic grounds, not on those of principle.

There is no basis within the Freedom House treatment of economic freedom for limiting majority rule. No role is given either to specific constitutional protection of individual economic rights or an underlying philosophical acceptance of the principles of natural rights. The only effective limits on the actions of majorities are the consciences of the legislators and the need to preserve the freedom of action of future legislatures.

Freedom of Movement

The third dimension of freedom is that of movement, which encompasses both physical and sociological mobility. Freedom of movement allows individuals to pursue alternative economic opportunities and interests without being coerced or restrained by others through such devices as internal passports, subordinated

ethnic groups, political opponents, closed-shop workplaces, violence, or systems of influx control (negative restrictions). Socio-economic mobility refers to the ability of individuals to pursue opportunity regardless of their race, religion, sex, or cultural heritage. In Wright's view, enforcing laws against discrimination and creating opportunities for disadvantaged groups promotes socio-economic mobility (positive intervention).

How do poor people fit within this definition of economic freedom? Freedom of movement is defined as a potential right for all in a free society. Those who lack the financial means to move retain the right to move when they acquire the means.¹⁵

Freedom of Information

The fourth and final dimension of economic freedom is freedom of information, which refers to a communications network that is free of government censorship. It must be accessible to individuals to gain information on prices about the actual value of goods and services (private consumption) and to express support of or opposition to economic policies and goals in any given country's decision-making process (political activity). Illustrations of pricing intervention include minimum wage laws, guaranteed prices for agricultural products, below-market compulsory procurement prices for agricultural products, and so forth.¹⁶

Wright observes that majorities often adopt a middle ground between completely free prices and completely regulated prices. What is the correct policy? To determine what the trade-offs should be, unrestricted access to the print and broadcast media becomes vital to the democratic process by which economic policies and arrangements are legitimated. Media freedoms become the basis for communicating opposing views on pricing and other issues of economic policy.

Economic Freedom Versus Economic Security

Wright accepts the notion of "freedom to" embedded in the positive view of liberty—the view that government can take positive steps to enhance the living standards of its subjects. Economic security is as legitimate a goal in society as economic freedom. Put another way, economic outcomes that conform to majoritarian values are as legitimate as maintaining freedom of individual opportunity. Since no freedom is absolute in any society, Wright accords democracies the right to make frequent compromises and trade-offs between short- and long-term goals, and between the aspirations of different groups.

Rising prosperity has enabled modern industrial democracies to afford, if they wish, the wherewithal to secure a minimum standard of living for all its citizens through appropriate tax and spending policies. Positive freedom for some

means less negative freedom for others. All free societies confront the effects of this trade-off between economic freedom and economic security. The Scandinavian states exemplify the willingness of citizens to relinquish personal control over property for collective protection against the risks of economic uncertainty.

Measuring Economic Freedom

Freedom House employs a generalized scale ranging from high to medium to low to rank each of the four economic freedoms, which are then averaged to obtain a single rating of overall economic freedom.

Freedom of property is evaluated by the degree to which individuals and groups control property independent of government restrictions. The rating examines the size of the public sector and the degree of state intervention, which displaces or substitutes private enterprises with government-operated or controlled firms.¹⁷ But positive ratings are also awarded government efforts to redistribute land or improve opportunities for more equitable land use and control where land ownership is unduly concentrated among a small number of private individuals. This is in sharp contrast with Locke's right to accumulate land and wealth.

Although the examination of property freedoms is largely focused on government interference, other groups in societies (e.g., small groups of dominant landowners) may play an equally effective role in obstructing freedom. And in countries such as India and Bangladesh where a combination of social, cultural, and historical factors have created highly fragmented or marginal land holdings as well as inadequate production incentives and barriers to co-operative farming which prevent large portions of the population from exercising economic freedom, government sponsored progressive reform may be necessary to increase economic freedom. Land reform in Taiwan and Japan would constitute exemplary illustrations of government sponsored progressive reforms that increased economic freedom, even though landowners were involuntary participants (in violation of classical liberal norms of liberty).

Freedom of association is measured by the extent to which the predominant methods used to distribute goods and services are left to the market or controlled by the state. It also reflects whether economic associations are formed through voluntary or compulsory membership. The measure also takes into account the ability of unions to bargain collectively, strike, and engage in political activities. A high rating reflects a relative absence of intervention by the government or other groups in the formation and activities of economic associations and a predominantly private system of distribution for goods and services.¹⁸

Freedom of movement focuses on citizens' physical and socio-economic mobility by examining restrictions on internal movement, constraints on emigra-

tion, and limits on class mobility through enforced discriminatory laws, social and cultural traditions, or highly regressive tax and expenditure policies.

Freedom of information examines patterns of control of the print and broadcast media and whether they restrict access to specific groups or views to the exclusion of others. It also assesses restrictions on or suppression of the presentation of news and opinion through government censorship, harassment, and intimidation of journalists, or outright closures of independent newspapers and broadcast stations. A high rating indicates the existence of predominantly privately-controlled media. A medium rating indicates the presence of state-operated media that occasionally control the reporting and editorials over other independent media. A low rating reflects strict government control and censorship over opposition groups and the total absence of questioning of economic policy in official media.

The ratings are arrayed in a lengthy table that also ranks the economic system in accord with the degree of capitalism or socialism that is practised, political legitimacy, the quality of life, and per capita income. Most countries receive high or medium ratings on overall economic freedom. Many autocracies of the right and left allow a degree of economic freedom, usually in the exercise of some types of property and mobility freedoms. Only the centrally-planned communist countries have succeeded in controlling most economic activity. In general, capitalist democracies score higher on economic freedom than capitalist autocracies, largely because the latter restrict freedom of association and information.

Wright concludes her comparative survey of economic freedoms by insisting that the best hope for advancing economic freedom lies in strengthening the rights of all people to choose their own government, and through the resulting democratic practices and institutions to determine their own economic arrangements.

I want to note that, as a practical matter, the Freedom House ratings are much better than the conceptual scheme which underpins them. The primary reason is that Freedom House resorted to a number of standard indicators of freedom of property, association, mobility, and information that intuitively reflect greater or lesser degrees of economic freedom. It becomes a very difficult data collection and evaluation exercise to determine, in the case of every number or classification, if that particular indicator reflects majority preference. Of course, majority preference is irrelevant in autocracies, dictatorships, or communist societies; it is germane only in democracies. It is therefore more straightforward to rate economic freedom in non-democratic countries. The injection of majority preference as a consideration in rating economic freedom would pose severe problems of comparability across countries that have different political structures and over time where countries changed forms of government. In the next section, I set forth my views

on those dimensions of economic activity that should be incorporated into a rating scale for measuring economic freedom.

Notes

1. This chapter summarizes Raymond D. Gastil and Lindsay M. Wright's "The State of the World: Political and Economic Freedom," in *Symposium on Economic, Political and Civil Freedom*, ed. Michael Walker (Vancouver: The Fraser Institute, 1988).
2. The Hoover Institution has been developing a data bank during the past two years as part of a large-scale democracy project. The full set of Freedom House ratings are an integral part of that data bank. The data bank does not have a comparable set of ratings on global economic freedom.
3. Alfred Kuhn, *The Logic of Social Systems* (San Francisco: Jossey-Bass, 1975), pp. 330-61.
4. Lindsay M. Wright, "A Comparative Survey of Economic Freedoms," in *Freedom in the World: Political Rights and Civil Liberties 1982*, ed. Raymond D. Gastil (Westport and London: Greenwood Press, 1982), pp. 51-90.
5. *Ibid.*, p. 52.
6. Wright argues, as indicated later in this section, that the Swedish condition is preferred to that of Taiwan or Korea.
7. The Freedom House approach to economic alternatives is the complete antithesis to Murray Rothbard's individualistic, stateless theory of liberty.
8. Wright, "A Comparative Survey," p. 55.
9. There is no provision in the Freedom House scheme for the government to compensate an individual whose property is involuntarily transferred to public use.
10. Wright, "A Comparative Survey," p. 56. On this basis, democracies enjoy the legitimate right to abolish private property.
11. So long as free entry into every line of production is permitted, concentration of ownership does not destroy opportunity. Wright does not address this issue.
12. President Ronald Reagan did not think that the air traffic controllers' union had the right to strike in 1981.
13. This is Freedom House's first clear statement on the inherent rights of individuals to be free from government intervention, or to be protected by government from the coercion of others.
14. Here, Wright implies that lower levels of taxation and regulation imposed on labour in autocratic societies are less legitimate than higher levels imposed in democracies. Thus, the level of taxation or regulation plays a smaller role in determining the degree of economic freedom that exists than the structure of government. In short, economic freedom depends on the legitimacy or illegitimacy of government decisions. In this view, Hong Kong's low tax rate of 15.5 percent represents a more serious violation of economic freedom than does Sweden's imposition of tax rates exceeding 50 percent in that the former is imposed by bureaucratic fiat and the latter by legislative deliberation.
15. In the Freedom House scheme, majorities could use public funds to finance physical mobility. The reality, in many democracies, is that government programmes that deal with unemployment generally provide incentives to keep people in depressed areas rather than reward them for moving to areas of greater opportunity.

16. The actual measure on freedom of information omits direct or indirect government pricing intervention so that consumers may have access to distorted prices rather than prices determined by market forces.
17. Intuitively, a larger public sector implies less freedom for private property. Recall that Freedom House gives majorities the legitimate right to choose a larger public sector without violating individual economic freedom. It is not clear from the text whether the rating attempts to discern if the size of the public sector reflects majority preference. Otherwise, Freedom House should assign a high rating to freedom of property where property ownership is highly restricted by majority rule.
18. The same omission in the text applies to freedom of association as to freedom of property in the case of democratic majorities that restrict association.

Discussion (Chapter 3)

Alvin Rabushka Let me begin by asking why is there a special section on economic freedom? I examined the economic literature on attempts to use socio-economic indicators to measure economic freedom, and to my knowledge the Freedom House study is the only serious attempt.

It is an inevitable consequence of having started the Comparative Survey of Political and Civil Freedoms in 1972 that ten years later they would recognize an economic dimension. That is very encouraging. One can take great heart from the fact that an organization whose overriding value is democratic process (regardless of outcome) also addressed the subject of economic freedom. Several people this morning pointed out that it would be a mistake to separate economic freedom from the general issue of freedom. My rejoinder was that there is nothing to keep from putting it back into the fold when you know what you are talking about. I would like to know more about economic freedom and then blend it into a broader definition of liberty and freedom that encompasses political, civil, and economic dimensions.

The overriding fact in the Freedom House view is the primacy of democratic majoritarianism. In their view, the ultimate value that any human being has is the ancient Greek notion of the right to participate in collective decision making. Through the universality of one man, one vote, the will of the majority dominates in the collective decision making of the state and society, and does so with respect to the fundamental economic institutions and arrangements.

I searched long and hard and never found in Lindsay Wright's paper the phrase constitutional limitation. I never found any words about fundamental and inviolable rights of individuals or about their rights to life, liberty, and the pursuit of happiness. From that paper, one would not know that there had been an intellectual tradition in the field of natural rights or natural law, nor would one know that there had been an intellectual tradition in non-intervention and the avoidance of coercion in economic matters. In fact, that paper went so far as to state that one has to be careful to make sure that there is no undemocratic thwarting of the will of the majority.

What, then, provides any basis for presupposing that there ought to be certain kinds of economic freedoms? The answer, under the Freedom House doctrine, is twofold. One is that creativity dictates a certain amount of pragmatism and privacy; for the state to run, own, and do everything is to thwart privacy, creation, and entrepreneurship. The second is that the rights of individuals depend upon the prevailing social consensus at the time, because future democracies must not be bound by current democratic decisions.

This view is process oriented, not outcome oriented. Under this view, a liberal community will generate liberal outcomes and a conservative community

will generate conservative outcomes. By this criterion, there is no way to distinguish which action is preferred to the other except to say that a majority prefers one to the other. There is a whole literature in political science that is not addressed but that bears on this view—the intense minority problem in which 49 percent of the population feel intensely and 51 percent are indifferent. Why should the indifferent majority rule over the intense minority? There is also the paradox of voting. There are rules for making decisions under which one will not reach a majority outcome even though there are procedures designed to obtain it.

As we listened last year to Lindsay Wright talk a little bit about this, the point that concerned Walter and me the most had to do with the question of labour. We thought it somewhat paradoxical that the freedom of people to associate with each other and to form labour unions and organizations was a fundamental economic freedom. Many of us in this room would say that the chief consequence of that is to exclude others from the right to make employment choices. This is a practical consequence of the violation of economic freedom. So that particular measure of freedom of association really seems to be a denial of individual freedom. Thus, a measure that would be used for one thing, in fact, would have the opposite intent.

What I think is interesting, and what comes out in Spindler and Still's paper, is that property is the first freedom mentioned even though it doesn't have the greatest weight. I agree with the definition of freedom of association, which is defined partly as consenting adults making voluntary transactions of all kinds. The movement and information measurements are also valuable and interesting in their own rights. However, their approach completely lacks concern for the fundamental economic rights of individuals. That omission, plus the fact that their's is the only extant attempt to analyse economic freedom in a qualitative evaluation, makes it a topic worth discussing.

James Ahiakpor I am going to react to David and Milton. If you remember we were talking about natural rights and the function of government. What I wanted to say was that natural rights were not an end, but rather a starting point. After we have gone through recognizing natural rights, we can then distinguish privileges that may be conferred by the state. My reply to David was going to be that we can distinguish certain agencies of the state, like Congress or Parliament or the judiciary, from government when government consists of people elected to perform executive actions. In the case of Canada, we have had different parties in power, and no one believes that Parliament is government. But when we talk about government we mean those who exercise executive functions of the state. This is why I thought unless we meant the whole apparatus of the state being given the task of defining rights, claiming that the government has a legitimate role in defining our rights is to give away the store because they can so define rights as to impair them.

Michael Walker Regarding Lindsay Wright's effort, a comment was made about her tendency to invest too much in the desirability of majoritarian decision making. But I think we are in danger of investing too much in the other direction. I wanted to conduct a little poll at the end of the last session, which I will conduct now if people are willing. Assuming that there would be appropriate decision-making tools and things of that kind, how many of us here can conceive of a free society in which the average tax rate is 75 percent?

Henry Manne As a result of tax rate changes? Did we move in and out of the status of free society?

Michael Walker No, an average tax, not a marginal...that is, 75 percent of the income of the society is spent through the public sector.

Voice An extremely rich society, conceivably, could handle that. It wouldn't get rich that way, of course.

Michael Walker Can I ask for a show of hands...

Rose Friedman I think you are going to have to give your other conditions.

Michael Walker A free society in which...well, let me make it even tighter...in which there is a unanimity principle for the determination of the electoral outcomes.

Voice And they decide to allocate 75 percent to the public sector?

Voice And sell themselves into slavery?

Milton Friedman They are very homogeneous and they all want exactly the same things?

David Friedman Is it a town within a society where taxes are deductible from federal taxes and therefore high town expenditure is a device for evading federal taxes?

Michael Walker That possibility was raised at our lunch discussions, as a matter of fact, but why I'm raising the point is to find out exactly where we might end up in terms of a bench-mark. How much contracting do we permit people to do to surrender their rights under different circumstances?

Milton Friedman You admitted that if you let us have the unanimity principle anything is possible.

David Friedman I find it hard to say whether something that uses the unanimity principle is a government. It is no longer initiating coercion against anybody, since everybody is consenting to everything it does.

Michael Walker No...wait a second...unanimity may not be on every outcome. I am referring to unanimity where, for example, people agree to appoint five individuals who will then decide how everything is going to be done.

David Friedman But if you unanimously agree, that could be done by private contract. It doesn't look like a government to me.

Michael Walker Well, then are we saying that it raises a very interesting question? But if one person dissents, what then do we make our bench-mark? Where do we draw the line? Do we say at 90 percent? 100 percent?

Milton Friedman Drawing the line is a practical matter, not an issue of principle. We agree that we don't have enough energy and effort to decide everything unanimously. We don't have enough time. And so we say some things are not terribly important and it will save a lot of time if we decide them through a vote. How large a percentage is purely a question of expediency. There is no question of principle involved.

Zane Spindler But that's where we get caught. Because that's where the small amount from everyone of us is taken to give a special benefit to the rent-seekers (special interests). But you don't have a limited constitutional right in a majoritarian democracy. However, with unanimity rule you don't need explicit limits because certain things would not be considered, and they should not be considered.

Milton Friedman Unanimity is an ideal. I agree with Mike, we want to measure things against an ideal. However, if you are now going to talk about whether we need 99 or 98 or 97 percent then you are reverting from the ideal to the expediential.

Zane Spindler But you see it needn't be an ideal if you admit that those things that don't get unanimous approval are not appropriate for public action. Then it is a practical mechanism that automatically limits the public sector.

Milton Friedman Suppose you unanimously agree that some matters on which we cannot get unanimity on details should be decided by public action? We might unanimously agree that it would be sensible to have public streets...to have the city government provide public streets even though we would not agree

on where the streets should go, how many there should be, how big they should be, etc.

Robert Poole I wanted to make a few comments about the attention we are giving to Lindsay Wright's exercise here. The fact that Alvin has identified it as the only one in existence and also that Freedom House has a fairly good reputation may be causing us to pay too much attention to it as a serious effort. What would you expect a social democratic political scientist to come up with but something as garbled and confused as this? No economist has even attempted to define such a measure, so it shouldn't have that much inherent validity to begin with. I just want to caution us not to get too caught up in the ins and outs of its details.

The fact is, it is accepted because Freedom House put it out and nobody else has tried anything. It seems to me that if respected economists put something out as a measure of economic freedom, it would have an excellent chance of gaining credibility, despite the fact that the Freedom House measure is there by default.

Henry Manne I think Bob made the correct observation and the wrong strategic conclusion from it. I would pay a lot of attention to the Freedom House study. I would bring serious people to bear on this as though we really do take seriously what they said. We should point out to them some of the mistakes in it, some of the inconsistencies between the different notions, and force them to consider those things to the point that they are very likely never again going to include economic freedom as one of the categories they study.

Robert Poole You are quite right. I didn't mean to not take it seriously in that tactical sense. I just meant that we shouldn't spend our time trying to dissect the details of it as opposed to constructing something from scratch that is economically valid.

Henry Manne Well, I spoke on the supposition that the motivation behind a lot of the present discussion relates to trying to popularize the concept of economic freedom. I think maybe it can be done more effectively through an indirect manipulation of Freedom House than the Fraser Institute trying to establish its own index and getting it published.

Gerard Radnitzky A remark on unanimity: Can it function as a regulative principle? When would a rational agent, if given a chance, opt for a social contract? He will sign the contract only if he has come to the conclusion that, although his submission to coercion by the state is costly, that cost is outweighed by expected benefits. What sorts of benefits could induce him to sign? According to Hobbes, people are so afraid of un-coerced chaos that they see the state as

offering maximum protection—external and internal—at a cost, at any cost, “mutual coercion mutually agreed on” and “government of the people by the people.” Later on, came the paternalistic and, in modern times, the welfare state argument for the state. In the latter case, the costs may be enormous, e.g., taxation may become confiscatory.

Sweden is an excellent example of the egalitarian transfer state. According to Swedish social democracy all income is potential tax and all consumption is subsidy. The best-known example of a 100 percent tax was the aggregation of the income tax and the gift tax on certain pensions, allowing the total levy to run up to 132 percent, and that system prevailed in Sweden between 1958 and 1980. (Incidentally, Ingmar Bergman was already upset by a tax of “only” 109 percent.) The purists among the ‘social cleptocrats’ attempted to classify part-time work as tax evasion. Thus, signing a social contract may be very costly.

There is only one borderline case in which there are no costs: if the individual has veto power—if unanimity is really required to extract tax, as Wickseil recommended. But making the assumption that the veto power will work in practice is tantamount to assuming that the state, which has the power of coercion, lets itself be controlled by those who have none. Anthony de Jasay illustrates this in his book *The State*. So we are back to the question of whether or not the costs of living in a certain state are outweighed by the benefits derived from living under its rule. Costs and benefits are evaluated subjectively. A skilled and hard-working person may prefer Hong Kong to Sweden, while a rational criminal is well-advised to emigrate to Sweden. There was a veritable exodus of valuable human capital from Sweden in the late 1960s and early 1970s. Apparently the government did not mind. This is probably the only sector in which no official Swedish statistics exist. Swedes still possess the freedom of exit option—although they may not be allowed to take their financial assets with them (as in the case of one of the Wallenbergs).

The case of Sweden shows how right Walter Block is when he recommends we put economic freedoms and civil liberties on one side, and regards the expression “political freedom” as a misnomer. Because most often “political freedom” means nothing more than a parliamentary election every four years, as in Sweden—a perfect democracy with few option rights left to the individual.

Michael Walker I am going back to this notion of unanimity. Where does it lead us in terms of our bench-mark? If we agree that we have unanimity, that poses no problem. That is simply a form of contracting where we have agreed to give up our rights, presumably because we think it’s a good deal. In formulating any bench-mark about where the tax burden bites in some coercive sense, we have to perform a conceptual experiment: we go back and say, well now, which of the issues that are currently decided in a collective fashion could we get unanimous consent for? That, of course, would probably vary, based on the cultural or institutional environment. I think in Sweden we could get unanimity

on a much broader range of issues than we could in a polyglot country like the United States. But you have to perform that experiment in order to get a conceptual bench-mark against which to measure other things.

I also wanted to react on the point about unions. This comment will come as no surprise to Walter or Alvin because I raised it with them before. Again, we have to be careful that we don't take a unilateral attitude towards the question of whether unions improve freedom or not. We, for example, have to have a different attitude towards the Solidarity union in Poland than the Teamsters. And we have to have a different attitude based on whether it is a union that is voluntaristic or one given powers of coercion by law. So it is labour codes, rather than labour unions, that mark a loss of freedom.

In the case of Solidarity, I certainly believe that unions were freedom-enhancing rather than freedom-reducing.

David Friedman I have a question for Alvin. I haven't read the Freedom House material he is commenting on, and find it hard to tell from his remarks whether the majoritarian views of the people who were doing the study affected their definition of economic freedom or merely their opinion of its value. It was not clear from his comments whether they said, "private property rights are part of economic freedom but not always desirable, since the majority should have the right to take those property rights away. Doing so diminishes economic freedom but is still a good thing," or whether they said, "a constitution that prevents the majority from seizing property is both undesirable and a restriction on economic freedom, since it eliminates the economic freedom of the majority to seize property." My question is, which are they doing? Are they including their political views in their definition of economic freedom or their evaluation of it?

Alvin Rabushka The answer to the latter point is yes. In this view, anything that thwarts the will of the majority would be a violation of the rights of the majority to establish conditions for economic activity.

David Friedman Would it also be a reduction in economic freedom as they measured it?

Alvin Rabushka No. When they actually talk about the kinds of qualifications of each of these four dimensions, and how one might rate it high, not so high, or low, they forgot to factor democracy into it. Consider the following comparison. What you have in a country like Sweden may be a majority vote for high taxation. What you have in a country like Hong Kong is one man, the financial secretary, imposing a regime of low taxation. According to the Lindsay Wright/Raymond Gastil notion of economic freedom, Sweden has more economic freedom than Hong Kong, which is surely absurd. When they actually

get into the measures, they don't take into account whether or not any of the numbers or data reflect democratic consensus.

David Friedman Are you sure you aren't confusing their definition of economic freedom with their definition of good? Isn't it possible that they agree with you about what economic freedom is and regard economic freedom sometimes as a good thing and sometimes a bad thing? It is a bad thing when it is a result of limiting the rights of the majority and it is a good thing when it isn't. And we can measure it either way. Is that a possible interpretation of what they are saying?

Alvin Rabushka I don't think that's an unfair statement. What they are saying is that no one could write a constitutional bill of economic rights in their system because it would infringe on the rights of the majority.

David Friedman If you wrote it they would say it was the right bill. They would say that society has high economic freedom and low political freedom because it is not democratic.

Alvin Rabushka No...because they really do mingle the two notions. They say that you cannot separate purely economic from purely political activities because an integral notion of what it means to be political is to make decisions about economic arrangements and institutions.

David Friedman But you can still separate it. You would then say that a society with a constitution that forbade the restriction of economic freedom would be a society with high economic freedom and low political freedom, because their definition of political freedom includes the right of the majority to do things. I do not know what they do say, but it would be perfectly coherent for them to say that sometimes there are conflicts between economic freedom and political freedom, that economic freedom is a particular kind of freedom that some people value, and that it is an empirical question whether in a particular case economic freedom is a good thing because the majority wants it, or a bad thing because it interferes with the ability of the majority to do what it wants. It sounds from your description of their empirical work as though that is what they may be doing.

Alvin Rabushka What they are doing is looking at ways that make any given society function better, and they recognize that you will get an economic system that performs better when you have certain kinds of arrangements. But they are not willing to sanctify or canonize them, and they rank them lower in the hierarchy of rights. At the top of the list is one man, one vote, regardless of any taxation you pay. They are as much concerned with private agglomerations of power as we might be with public agglomerations of power. This will of the

majority is partly designed to neutralize private concentrations of power. For example, they are very hostile to Indian landlords who acquire excessive concentrations of land at the expense of Indian peasants. They are very worried about monopolistic industries that would, for example, give private holdings enormous amounts of power. You and I might say it was all right if it was done through a Lockean framework. They would say no. They have concerns about private concentrations of power and the antidote to that is majoritarian decision making.

Much of what you are saying is right but it's a little more complicated than that. They find it very hard to keep economic freedom on its own terms and merits apart from the democratic institutions that make the choices of how economic rights work.

David Friedman What their hierarchy is doesn't matter if they report the different things separately. If you give separate reports for A, B, and C, the fact that you think A is most important does not prevent me from using your data on B or C.

Alvin Rabushka How they define it is in part conditioned by this democratic process. It is all mixed in together, so they are going to come up with a different way of thinking about these things because they are always thinking about whether or not these things represent majoritarian outcomes.

Michael Walker Lindsay Wright quite clearly states that it is the business of a majority to decide what the correct distribution of income is. If that happens to imply a tax rate of 95 percent, having made the decision that there should only be a gap between the top and the bottom of 4 percent, then taxation is simply the way to achieve the result that the majority desires. The achievement of that result...the objective rather...is the expression of freedom. The freedom of the majority to select that outcome.

Voice Isn't she basically saying that a democratic arrangement of that sort will indeed achieve some grander end result?

Michael Walker No. That's the value. The value is the ability to make that choice.

Alvin Rabushka The process is not the same as the outcome. Her view is process oriented. And the outcomes are accidental, whether they are desired or not.

Michael Walker Listen to this quote that Alvin included...it's a beautiful quote: "If popular majorities freely choose the rules of ownership and

opportunities to change them remain available to future majorities, then societies may legitimately define limits on both state and private property within a broad range.”

Alvin Rabushka And there is no limit implied or expressed as to what those are.

Michael Walker But it certainly leads us back to the question I am trying to inject into the discussion: Is there some amount of tax that is legitimate? We have agreed that if we perform a conceptual experiment in which we imagine that 25 percent of the outcomes can be altered by a tax regime that would receive unanimous agreement, then that is our bench-mark. Maybe she is saying that as long as it is determined by a majority, as opposed to the unanimity principle, then any outcome is justified.

Alvin Rabushka With regard to a point Milton raised, I observed in Hong Kong that what is being attempted there is to limit the powers of popularly elected government to interfere in certain kinds of activities in ways that would ensure individual economic freedom, and at the same time they are trying to find a collective set of policies that would be directed toward that end. So to state, for example, that the government shall follow a low-tax policy, that there shall be no restrictions on free trade, that there shall be free movement of capital and convertibility of currency, is to state that when the majority sits down to make decisions that affect us economically, it hasn't got the right to make certain kinds of decisions that remove those rights from us. Or, as John Locke would say, we don't surrender the freedoms that we have in the state of nature when we transfer them to the collective. They are still ours. We have simply made some expediency notions in terms of punishment, but we haven't surrendered our rights. Therefore, to the extent the government violates them, it lacks legitimacy; and you have to fight a revolution in Locke's view to put a stop to that.

There is a fundamental difference here from the way I would want to think about individual economic freedom. There are no limits within this particular political process value framework, whereas I would like to think there are inalienable or inherent or desirable limits—and that's what we mean by individual economic freedom—that represent the borders over which the state cannot act.

To make one last minor point. It is one thing to have a constitutional limitation on, say, high taxes, but it is quite another to get involved in how you are going to spend the small amount of taxes you collect. I would be less concerned about the latter than I would be about the former.

Milton Friedman As a sort of a side comment, I can answer Mike's question about what the appropriate level of taxation is if the public were to unanimously

agree to it. On a historical basis, it is 10 percent. The church tithe and the rate of taxation in Britain at the time of Queen Victoria's jubilee was 10 percent. In the United States, for more than a hundred years before 1929, except during war time, it was 10 percent. So empiricism tells me 10 percent is right.

Richard McKenzie But none of that was unanimous.

Milton Friedman No, I am just saying what in his hypothetical conceptual experiment would be the number he consents to. But seriously, wealth maximization is not the same thing as maximization of well-being. We know what wealth maximization is. I do not believe that it makes any sense in any way to treat wealth maximization as equivalent to economic freedom. For two reasons.

The first is that I believe in the example Alvin gave of a Brunei, that is, there are many of us and many individuals throughout the world who would prefer a lower level of wealth maximization with more freedoms to a higher level of wealth maximization with no freedom. I am not saying that there is no difference large enough to compensate them, but there is a price they would be willing to pay for freedom. And so you can't confuse the two if one of them is something you are paying for with the other.

Secondly, it begs all the interesting scientific questions to assume that Henry or Dick knows how to maximize wealth. We don't. We don't know what set of rules, what set of processes maximize wealth. We cannot demonstrate that something we call economic freedom produces a maximum of wealth. That's a proposition to be investigated. You mustn't confuse the cause with the effect.

Finally, I want to go back to Mike's comment about Solidarity. In the collectivist society of Poland, Solidarity is freedom-enhancing—by producing disturbance. But if Solidarity had power it would be a collectivist state too. If you look at the principles of Solidarity, it believes in socialism. It doesn't believe in freedom. So looked at in a broader way, I don't think Solidarity is a good example. I agree with his main point. If trade unionism is voluntary, if people want to get together and form an organization, voluntary association is an important economic freedom and that has to be distinguished from coercive trade unions which have the power of the state behind them. But I don't think Solidarity is a good example.

James Gwartney I would like to make a point and then ask a question. It seems to me that Lindsay Wright has mixed together the political and the economic. She sees a spectrum running from freedom, representing majority rule, to coercion, representing dictatorship. In contrast, we see the spectrum running from freedom as associated with individual choice to coercion as associated with collective choice and interfering with individual choice. This is very different.

The question I have relates to whether or not this same criteria would be applied in other areas that we might think of as non-economic. For example, has one's right to freedom of speech been interfered with if the majority decide that you shouldn't be able to give speeches on public corners or to rent an auditorium in order to give a speech? Or has your right to assembly been interfered with if the majority decide that it is not a good thing for more than three people to get together at a given site? It seems to me that if she is going to be consistent, then she would have to say that if the majority decides such things then they are not a violation of freedom because they reflect the will of the majority. If, in fact, you take this approach, then you essentially completely negate the idea of freedom.

Milton Friedman I am going to take Lindsay Wright's part. She isn't here, so somebody has to take her part.

She wouldn't agree with your statement at all. She would say the idea of the majority preventing freedom of speech would be consistent with her concept of freedom. Because she would say an essential element of her definition is that you can have more than one choice. Since there is not a one-time majority, it would always be possible for a majority to reverse what a former majority has done, and she would say that you could not achieve that unless you retain freedom of speech and freedom of assembly. And therefore those are the means to the more fundamental objective, in her view, of having a society ruled by the majority but permitting turnover.

Henry Manne May I interrupt with a humorous quote which supports what Milton just said. It is on page 99 [of *Freedom, Democracy and Economic Welfare*—ed.]. Lindsay Wright says, "Theoretically, then, a majority might have the right to decide on any policy or any degree of government control that it wished. In fact all democracies emerged from traditional societies that understood certain rights to be the natural property of all citizens and so insulated from majority rule." Then she comes down from that height with, "For example, the assumption in our tradition that everyone has a right to a fair trial limits absolute parliamentary or plebiscitary sovereignty." She doesn't know what she is talking about.

James Ahiakpor This is part question and part comment. Although I share Alvin's criticisms, I also wonder whether these might not be due to Wright's failure to specify certain conditions. For example, we keep coming back to the taxation argument. Alvin writes that she does not address the threshold beyond which taxation becomes confiscation. She might well have in mind the empirical fact that people voluntarily do not like to legislate higher taxes, which is why democracies are plagued with deficits. In the U.S. more people want government spending but when they hear someone pledging to increase taxes they frown on them. Thus, some of the criticisms may well be acceptable to her when they

appear to be enhancing what she perceives to be greater freedom or well-being of people. And as Alvin correctly points out, she seems to be most concerned with dictatorships as being against people having the ability to make laws to promote the collective well-being. At the basis of such collective well-being, Wright may have at the back of her mind the welfare of the individual as well. So the strong criticism may be simply because she hasn't mentioned some of these things. Or is she really against individual welfare?

Henry Manne There is the instrumental matter of interest. Can this be utilized as a way to have Freedom House consider a sounder economic approach, to understand that there are serious economic issues other than going into court to sue for an invasion of privacy? These things are magnitudes, orders of significance, for large numbers of people. Even given the collectivist bias that clearly is behind their preference for political ordering as opposed to individual and market ordering of things, these are people who can be talked to.

Milton Friedman Zane Spindler says in his paper that there is a very high correlation between her final rankings of economic freedoms and his. Isn't that right?

Zane Spindler A couple of brief comments. The notion of process that was involved in Lindsay Wright's paper also is involved in wealth maximization or other notions of freedom. That is, what comes out of the market process (or a political process that is unanimous) is in a sense wealth maximization (or freedom).

I think the thing to concentrate on in Lindsay Wright's ratings is the extent to which they can be used to meet the distinction that David Friedman set up before with respect to the value of freedom versus specific freedoms. We could look at what she has done to see the extent to which the things that she has measured are in some sense measures of freedom, or in another sense that they capture the value of freedom. What we were discussing earlier was sometimes at cross purposes because there were two different underlying philosophical concepts there: one was consequentialism and the other was essentialism. We have to recognize that we can meet both. We can develop a measure that a consequentialist would like, which is the value of freedom, and measures that essentialists would like, which are the individual freedoms.

Richard McKenzie I would be the first to admit that wealth maximization is not the end all and be all. But I guess I am somewhat confused because I thought one of the purposes of coming up with a measure would be to specify something that can be empirically handled. We are not just aiming at a barometer that we will hang on the wall. We want a measure that is quantifiable and useful. That

means we have to link it to other things that are useful. Well-being is something that's not useful, because it is unmeasurable.

Michael Walker Just quickly on the last point. I think we want to correlate the measure of freedom with measures of wealth. But we don't want to presume that something that enhances freedom automatically enhances wealth. Because it may not. We may find all kinds of instances where people would agree to forego a wealth-enhancing phenomenon.

Back to the question of Solidarity. We have to remind ourselves what our starting point is in our analysis. If we are rating unions in North America with all the institutional arrangements that lie behind them and all of the laws that give them powers and so on, that is one thing. If we are evaluating Solidarity in the context of Poland, where they are providing the only opportunity for assembly and the only locus for expression of viewpoints that are contrary to the totalitarian mechanism, then it doesn't matter what they espouse. The point is that they may be the only point of freedom within the context of that polity. So I have to stick with my point that without considering the bench-mark against which we are comparing, we can't decide whether a union is freedom-enhancing or freedom-reducing.

Charles Murray I just want to put an asterisk beside something that is useful which has come out of this discussion involving majoritarian rule. It goes back to the question of dimensions, and it is illustrated perfectly by New Zealand right now.

If you want to measure economic freedom in New Zealand, it must, in one dimension, reflect the very large degree of freedom that they just recently installed with a variety of legislative changes. That freedom is a reality. It is also a reality that New Zealand can instantaneously go all the way back because of the way the unicameral legislature works. After the next election, everything may be changed, and that instability must also be reflected in locating New Zealand on that open dimensional space.

Alvin Rabushka I wanted to wrap up this session by observing that the positive-freedom, negative-freedom, freedom-from, freedom-to distinctions are what pervade this whole business. Wright is very clear that you have the right to use the state to attain desirable objectives, whereas the classical liberal notion for most of us means freedom from state intervention. The other point I want to make, and I appreciate what Mike is trying to do, is that up until now I haven't thought in terms of bench-marks by which we will ultimately rate or measure economic freedom. We will incorporate within democratic decision-making rules, e.g., certain majority rules like simple majority, two-thirds, three-quarters, or even unanimity. I have tended to think in terms of the opening statement of the Declaration of Independence, which talks about inalienable rights to life,

liberty—I think the first draft mentioned the pursuit of property but it ended up being pencilled out and being called happiness. John Locke was clear on the right to property. When we think in terms of these classical notions of economic freedom, we are thinking about the social orderings of society in which individuals have certain rights to these activities, to these freedoms. To be free from state intervention.

If you had a government in which 80 percent voted to interfere with property rights and the other 20 percent were offended, it is still a violation of basic economic freedom for the 20 percent. Short of unanimity, it is a violation of somebody's basic freedom. I want to think in terms of what we would regard the ideal state of economic freedom to be, and then to be able on a score of zero to a hundred, to assign a 17 to China today and say it was 15 last year and 13 the year before, and say that a 17 in China means what 17 may mean in Vietnam. I am not prepared to completely lose sight of the fact that some set of political freedoms and civil liberties are critical and important. But I don't want to burden the task of trying to come up with some way of creating a multi-dimensional notion of economic freedom and ultimately move to specify and rate it. I don't want to confuse the issue by also considering at the same time matters of political freedom and democratic decision making.

Chapter 4

Preliminary Definition of Economic Freedom

Alvin Rabushka

The attempt to develop a rigorous, quantitative measure of economic freedom may strike some as a presumptuous undertaking. The effort requires agreement on the conceptual dimensions of economic freedom, the indicators or data that fit or reflect each of the several dimensions of economic freedom, and the generation of a number (or numbers) that sums up all of the different dimensions, thereby permitting comparative ratings on the degree of economic freedom that exists both in the aggregate and for each of the different dimensions of economic life in every country in the world at any point in time. This chapter constitutes an initial effort of defining economic freedom and some possible measures. It lays a foundation for subsequent symposia that will focus exclusively on refining the conceptual elements of economic freedom, identifying data requirements, and developing quantitative measures. The ultimate objective is an annual report or yearbook that rates economic freedom in every country around the globe, thereby replacing and upgrading the Freedom House rating.

The brief review of various philosophical treatments of economic freedom in chapter 2 was intended to develop a working consensus on those aspects of economic freedom that are quintessential in any rating scheme. Locke, Smith, Friedman, and Rothbard all subscribe to the institutions of private property, the right of individuals to transfer titles to property on the basis of voluntary and unanimous exchange, and the rule of law (although Rothbard does not give the state pre-eminence in legal matters). Economic freedom is primarily an issue of the rights of individuals, not of groups or collectives. Apart from Rothbard, every treatment of economic freedom also recognizes a legitimate, but limited, purpose for the state or government. The range of legitimate tasks includes the maintenance of law and order, defence against external enemies, definition and

protection of property rights, enforcement of contracts voluntarily entered into, and the provision of a variety of public works, which varies from author to author. Adam Smith, for example, accorded the state responsibility for education, provision of roads, and monopoly rights in national shipping. Milton Friedman assigns the state the legal right to issue money. The central problem with every philosophical advocate of limited government is how to confine the state to its agreed-upon limited tasks! There is no stable law of limited government equilibrium. As Thomas Jefferson has stated: "Eternal vigilance is the price of liberty," and sometimes even that is not enough.

Once the government has ceded (or arrogates to itself) any task, it requires resources to carry out these duties. It can acquire resources through taxation, borrowing, or by issuing its own money.¹ Taxation is inherently compulsory and borrowing is possible on the promise to repay through the power to tax. The state spends money to accomplish its principle objectives. It can, if it wishes, coerce individuals and private firms through the issue of regulations to perform certain tasks in addition to or in lieu of its spending objectives. It can permit or restrict an entire range of private economic activities, including travel, transfer of funds, determination of prices and wages, choice of occupation, and entry and exit into particular lines of industry, as well as specify the conditions for the establishment of a business. In the pages that follow, I try to identify a wide range of factors that, taken together, comprise a comprehensive view of those areas of government control over economic activity that impinge on individual economic freedom and that will, when fully elaborated, permit an assessment of the degree of economic freedom that exists in any given society.

Governments are a fact of life in every country of the world. They possess a legal monopoly on the use of coercion which can be used to restrict or expand economic choices. Several Western industrial democracies have been restrained in the exercise of their coercive powers by written constitutions, custom, convention, or social consensus, though these restraints have been significantly weakened in the twentieth century. The majority of countries in Africa, Asia, and Latin America have been and remain under the control of largely autocratic regimes, though a handful of these in East and Southeast Asia have excelled at promoting economic freedom, despite the absence of democratic institutions. In some Third World countries, democracy appears to be springing to life, but only time will tell how durable these new representative institutions are.

Private Property

Private property is the common denominator that underpins every liberal philosophical treatment of individual economic freedom. John Locke regarded the existence of private property as the proper condition of man in a state of nature; the primary function of civil society, to which man granted the rights he

enjoyed in the state of nature, was to protect and preserve private property. Most important, the state has no right to take any part of a man's property without his consent. For Friedman, the conditions of voluntary and unanimous exchange that constitute the free market require private ownership of the means of production. The institutional arrangements upon which the market system rests include the definition and meaning of property rights, and the enforcement of exchange of property (contracts) voluntarily consummated. Rothbard's theory of liberty rests upon the rights of private property and the free and voluntary exchanges of property titles. Even Freedom House regards private property as the most fundamental component of economic freedom, although restrictions may be imposed on its use by the will of the majority.

The free and voluntary exchange of property titles goes hand in hand with the rights of private property. Unless each individual controls the use of his property, including his right to transfer it to another party in exchange for some consideration, the notion of private ownership and use has little meaning. Thus, freedom of contract is inherent in private property. Western history can be described as movement from social relationships based on status to relationships based on contract, in which an increasingly larger share of the population enjoys freedom of contract. A free society affords every individual freedom of contract in contrast with, say, an aristocratic society in which only the nobility can enter into contracts to exchange titles. Economic freedom is thus enhanced as societies evolve from relationships based on status to relationships based upon the universality of contract.

Property rests in one's own body, labour, and possessions. The pages of the *Wall Street Journal* illustrate a myriad of forms of property ownership encompassing human capital, real assets, and financial assets. Apart from a strict libertarian perspective as set forth in Murray Rothbard's writings, the freedom to have and use property is not absolute. It is limited by concern for the rights of others and the requirement that the state extract from individuals a portion of private property to perform its essential tasks (e.g., build roads and maintain national defence). Once the state secures sufficient resources to fulfil its tasks, further state control over property, either through additional extraction of resources, direct ownership, or regulation of its use, concentrates power in the hands of political authorities and erodes an individual's freedom to use his property as he deems best.

A good starting point is with land ownership and control over the right to use or transfer land. Land titles may be held freehold, leasehold from other private individuals or the state, or in common. Land titles may be freely transferred or subject to restrictions. Land use may reside largely at the owner's judgement and discretion or may be severely limited by governmental authority.

A good illustration of strict control of private property is found in Great Britain. Every structure that is more than 30 years old is subject to planning consent on the part of local government. A disproportionately large share of the en-

tire British housing stock effectively comes under historical preservation regulations. Modifications, renovations, and additions to privately-owned dwellings are subject to government control. In this case, the property itself is private, but its use is largely controlled by government.² Britain also maintains large areas of land on the outskirts of cities in the form of green belts, on which most forms of private development are disallowed.

Zoning, which is nearly universal, also affects the scope and extent of freedom of land use.³ Building codes and permits are an almost universal vehicle used to control private premises in advanced industrial countries.⁴

In April 1988 the National People's Congress amended China's Constitution to permit individuals to trade 15-year leasehold rights to state-owned property, thus giving those leaseholds the characteristics of private property. Previously, the Chinese Constitution banned private ownership of land. The Chinese case demonstrates clear movement in the direction of establishing a greater degree of private property rights.⁵

The power of eminent domain represents another intrusion into private property. The amount of compensation that may be paid to someone whose property is confiscated or used for public purposes determines whether the rights of the property owner have been mildly or seriously violated. Access over private property to waterfront beaches represents another encroachment on private ownership.

An especially insidious violation of the economic freedom of property owners is rent control. Rent control ordinances restrict owners of rental property in the rents they can charge and in the annual increases they can impose on existing tenants. Rent control has played havoc with the housing stock of U.S. cities ranging in size from New York to Berkeley. In each case, buildings are allowed to be run down since owners cannot obtain a reasonable return on their investment and new construction is often discouraged. Rent control is also unfair. New York is home to thousands of well-to-do tenants in luxurious accommodations protected by rent control, who may pay as little as ten cents on the dollar in rent as against true market value, while others scramble for cramped quarters at vastly higher market prices.

Apart from land and residential dwellings, patterns of control over the ownership of capital in all of the various forms that financial assets are held and over productive property should be considered. What are the limitations on the form and scope of financial assets that can be privately held? Does the government limit interest payments (as in the prior Regulation Q) to deposit holders? Is the banking system competitive or regulated by the government? Can individuals and firms obtain capital from private institutions, which hold private savings, rather than depend on the government to allocate capital? Are there any restrictions on the transfer of financial assets between people within or across national borders? Do factory owners have to compete only with other private firms or with subsidized government-owned enterprises? How extensive are regulations

on the activities of private industry? How widespread are the economic activities of state-owned enterprises? What is the size of the public sector (as a measure of the share of private property that is taxed away)? What is the extent of government intervention in the economy (e.g., pollution controls, mandating fringe benefits, etc.)? Answers to these and other questions measure the relative degree of freedom that owners of property possess over its use.

The Rule of Law

The rule of law is generally regarded as an indispensable requirement of a free economy. The rule of law serves both to protect individuals from the criminal acts of other persons and to prevent political leaders from making arbitrary, capricious decisions that transgress individual rights. The enjoyment of fundamental human rights, including individual economic freedom, the sanctity of contracts, and the protection of private property, depends on the rule of law, which requires capable lawmakers, an efficient, incorruptible police force, and an impartial and independent judiciary. Throughout history, many countries (e.g., China) were governed under a system best described as the rule of man, in which emperors and their officials made case-by-case rulings without regard to a formal written law or prior decisions. In such instances, the judiciary is typically an extension of the government, and generally upholds the claims of the state against non-compliant individuals or groups.

A key feature of the rule of law is equal application of the law for all classes of people. Every individual should receive equal treatment before the law. Otherwise, society can discriminate in favour of one or more classes of people against others by according differential treatment in the making, enforcement, and adjudication of the law.⁶

Lawmakers play a critical role in protecting economic freedom. Virtually every country has a constitution, or basic law, which may contain provisions regarding the security of property and individual economic freedom.⁷ It is important to assess whether legislatures or other law-making bodies respect or disregard those constitutional provisions. In many countries, constitutional provisions have no applicability whatsoever; in others, they may be strictly honoured. In yet others, courts may possess the legitimacy and authority to compel legislatures to respect basic constitutional provisions.

Law includes a dimension of order. In this vein, it is relevant to examine systems of police protection to measure their effectiveness in preventing crime and apprehending criminals. Victims of crime are not secure in their property.

It is especially critical to examine the legal system of every country to determine how it enhances or infringes economic freedom. This examination should include the following:

- the presence of a formal legal code;
- a description of the legal code;
- the place of the judiciary within the governmental structure, its independence, and its powers to overturn legislation or executive decrees;
- the constitutional status of the judiciary;
- the stability of the judiciary;
- rights of appeal;
- the attitude of the judicial system to private property; and
- the tradition of the judiciary in enforcing property rights and individual freedom.⁸

Taxation and Non-tax Revenue

The subject of taxes is as old as history itself. Since the beginning of time, tribal leaders, monarchs, generals, feudal lords, and their successors have exacted taxes from their subjects to pay military and civil expenses. Unwilling subjects have grumbled and often revolted against excessive exactions. French peasants revolted against a salt tax in the fifteenth century. The founding of the United States can be traced to the revolt against English impositions: the stamp duties, the tea tax, and others. The lore on taxation is replete with sayings that are in everyone's lexicon: "the power to tax involves the power to destroy," "the art of taxation consists of plucking the greatest number of feathers from a goose with the least amount of squawking," "no taxation without representation," and "death and taxes are inevitable."

Every government needs revenue to pay its bills for military and civil expenses. But governments don't want to spend all their time putting down taxpayer rebellions. Therefore, the question of how to tax has preoccupied social philosophers from the virtual beginning of recorded history.

The father of modern economics, Adam Smith, offered his views on taxation in his classic work, *The Wealth of Nations*. Smith strongly opposed direct assessment of income through an income tax, because it entailed an inquisition of each taxpayer. Second, he opposed taxes on necessary articles of consumption or on wages, on the grounds that such levies would raise the price of labour. Third, he advocated the financing of public works by their users without placing any burden on general tax revenue (Smith was an early proponent of user fees). Fourth, he argued that taxes should be kept low because high taxes encourage evasion and often result in a smaller revenue than might be collected from more moderate taxes.⁹

To implement these general principles, Smith set forth maxims of tax collection. Taxes—time of payment, manner of payment, and amount of pay-

ment—ought to be certain and not arbitrary. Every tax ought to be levied in the manner in which it is most convenient for the taxpayer to pay it. Administrative costs should be minimized.

The objectives of taxation are relatively straightforward. First, it must raise sufficient revenue to support the operations of government. Until the twentieth century, most governments taxed away no more than one-tenth of their nation's annual income, except during wartime or when they were in grave economic straits.¹⁰ Second, taxation can be used to encourage socially desirable behaviour or discourage undesirable behaviour (e.g., drinking, smoking, and gambling).¹¹ Third, taxation should try to distribute the cost of government equitably, though the issue of fairness is a thorny question. Finally, a tax system should foster economic growth, stability, and efficiency.

How can we evaluate tax systems? Economists have traditionally invoked the standards of efficiency, equity, and simplicity. Efficiency is a tried and tested concept in economics, which means maximizing the satisfaction that citizens derive from the economy. An efficient tax system requires that taxes should distort as little as possible the prices resulting from the interaction of supply and demand in the market. Tax policy should strive for neutrality between investment and consumption and among products and industries. To achieve this goal, it is imperative to avoid high rates of taxation. High tax rates are associated with smuggling, bribery, corruption, tax shelters, evasion, and the erosion of incentives to work, save, and invest. High tax burdens (aggregate levels of taxation) shift resources from private to public hands, where funds are typically used less productively.

Equity, the second standard, historically meant equal treatment of equals, which conforms to American constitutional guarantees of equal treatment before the law. Families with identical incomes should, according to this principle, contribute identical shares in taxation (except in unusual circumstances). A uniform or proportional tax meets this norm of "horizontal equity."

Since the Great Depression and the New Deal, ability to pay, or "vertical equity," was regarded as a hallmark of sound tax policy. Underpinning vertical equity was the idea that fiscal policy could be a tool for redistributing income. Taxing incomes at progressively higher rates—graduated taxation—became associated with this norm. In practice, the high tax rates that exceeded 90 percent in the United States in the 1950s fostered a steadily expanding regime of loopholes. Vertical equity fell into disfavour in the 1980s as several Western industrial economies sharply lowered their marginal tax rates.

A third norm for evaluating tax systems is simplicity, which encompasses comprehensibility of the system, the ease with which taxpayers can figure out how much they owe, and the time and effort they have to put into filing their tax returns.

With these standards, low aggregate burdens of taxation, low rates of taxation, and simple systems of taxation enhance economic freedom. Con-

versely, high tax burdens, high marginal tax rates, and complexity harm economic freedom.

Taxes can be levied in a variety of forms. They may take the form of direct (on income or wealth) or indirect (on consumption) taxes. They may be visible or hidden.¹² They may be explicit or implicit. (Implicit taxes include a whole range of governmental regulations, price controls, subsidies, tariffs, and exchange rate policies that have tax-like effects on decisions to work, save, and invest. These are taken up in the discussion of regulation, trade, etc.)

The International Monetary Fund's list of tax and non-tax revenue includes the following broad categories:

- taxes on income, profits, and capital gains;
- social security contributions;
- employers payroll or manpower taxes;
- taxes on property;
- domestic taxes on goods and services;
- taxes on international trade and transactions;
- others taxes (poll taxes, stamp taxes);
- surpluses of government departments;
- administrative fees;
- fines and forfeits;
- capital revenue (sales of assets, stocks, land); and
- grants (from abroad).

There is one or more specific tax subsumed within each broad category. For example, domestic taxes on goods and services include general sales or value-added taxes, excises, profits of fiscal monopolies, taxes on specific services, motor vehicle taxes, professional licenses, etc. A well-designed tax system for any given country may need to take into account the specific structure of its economy (agricultural, industrial, services, open, closed), and try to strike a balance between direct and indirect taxation.

Taxation and Freedom

Every dollar levied in taxes reduces private consumption by a dollar, thereby diminishing the freedom of the taxpayer to spend his money as he sees fit. On that basis, freedom is diminished in direct proportion to the level of taxation. In aggregate terms, the higher the level of taxation, the lower the degree of freedom.

The structure of a tax system is also critical in assessing the consequences for economic freedom. A low-rate system enhances freedom in giving the taxpayer control over the lion's share of every dollar earned. A high-rate system gives government the lion's share of the last dollar earned. It turns the taxpayer into an economic agent of the government. High rates of income or consumption

taxes diminish economic freedom. By reducing efficiency, high tax rates reduce after-tax incomes for everyone in society, thereby diminishing choice and freedom. Thus, a system of low rates is preferred to a system of high rates even if both raise equal amounts of revenue. Indeed, if low tax rates stimulate strong economic growth, total government receipts may actually rise. However, so long as personal disposable after-tax income rises in excess of what it might if based on a system of higher taxes, the fact that overall government receipts also increase need not diminish individual economic freedom.

Visible taxes foster economic freedom. When taxpayers know and feel the real burden of taxation, they are more likely to take an interest in government finances. To the extent that invisible or hidden taxes foster a fiscal illusion, taxpayers may be more tolerant of high levels of taxation.

General tax revenue should be limited to the minimum required to finance the legitimate essential tasks of government. Taxes should not be used to redistribute income or pursue social goals. These can be accomplished through expenditures after careful deliberation by legislatures or other governmental bodies. Reliance on user fees to support specific benefit programmes minimizes redistribution. Economic freedom is thus enhanced to the extent that costs and benefits of government programmes are effectively synchronized for individuals.¹³

Government enterprises should operate on a commercial basis without taxpayer subsidies. Users of postal services should bear the full cost of mail delivery. Of course, economic freedom is enhanced to the extent that the provision of economic services is left in private hands.

Modern technology gives government tax agents steadily increasing power to intrude into the private affairs of individuals. High speed computers, which can match taxpayer identification numbers for billions of magnetic tape entries and pieces of paper on virtually every conceivable form of economic transaction, threaten to unmask the private economic affairs of individuals before the scrutiny of revenue agents. Sustained improvement in the means of collecting taxes in the hands of rapacious revenue agents seriously threatens individual freedom. It helps to recall that social security numbers were not intended to be used for purposes of identification.

The imposition of severe penalties without regard for due process, including the power to seize assets for non-compliance or tax evasion, gives the government another powerful tool with which to encroach upon individual economic freedom.

Public Spending

Public spending is the counterpart of taxation.¹⁴ For centuries, the principle of balanced budgets regulated budgetary policy. Governments sought to avoid sustained or systematic deficits, although wartime and periods of economic

downturn required borrowing or the inflationary practice of printing money to cover costs. During the past 50 years, budget deficits have become a way of life in most advanced and developing countries alike. One hopeful sign occurred on 16 March 1988 when British Chancellor of the Exchequer Nigel Lawson announced both a surplus of £4 billion in the budget and his government's commitment to budgetary balance in future years. The public sector borrowing requirement (PSBR), the British term for deficit, has been replaced by public sector debt repayment (PSDR), a novel change of events.

Until the twentieth century, government spending in most countries generally consumed less than one-tenth of national income. There was widespread agreement that government spending was to be limited to the provision of law and order, national defence, and a modest level of public works and education. In nineteenth-century Britain, for example, spending on social programmes comprised 10 percent of the overall budget in 1801 and remained at that level through 1851. By 1885, spending on social programmes consumed 20 percent of the budget which itself only represented 7 percent of the GNP. Thus, in the late nineteenth century, government social spending comprised between 1 and 2 percent of GNP. Social spending, largely transfer payments, grew by leaps and bounds after the Second World War. Public sector employment in Britain comprised only 0.9 percent of the labour force as late as 1881; by 1980 one-third of the labour force were working for the government.

Public spending can be classified into the following broad categories: expenditure on goods and services (including wages and salaries), interest payments, subsidies and other transfer payments (to non-financial public enterprises, other levels of government, non-profit institutions, households, and transfers abroad), and capital expenditures. A functional classification would include: general public services (general administration and public order and safety), defence, education, health, social security and welfare, housing and community amenities, other community and social services, and a broad range of economic services (roads, postal services, airports, etc.).

A balanced budget would eliminate the need for interest payments, which has become among the largest spending categories for many countries. Within the classical liberal tradition, general administration, public safety, defence, and some public works represent legitimate expenditures of government. Housing, social services, social security and welfare, and health represent the unwarranted intrusion of government into the private affairs of individuals.¹⁵

Generally speaking, economic freedom is maximized to the extent that people exercise responsibility for their own affairs. The modern welfare state represents a major intrusion in the private lives of most citizens, since many transfer payments and in-kind services come with strings attached. The recipients of welfare payments and services often have to meet conditions laid down in law and enforced by bureaucrats, at great cost in personal freedom.¹⁶ The size of the welfare state has grown dramatically in the twentieth century. In many West-

ern industrial democracies, the public sector spends more than half the national income, with the overwhelming share going to transfer payments and social programmes.

Public Spending and Economic Freedom

An assessment of the relationship between public spending and the enhancement or diminution of economic freedom should examine the relative size of the public sector as a share of national income. However, this simple measure fails to capture the structure of public spending. A large public sector in wartime may be far more compatible with maintaining individual freedom than a considerably smaller public sector in peacetime in which the bulk of public spending does not reflect those legitimate tasks of government that cannot be left to the private market. It is important, then, to classify expenditures on the basis of legitimate essential tasks and other categories that could and should remain the responsibility of private individuals and firms. The range of legitimate essential tasks may vary among countries in accord with differing political cultures.

The requirement of a balanced budget also impinges on economic freedom. When taxpayers can shift the costs of current spending onto future generations, it allows them to demand and consume a higher level of government services than they might be willing to pay for under the requirement of budgetary balance.

A final note on public spending and economic freedom. In the absence of some constitutional limitation on the level of public spending that may be permitted in any society, it may be important to assess the degree to which categories and levels of public spending represent genuine social consensus. In California and other states, constitutional tax and spending limits require voter approval by simple or supermajority to override these limits. This process of amending state constitutions is available to simple majorities in many states; the federal U.S. government process is more cumbersome. Thus, the presence of constitutional limits on taxes or spending is an indicator of economic freedom.

Economic Regulation of Business and Labour

Economic regulation is a commonplace activity of government. It affects the activities of individual businessmen and firms, the rights of individual workers, choice of occupation, freedom to travel at home or abroad, free entry and exit into different lines of production, and the freedom of prices from government control to equate supply and demand in the market place.

Some historical examples illustrate changes in the scope and nature of government regulation of business and labour. Control of employment in the Middle Ages in Britain, for example, resided in municipal guilds and manorial authorities. As economic life organized on a national basis, the central government assumed this regulatory power. For centuries, the government enforced an

industrial regulation code that mandated apprenticeship in various crafts, set and revised maximum wages each year based on the prices of bread and ale, and required a minimum yearly term of employment to insure job security.

Other historical instances of economic regulation include the woolen industry. The British Parliament issued innumerable acts containing prescriptions about the length, breadth, and weight of pieces, processes of stretching and dyeing, ingredients either prescribed or forbidden for the preparation of raw material, finishing of the cloth, and methods of folding and packing. To enforce these elaborate laws, England had a regular army of specially appointed officials, measurers, inspectors, and checkers who stamped each piece of approved cloth.

Other examples of economic regulation include chartered trading companies which received royal monopolies to operate in specific regions; the Navigation Acts which severely restricted shipping; and colonial regulations which proscribed commerce between colonies and mother countries.

In the midst of the heyday of *laissez-faire*, the British government began to issue factory acts to protect children and women, and to regulate hours of work. Factory and coal mine regulations were followed by a variety of measures dealing with sanitation, public health, food and drugs, housing, public education, and broader rights to unionize and strike.

The twentieth century, especially the latter half, has witnessed a rapid expansion in the extent and variety of government involvement in business. In the United States and other countries, a plethora of government agencies were created which are involved in actions affecting virtually every firm in every industry. These affect environmental controls, job safety inspections, equal employment opportunity enforcement, consumer product safety standards, and energy restrictions. The costs of regulation include the support of government regulators,¹⁷ higher prices to consumers to cover the added expense of producing goods and services under regulations, jobs lost due to regulation, the closure of small firms that can't afford the burdens of regulation, and a reduced flow of new and better products that slow the rise in living standards. Each of these effects diminish individual economic freedom.

Regulation of business has its counterpart in labour regulation. These include the presence or absence of statutory minimum wages, legislation governing sick leave, vacation time, fringe benefits, and the hours of work of men, women, and children, workmen's compensation ordinances, wages that must be paid workers on government contracts, and pension fund requirements, among others. To the extent that these regulations reflect current market realities, they need not be viewed as obstacles to productive enterprise. To the extent that they raise the costs of production, they are likely to reduce employment.

In most countries, individuals are free to choose their own place and type of employment, and to offer services on the basis of mutual agreement.¹⁸ In some countries, however, the government assigns jobs and place of work. In mainland

China, for example, most workers are rigidly tied to geographically-based work units that control ration cards for housing, food, clothing, health care, and other goods and services; workers are not free to move about the country in search of better or higher-paying jobs.¹⁹ In South Africa and the Soviet Union, internal passports limit worker mobility. In a handful of countries, people have been compulsorily resettled to new locations or involuntarily exiled. Freedom of travel, either within a country or to emigrate abroad to pursue economic opportunities and interests, represents an important aspect of any person's economic freedom.²⁰

Most governments control the activities of labour unions or trade unions, including the right to strike, political activities, and membership requirements. When the union representing air traffic controllers declared a strike in 1981, President Ronald Reagan fired the publicly-employed strikers on the grounds that the strike was illegal. Mrs. Margaret Thatcher struggled long and hard to break the coal miners' union's stranglehold over the coal industry in the early years of her first term.

Regulation is a two-way street. A government can regulate or deregulate industry and labour. Nineteenth-century Britain illustrates the process of deregulation. A succession of political leaders reformed and ultimately repealed the navigation clauses, which resulted in free competition in shipping. Other acts included deregulating the manufacture of linen, repealing the ban of the free movement of goods and skilled artisans out of the country, repealing the colonial regulations, terminating the monopoly privileges of royally-chartered joint-stock enterprises, and allowing the formation of labour unions. Modern American examples of deregulation include the airline, communication, financial service, and other industries.

Regulation and Economic Freedom

The proper regulatory role of government in a free society should be restricted to those acts that support the essential legitimate activities of the state. In this view, government should be empowered to control negative externalities such as air and water pollution, and to impose safety requirements on food and drugs, transportation carriers, and the producers of other goods and services that affect public health and safety.²¹ Of course, how government goes about its tasks may determine the cost and effectiveness of these measures. It makes a big difference whether government taxes, fines, or shuts down any enterprise that emits pollutants. In this vein, government may possess the right to ban strikes of public employees in health, safety, and security areas.

Regulations that confer benefits on specific firms within an industry, or that confer benefits on an entire industry at the expense of consumers, violate the economic freedom of those who wish to enter into a regulated line of production and of consumers who are forced to pay higher prices or are denied the

opportunity to purchase certain goods and services that are not produced. It should be possible, in principle, to assess the degree and costs of regulation on an industry-by-industry basis within each country and the extent and costs of labour regulation. The minimum degree of regulation consistent with the government performing its legitimate tasks maximizes individual well-being and economic freedom. One approach might be to issue the equivalent of a regulatory yearbook.

Other indicators of economic freedom include the presence of free entry and exit into every line of industry—save those that affect internal and external security, the absence of wage and price controls, and the lack of compulsory government allocation of inputs or procurement of outputs. Legal formalities required to set up a business should be few and inexpensive. The government should not discriminate between resident and non-resident investors.

In addition to the freedom of individuals and firms to conduct business free from government regulation, the conditions of employees—how wages are determined, the freedom to choose type and place of work, the right to travel at home or abroad in search of better opportunity, the right to form collective organizations (without coercing other individuals to join against their wishes), the right to strike—also affect economic freedom. A free market in labour goes hand in hand with a free market in business.

Money

The relationship between monetary systems and economic freedom is extremely controversial. Friedman, for example, stipulates that the provision of a monetary framework is a legitimate task of government, and that a commitment to sound money can best be realized by a (constitutional) rule which requires the monetary authorities to keep the percentage rate of growth of the monetary base within a fixed range, say, between 3 and 5 percent per year. In this view, a well-regulated fiat currency system is consistent with economic freedom. Other students of monetary history disagree. They point to instances of free banking that did not require any central monetary authority, thereby reducing the role of government in the private affairs of individuals; or they point to the gold standard, in which the government sought to guarantee the value or price of money, rather than try to determine the quantity of money in circulation.²²

In modern times, virtually every government in the world monopolizes the issue of money and the operation of its nation's monetary system. Apart from issuing its own national banknotes and coinage, a government may select another country's currency as its legal tender (Panama uses the U.S. dollar), permit other currencies to circulate alongside its own (the Bahamas), issue gold coinage which enjoys legal tender status (though these coins are not intended primarily for use in financial transactions but rather to raise funds from coin collectors and

those who want to hold gold in the form of coinage), or peg its currency to that of another nation (the Hong Kong dollar is equivalent to the U.S. dollar one step removed, at a rate of H.K. \$7.8 to U.S. \$1). In addition to the issue of money, governments may promulgate legal tender laws, regulate banks and other financial institutions, impose exchange controls, and forbid private competition.

The primary objectives of monetary policy are to provide a regime of stable prices and to facilitate commerce and steady non-inflationary growth by insuring the right supply of circulating medium and credit without excessive cycles of boom and bust. These are no easy tasks!

There seems to be no inherent reason why government should possess a monopoly on the right to issue money and declare it the sole legal tender for transactions involving the government (payment of debts and taxes) or transactions between private parties. Nor do practical reasons weigh in on the side of government monopoly. Friedman has repeatedly written in the *Wall Street Journal* that the Federal Reserve Board does not operate on the basis of any consistent rule that he can find, even during that period in which the Fed said it was adhering to a money supply growth formula. (The Japanese, Germans, and Swiss have been more successful than the Americans in maintaining price stability since the collapse of the Bretton Woods agreement in 1971.) He has also written that it is neither feasible nor desirable to restore a gold or silver standard in the United States. Friedman is thus left with an ideal, but as yet unrealized, practice of monetary policy as a legitimate task of government consistent with his arguments on individual economic freedom.

Once government monopolizes money issue, a basic point of principle is at stake. The role of government in enforcing the rule of law is to provide a framework within which individuals can conduct their personal affairs. A key element in that framework is to preserve the value of the medium of exchange, which requires a sensible monetary framework. Debasing the currency through inflation, letting its value decline sharply in the foreign-exchange markets, suspending convertibility, or imposing exchange controls violates that point of principle. It is highly desirable for the government to sustain a mechanism of monetary control that is compatible with a stable value of the currency and that requires an absolute minimum of government intervention in either domestic financial markets or the foreign-exchange market, thereby minimizing the need for financial regulation and foreign-exchange controls. Only a handful of governments have successfully preserved the values of their currencies in recent decades.

As indicated above, monetary systems have taken a number of forms throughout history. These include metal coinage, both gold and silver; a strict gold standard in which paper currency is convertible into gold coins or bullion at a fixed rate; a silver standard; a bimetallic standard; a fiat currency in which banknotes are neither backed by any commodity (or commodities) nor are redeemable at a fixed rate, and which may or may not be convertible into other currencies; a pegged currency in which the government guarantees the

convertibility of its currency into the currency of one or more other nations at a fixed rate of exchange; and a floating rate system in which the government lets market forces determine the value of its currency in world financial markets.

Other aspects of monetary policy include the regulation of banks and other financial service sectors, the presence or absence of restrictions on capital movements (e.g., foreign exchange controls), and the right of private individuals to own gold and other precious metals.

It is important to put monetary policy in the broader context of overall economic policy. The experience of the four Asian “tigers”—Hong Kong, Korea, Taiwan, and Singapore—demonstrates that businessmen in free economies can adjust to a wide range of or major changes in monetary systems. Hong Kong’s economy grew at annual real growth rates of 9 percent for three decades even though its government switched from a fixed-rate pound sterling standard to a floating-rate system in 1974 and back to a fixed-rate dollar standard in 1983. Korea suffered high rates of domestic inflation, but the government periodically devalued the currency to maintain a stable real exchange rate, which kept Korean products competitive in world markets. Taiwan fixed the New Taiwan dollar between 1960 and 1979 at the rate of N.T. \$40 = U.S. \$1, thereby maintaining the equivalent of a gold-standard rule, balance-of-payments, fixed exchange-rate monetary system. Since 1980, the central bank has pursued a quantity growth rule of money supply designed to accommodate non-inflationary, high real growth. It has also adjusted reserve requirements, conducted modest open market operations in treasury bills, raised or lowered interest rates, eased or tightened import and capital controls, and acquired a growing stock of foreign assets to neutralize the persistent, large trade surpluses which exceeded \$75 billion in 1988. During the past year, the currency has appreciated to N.T. \$28.50 = U.S. \$1, yet economic growth has remained at double digit levels. Singapore sets the value of its currency in terms of a basket of foreign currencies. In every case, businessmen in each country possess a large measure of economic freedom to buy and sell in domestic and world markets, which enables them to cope successfully with wholesale changes in the monetary system or the exchange rate.

Mainland China, in contrast, virtually eliminated inflation between 1957 and 1978, maintaining almost perfectly stable prices, but its citizens conducted their economic affairs under a Soviet-style, highly centralized, command-and-control economy that brought only modest increases in productivity and living standards.²³ Since 1978, the government has increased its reliance on market forces to stimulate growth. As a result, prices have been allowed to rise to reflect conditions of supply and demand. Repressed inflation has broken into open inflation, which has reached double-digit levels on more than one occasion. Rising prices have gone hand in hand with greater economic freedom. Thus, in the case of mainland China, the presence or absence of price stability is a misleading indicator of economic freedom.

Money and Economic Freedom

The preceding discussion points to the following policies, practices, and institutions that should be examined to establish a link between monetary policy and economic freedom:

- the legal right of non-governmental entities to issue private currency;
- the absence of legal tender laws;
- the right to buy (free of sales or other taxes), own, and exchange gold coins;
- an accurate description of the monetary system;
- the successful conduct of monetary policy in terms of both price stability and sustained economic growth while avoiding cycles of excessive boom and bust induced by overly rapid expansions or contractions in money supply. Price stability without growth does not necessarily foster economic freedom;
- convertibility of currency (into goods and services and other currencies);
- the absence of foreign-exchange controls;
- free inward and outward movement of capital; and
- competition within banking and financial service sectors.

Foreign Trade

Economists generally agree on the economic merits (efficiency aspects) of free trade. Free trade also maximizes economic freedom. It enables individuals to buy and sell freely on world markets, thereby purchasing goods and services at the lowest possible price and selling products at the highest possible price. It gives individuals the widest possible choice of consumer goods. Free trade also permits specialization, division of labour, and the principle of comparative advantage to work to the benefit of individuals and firms in each country. Autarchy or self-sufficiency rarely produces sustained high rates of economic growth for long nor does it foster individual freedom. Those socialist and developing countries that pursued policies of self-reliance, self-sufficiency, import substitution, protectionism, and other inward-looking policies turned in dismal records of economic performance since the end of the Second World War compared with other countries that pursued outward-looking export-oriented policies in a general milieu of free trade. Today, mainland China pursues an open-door policy toward the West, and even the Soviet Union has stated its goals of glasnost and perestroika (openness and restructuring) in search of better economic performance.

Throughout history, instances of genuine free trade have been few and far between. Most have been in small communities on the frontiers of major powers or city-states that lived on their trading wits. A chronological listing would include the following:

- The Greek island of Delos: 166-69 B.C.
- Cyprus: fourth century, (under Ptolemaic rule); fourteenth century
- Champagne Fair Towns of France: twelfth to thirteenth centuries
- Flemish city-states of Belgium: eleventh to sixteenth centuries
- Hanseatic league cities: twelfth to nineteenth centuries
- Antwerp: fourteenth to sixteenth centuries
- Livorno, Italy: 1593-1860
- Genoa, Italy: seventeenth century
- Tangier, as British colony: 1662-83; as international city: 1945-57
- Gibraltar: 1704-1988
- Malta, as British colony: 1801-11
- Ionian Islands, as British colony: 1814-62
- Heligoland, as British colony: 1815-90; within Germany: 1890-1910
- Singapore: 1819-1957
- Hong Kong: 1841-1990
- Great Britain: nineteenth century
- New South Wales, Australia, as British colony: 1870-1900
- Danzig: 1899-1940

Other mini-states include the Channel Islands, Cayman Islands, Monaco, Liechtenstein, Andorra, Melilla, Trieste, Canary Islands, Aden (now defunct), and Labuan and Penang (now defunct). The general pattern is one of free trade largely confined to small territories that specialize in serving as warehousing and trans-shipment centres and free trade surviving for relatively short periods of time.

Impediments to free trade include customs levies on imports (tariffs); export duties; capital controls; restrictions on foreign direct investment and the free repatriation of capital, interest, and dividends; and the existence of government-controlled marketing boards that acquire and distribute imported goods, or which purchase primary products at below-market prices for resale abroad at market prices. In addition, many governments employ a wide variety of non-tariff restrictions that include quotas, permits, licenses, monopoly rights, preferential access to credit and foreign exchange, and the deliberate policy of maintaining an overvalued exchange rate to cheapen imports (and which effectively taxes exports). The presence or absence of these obstacles to free trade across national boundaries affects the degree of economic freedom that exists in a country.

Summary

We have examined the basic attributes of economic freedom and the conduct of government policies that enhance or harm individual economic freedom. Seven distinct categories have been identified for consideration: private property, the rule of law, taxation, spending, regulation of business and labour, monetary policy, and free trade. Each of these categories is enormously broad and requires detailed conceptual specification to enumerate those features that support or endanger economic freedom.

Other methods of classification can further subdivide these seven categories. For example, regulation of business and regulation of labour can be treated as separate categories. Within the realm of public spending, such areas as welfare and environmental controls may deserve separate consideration. It is hoped that this symposium will make considerable progress in refining these preliminary definitions of economic freedom.

Notes

1. The state can issue gold or silver coinage and it or the market can employ that coinage as a monetary standard. It can also clip coins, issue paper money which is backed by bullion, issue fiat paper money which contains no backing, or issue bonds with a promise to repay borrowers through its compulsory powers of taxation.
2. Taxation of real property, and general wealth taxes, is discussed in this chapter's section on taxation.
3. To preserve the character of neighbourhoods, Palo Alto and several other mid-peninsula Bay Area cities in California have adopted rules that restrict the size of homes and renovations that add living space and second stories to a formula which states that no structure can consume more than 45 percent of a lot's size. An initial proposal of 50 percent was rejected and even the current 45 percent limit may be further downsized. In other California communities, the public sector has chosen to limit the number of sewer hook-ups it will permit, thus restricting development.
4. The existence of shanty towns and slums in many Third World countries indicates an enforcement problem.
5. It will be interesting to see if the Soviet Union and its Eastern European allies follow the Chinese path of injecting private property rights into their agricultural (and industrial) sectors.
6. Goals, quotas, and affirmative action measures pose serious problems for the notion of equal treatment before the law. To the extent that ethnic, racial, religious, sexual, or other categories of classification receive preferential treatment under law, such as jobs, university admissions, government contracts, etc., society will devolve from relationships based on contract, consisting of voluntary, unanimous exchanges between the contracting parties, to those based on status, controlled by the state. Individuals who do not enjoy preferential status will be inherently unequal, and thus suffer a diminution in their personal economic freedom.

The world is full of examples of the consequences of political conflict stemming from ethnic differences in the struggle to control resources. Good illustrations include Northern Ireland, Belgium, Lebanon, Malaysia, India, and a raft of tribally-divided African nations. See Alvin Rabushka and Kenneth A. Shepsle, *Politics in Plural Societies* (Columbus: Charles E. Merrill, 1972).
7. Separation of church and state may be an important provision in preventing one group of people from imposing their values over others, including the economic relationships of others. Islamic countries, for example, have always had to wrestle with the problem of charging interest on loans, which is prohibited under Islamic law.
8. The history of the United States Supreme Court shows dramatic swings in court rulings that serve to protect or erode individual economic freedom. Court rulings constitute an invaluable data source in determining increases or decreases in economic freedom.

9. Adam Smith was simply one in a long line of supply-siders who understood that high tax rates often result in less revenue than moderate rates.
10. We often forget that the War of the American Revolution was fought over a tea tax assessed at a rate of 1.25 percent. If one reads the contemporary fiscal policy literature of late nineteenth-century Britain, it becomes apparent that tax rate increases of fractions of a percent of GNP were seriously disputed on grounds of inefficiency and extravagance.
11. One must be very careful in the application of this provision. One man's merit may be another man's vice.
12. Perhaps the best example of hidden taxation is the inflation tax, which erodes the real value of personal wealth and which, combined with unindexed graduated rates, pushes taxpayers into higher tax brackets. Indirect taxes tend to be less visible than direct taxes. It may be no accident that Western Europe's disproportionate reliance on indirect taxes partially explains why it has higher tax burdens than found in the United States.
13. To the extent that taxpayers want government programmes, the burden of taxation that is borne does not diminish economic freedom. The problem is finding some basis for agreement on what programmes are truly desired and what decision rule (simple majority, supermajority, unanimity) should be used. Simple majority meets the criterion of John Locke and Freedom House. A two-thirds rule for new forms or rates of taxation is in place for California as a result of Proposition 13. One could argue that individual economic freedom rises in proportion to the degree of supermajority vote required.
14. Milton Friedman regards government spending, not taxation, as a better measure of the size of government intervention in the economy. The reason is that spending, if it exceeds tax and non-tax revenue, must be financed by borrowing or printing money, which imposes still further costs on the residents of a country.
15. The public safety aspect of controlling the spread of contagious diseases would constitute a legitimate task of government in classical liberalism. The benefits of an educated population also merit public support in the views of some classical liberals, but the practical effects of compulsory public education suggest that private provision could work as well.
16. Many welfare recipients may be perfectly willing to trade off individual economic freedom for financial security. In that event, the loss in individual economic freedom accrues not to the welfare recipients, but to those taxpayers who foot the welfare bill.
17. The estimated administrative costs of federal regulatory activities in the United States for 1989 come to \$10.1 billion, of which two main categories are environment and energy and consumer safety and health. The number of federal regulators in 1989 will total 106,000. See Melinda Warren and Kenneth Chilton, "1989 Federal Regulatory Budgets and Staffing: Effects of the Reagan Presidency." OP 69, April 1988. Center for the Study of American Business, Washington University, St. Louis.
18. Individuals are free to choose their type and place of employment in most countries, resources permitting. Those who cannot afford to leave their village, farm,

town, or country in search of better opportunity are free in principle that the opportunity remains once they acquire the needed resources. They are not necessarily banned by their governments from migrating. This illustrates the distinction between negative freedom (freedom from restraint) and positive freedom (freedom to do something on the basis of positive government action).

19. The process of liberal economic reform which has been underway since 1978 is gradually improving the economic freedom of both enterprises and workers. The National People's Congress in April 1988 adopted constitutional amendments legitimizing private enterprises, permitting the private transfer of long-term leases to rural land, and granting enterprises greater autonomy from party cadres. Experiments are underway with the selling of land and housing in certain portions of the country. Other proposals include freeing up labour and capital markets. The general pattern, however, remains one of state domination over economic activity.
20. Until a few years ago, Koreans under the age of 55 were not permitted to travel abroad, ostensibly to preserve scarce foreign currency. The age limit was recently lowered to 45. Similarly, Taiwanese were limited in their overseas travels by restrictions on the ability to acquire foreign exchange; their restrictions have been virtually eliminated. Finally, mainland China recently announced a sharp reduction in the number of students that will be allowed to pursue education abroad, with the greatest cutback applied to those who wish to study in the United States. The Chinese government fears that many, if not most, will be reluctant to return home upon completion of their studies since economic opportunities and economic freedom are much greater overseas.
21. Control of narcotics by government is a controversial proposition among libertarians and other proponents of economic freedom. Does the state have the right and duty to protect children from possible addiction? Do the ravages of drug abuse fall in the same arena as the need to control the spread of communicable diseases? Does the existence of drug enforcement programmes thus compromise economic freedom?
22. See Rep. Ron Paul and Lewis Lehrman, *The Case for Gold. A Minority Report of the U.S. Gold Commission* (Washington, D.C.: Cato Institute, 1982), for a brief monetary history of the United States and for arguments supporting a gold standard.
23. For a comparison of the effects of different economic institutions and policies on three different Chinese communities, see Alvin Rabushka, *The New China: Comparative Economic Development in Mainland China, Taiwan, and Hong Kong* (Boulder: Westview and San Francisco: Pacific Research Institute, 1987).

Discussion (Chapter 4)

Alvin Rabushka I tried to offer a preliminary definition, a check list, or a recipe of economic freedom ingredients. I was trying to identify the fewest number of dimensions that would be self-contained, consistent, and coherent. Obviously you could break them apart into many more. This same set of seven could be subdivided in ten, 15, 20, 25, or 30, as the case may be. I compromised in the trade-off to produce something that is both meaningful and simple.

Some of the seven dimensions represent notions about individuals and others represent aggregate notions about the whole society. For example, a marginal tax rate will affect an individual and an average tax burden may affect the society as a whole. Private property rights are largely an individual matter along some notion of the rule of law, but the overall level of public spending is a collective enterprise. The monetary framework is a collective enterprise. So there are dimensions co-mingled here that represent rights of individuals and that affect the collective, but in turn bear upon the likelihood that individuals will have more or less economic freedom.

A second way to slice through these seven categories is in terms of institutions or rules and policies or incentives. The first two—private property and the rule of law—I regard as institutional framework rules. The others are public policies that governments undertake which have an effect on people's capacity to do things economically and make them more or less free.

My taxonomy is guided by philosophical considerations. One cannot proceed without talking about private property. Indeed, almost every single socialist society in the world today has decided that what is fundamentally wrong is their lack of private property. The Constitution of the People's Republic of China was just revised to include private property. We are hearing talk about private property in other socialist and communist systems. I gave examples of areas that would come into private property, such as the right to transfer titles, rent control, zoning ordinances, or eminent domain. I read that virtually any building older than 30 years in Britain comes under historical preservation ordinances and one needs state approval to make any internal or external changes. That is an extraordinary example of control over private property.

A second area connected to private property is the rule of law. One is struck by the differences between societies when looking at their laws; in one community the rules are clear and one can expect fair and impartial treatment, and in another the laws seem whimsical and decision making appears capricious. How can one talk about the rule of law as promoting or enhancing economic freedom? I ran through several items such as the existence of a written legal code. For example, China doesn't have much of a written legal code so it is not surprising that people's individual rights, civil or economic, are rarely protected in practice. One can also talk about whether the judiciary is

independent, the structure of the legal codes, what kind of legal code it is, rights of appeal, and so forth.

For example, there have been some recent court decisions in the United States that have significantly expanded the rights of private property along the coast. In reviewing this legal dimension in the last year in the United States, a higher score could be given for the rule of law in advancing economic freedom for individuals. Once you create the state you empower it. The first area of state intervention I discuss is taxation. Taxation encompasses high taxes, low taxes, the structure of taxes, composition of taxes, rates of taxes, and whether a proportional low tax scheme promotes or enhances economic freedom as opposed to a loophole-ridden selective system with high rates on some and no rates on other kinds of activities. This is a question that Buchanan and others have debated at some length as to which enhances freedom more and which doesn't.

Public spending is another area. The size of public spending, how it is spent, and what it is spent on. There are any number of dimensions here. We have all too often looked at public spending as a share of GNP, which is too simplistic. One should identify within the realm of public spending the kinds of programmes that are good for economic freedom and those that are harmful.

A third area is regulation, and I have lumped in here regulation of business and labour. Apart from the power to spend money and the power to tax, the government can order us through decree and edict. Critics of a balanced budget amendment say that if one were passed then the government would change from spending money to regulating everything to accomplish its objectives. Regulation of business activity concerns internal free trade. Regulations that enhance internal free trade promote economic freedom; those that restrict internal free trade harm economic freedom.

A fourth area is money. In recent years a controversy has been developing over whether the government should have a monopoly on the issue of money. One can hypothesize that a gold standard would foster more economic freedom than a fiat standard. Or that the fixed exchange rate would foster more freedom than floating rates. In any case, since every country in the world runs a monetary system, it is worth exploring the relationship between monetary systems and economic freedom.

A final category is foreign trade. To the extent that there are restrictions on the free flow of goods, services, money, and people, they impinge on freedom.

My taxonomy is intended to lay a broader framework than the kinds of dimensions of economic freedom that were included in the Freedom House survey. It is intended to incorporate dimensions that make sense and expand to include new dimensions, producing rankings in each area that would, ultimately, lead to a rating or ranking of economic freedom.

Robert Poole I would like to focus some attention on Alvin's discussion of rule of law as one key category. Obviously, the rule of law is fundamental and the kinds of things that he talks about—a formal legal code, constitutional status, an independent judiciary, rights of appeal, etc.—are basic for a free society. However, I am wondering whether this really belongs in the *economic freedom* rating of countries on a comparative basis, as opposed to the political or civil freedom category that Freedom House is already rating.

One of the problems with Lindsay Wright's discussion of economic freedom is that it tends to mix in civil liberty-type things like freedom of assembly, communication, speech, media freedom, and so forth which aren't really economic. They are really more like civil and political freedoms. I think we should be careful not to fall into the same erroneous position. Given that this enterprise is attempting to work within the general framework of the Freedom House scheme of things, namely three separate components—political, civil, and economic—I question whether these types of rules of law considerations really are properly economic per se. They are presupposed in economic freedom, but they are also integral to the kinds of political liberties and civil liberties that are talked about in the other categories.

Henri LePage I'd like to say to Bob that the concept of the rule of law is much broader than the concept of political freedoms. I find it more essential, and the very basis for the idea of economic freedom.

Alvin, when he was presenting the framework of Freedom House, noted the absence of constitutional limitations. But I don't find any reference to the rule of law in his listing of constitutional limitations. I would like to know why.

Just one more comment on this issue. It is very interesting to look at one of the paradoxes of freedom. In France, we never had any constitutional limitations for 200 years. In 1974 a change was introduced in our Constitution. It was a very small change—a different means for appointing people to the Supreme Court. Since then two methods of constitutional limitation have developed. The first one appeals to the French constitutional court, and the second, to the European Court of Justice in Luxembourg. So I am tempted to think that for the last 15 years we have had an enhancement in our liberties.

But look at the opposite side of it. Once you start having appeals to the constitutional court you get precedents. When you are on the opposition side, every time the majority passes a new law you call on the court and say, "this is not constitutional." Then you get a precedent determining whether they are going to reaffirm the right to private property or reaffirm some kind of welfare right. When there is a change of government, the opposition becomes the majority and the majority becomes the opposition. The new opposition is going to call into question any new law that is passed by its opponents. What is the end result of this? It is very simple. Today we find ourselves in a situation where we can no longer move in any direction. We cannot have a socialist revolution. But

we cannot have a full liberal or classical liberal revolution either. For example, if we wanted to privatize some industry we could be deemed as acting unconstitutionally because there is a precedent for a conflicting welfare right. The principle of constitutional limitation or review is something of a two-edged instrument. It can enhance freedom and, at the same time, reduce it by reducing your liberty of action in the future.

Michael Walker This comment bridges between the comments Alvin made in the last session and those he made this session. Is the measurement we are trying to make here like relative humidity, where you have to know what the capacity of the system is in the first place before you can make an assessment? Or is it a constant like an atomic number, or inches, where you know what your measurement of length is at a fixed temperature or pressure or whatever?

It seems to me that what we are after is a measurement more like relative humidity than an absolute measurement. We can't ignore the ways in which people choose and the kinds of choices they might make. Consider Alvin's section on taxation and how we would go about assessing it in this context. The level of taxation may or may not be coercive depending on what the capacity of the economy is to absorb taxation. I don't think Milton's humorous comment about the 10 percent tax rate having been a kind of universal maxim through history gives us any help, because I don't think it has been universal. Further, in each of those contexts the 10 percent rate would have meant something different. We really do have to establish a context before we can make a judgement. Or did he have some absolute measure in mind? I guess I am really asking a question. My conception of this is that it has to be relative but maybe I am wrong. Maybe it can be an absolute measurement.

Alvin Rabushka Ideally, I would like to have some absolute yardstick measure. Then, to the extent I can measure each society, I can have relative ranges. But Mike's point is certainly valuable. If there was a unanimity principle at work, then a society with a high tax rate based on unanimity would be more free than a society with a lower tax rate based on less unanimity. But there never is unanimity—there never will be. My inclination is to shoot for something more absolute and then from that try to attain relative rates. I would like to think that low tax rates and low overall tax burdens foster economic freedom. People who choose to have higher tax rates or higher tax burdens are choosing to accomplish other things, but at a price of less economic freedom. They are not getting economic freedom by collectively choosing higher taxes. They are getting something else with the money spent and they are getting less economic freedom. I don't want to confuse or link together the issue of economic freedom and what they are getting for their money. I think those are separate issues.

Zane Spindler I want to address Bob Poole's point about the necessity of the rule of law. It is absolutely essential if you want to protect the three D's of private property—how it is defined, defended, and divested. Without the rule of law these concepts cannot be stable (which is Milton's point on the requirement for freedom) and hence they cannot give a basis for private property or, equivalently, personal freedom.

Ellen Paul I want to respond to Henri's point about the problem he sees with constitutional limitations and the likely role the constitutional court would play in setting precedents that would thereby make change more and more impossible. I think the problem is that French justices have only been at this for 14 years. They should study the experience of the United States. Our justices have become very adroit at rarely overturning or overruling cases but raising to a high art form the making of distinctions when there really are no distinctions to be made. Our Constitution and our courts were no barriers at all to the New Deal and the welfare state.

One of the clearest examples of distinctions without a difference was a case called *Pennsylvania Coal v. Mahon*, decided in 1922. The case dealt with the regulation of coal mining that caused subsistence. It was challenged as a taking of property without just compensation, a violation of our Fourteenth Amendment to the Constitution. The Supreme Court held that when regulation went too far—as they said it did in this case—it would be overturned as an unconstitutional “taking.” Virtually the same case, as factually identical as any two cases could be, appeared before the Supreme Court in 1987 (*Keystone Bituminous Coal v. DeBenedictis*). They now said the same sort of regulation is perfectly constitutional. The only difference anybody could see was in one case the legislation affected bituminous coal mining and the other anthracite. The legislation in both cases was nearly identical but the 65 years between them made a big difference.

Antonio Martino I want to comment on this point. Italy has had a constitutional court for 40 years now, and the results are mixed, to say the least. By accident, they recently ruled in favour of free television. We now have free television because they made a mistake! But what is meant by constitutional limitation is not the existence of a constitutional court; it is, rather, having articles and principles embodied clearly in the written constitution that limit the scope of government. Italy has one such article. It didn't work very well because it was not phrased clearly.

Henri LePage France has it too but the French live in both worlds. We have strong principles of individual rights and at the same time we have welfare “rights.”

Antonio Martino If you have a bad constitution, it is not the fault of the constitutional court.

Henri LePage It is not really the Constitution that is at fault. It is the Declaration of Rights.

David Friedman With regard to the 10 percent rule, let's get our attribution correct; it's C. Northcote Parkinson's. As he put it, the productive people of the world discovered long ago that they would usually have to pay about 10 percent of their income to some gangster, feudal lord, or department of internal revenue. It matters little what you call it. But if the rate gets above that, the Israelites start looking at the atlas. There are probably better places to be than Egypt.

The second thing I wanted to say is related both to Bob's original point and to the discussion between Alvin and Mike. We want to distinguish democracy and economic freedom. If we have two societies, one of which has a 50 percent tax rate with broad popular support and the other a 50 percent tax rate with very little support, they are both missing exactly the same amount of economic freedom. Each individual only gets to keep 50 cents out of each dollar, but one of them is much more democratic than the other. That seems to me the only sensible way of getting a clear distinction between these two separate ideas of democracy and economic freedom.

I want to go on to a problem that has been bothering me. I would like to propose a solution, not necessarily the best one. The problem is, if you are trying to measure the amount of economic freedom by its value, how do you deal with a situation where some people claim that taxes produce benefits greater than their cost? That claim is itself a political argument, of the sort we are trying to use our measure to answer.

The best solution is to separate costs and benefits. Suppose we have a society with a 50 percent tax rate. Imagine another society that somehow produces all the same public goods, but the money comes from heaven so the society has a zero tax rate. How much better off would people be in the second society? That is, the cost of the restriction of economic freedom, via taxes, in the first society measures how much worse off they are for having the tax collected. In asking whether reducing people's economic freedom makes them worse off, we ask whether a society that by that measure has low economic freedom is poor or rich as a result. We are asking, in effect, whether the benefit from the taxes turns out to be more or less than the cost. To do that, we need to measure the cost separately from the net effect.

Let me put the same idea in different words. My definition of what we are measuring goes as follows: We take a society and we ask, if every restriction on what a libertarian considers complete economic freedom were removed and if nothing else changed, how much better off would the people in that society be? That is a measure of the costs that people in that society are paying in the form of

lost economic freedom. Once we have answered that question, we then let loose all the things we are artificially holding constant and ask, if we have two societies, one with high economic freedom and one with low, which is better off? That lets us measure whether what they are buying with economic freedom is worth the cost.

That is a suggestion for how you could deal with the problem conceptually. Not by asking whether taxes are popular or unpopular. Not by asking whether taxes produce net benefits or net losses. Merely by saying that if 50 percent of my income goes to the state, that is a reduction in my economic freedom. Maybe I get something that is worth that cost, maybe not, but the cost of government is how much that reduction hurts me, independent of what I get for it. That gives us a measure of the cost of reductions in economic freedom. If we could then somehow compare that reduction from taxes with the reduction due to the minimum wage law and the reduction due to some other restriction and sum them all, we would know how much economic freedom each society is missing. What I am proposing is an odd sort of contra-factual way of defining the cost of restrictions on economic freedom, but I am not sure I can see any alternative way.

Michael Walker David, are you saying that we have to think of freedom as choices, and what we are trying to do here is to conceive of the maximum choice set?

David Friedman Lack of freedom is having your choices restricted by other people's actions. Perhaps there are cases in which that is a good thing. I think we want to be agnostic about that in defining what we mean by economic freedom. Anybody who believes in limited government believes that some restriction is a good thing. Even I believe that under some circumstances it might be acceptable. But it seems to me that if I want to measure the lack of freedom, I want to add together the cost to me of every restriction on my action that is imposed by another human being.

To define what we mean by "imposed" we need some baseline of property rights; I do not want to include the cost to me of the "restriction" of not being permitted to steal from you. So start by imagining that I have all the rights I would have in Rothbard's perfect libertarian society or my perfect libertarian society or something similar. Everything else stays the same, the society is still defended, the garbage is still collected, but I have somehow been freed from all coercive restrictions. How much better off would I be? Now do the same calculation for each other person and sum it for everyone. We may be describing an impossible world, an internally inconsistent world, but we can still use it to define what we mean by the cost of restrictions on economic freedom.

Alvin Rabushka Let me try to make public what was a muddled, but getting clearer, exchange between Michael Walker and myself as a way of indicating where I hope this session will go.

To do that requires linking chapter 2 with chapter 4. That is, why did I even get into the philosophical aspects of economic freedom? The answer is that if you haven't decided what you think the conceptual notions are, there is not much point in trying to do a checklist of elements that you have pulled out of thin air.

What I was trying to do by looking at some cross-section of people who thought about this topic was to identify the quintessential aspects of economic freedom. They include private property, the rule of law, and so forth. But these features don't exist in a perfectly anarchical world, so we have government. How does one want to think about economic freedom? I thought it would be useful to define what represents the essential conditions of economic freedom, look at the minimum essential activities that the public sector performs, and classify those activities in terms of taxing, spending, regulation, and so forth. The bench-mark is a limited government maximizing individual liberty. All this government does is to enhance individual freedom. Conceptually, it is important not to confuse the additional things government does, even if people want them, with economic freedom. They reflect mere majority will.

There are two stages to measuring economic freedom. One is to pick out the dimensions that one wants to include in a system of economic freedom in a precise, rigorous, or quantitative way. The second stage is to question what the primary elements are within each dimension and how they can be qualified and quantified.

Milton Friedman I am glad to follow what Alvin has said. What I am going to say is not inconsistent, but more or less orthogonal to what he said. I am not going to go into the question of why I disagree with David except that it seems to me he was begging the essential question.

I want to go back to the very fundamental question of why we are here and what we are trying to do. This really comes to the concept of measurement that we keep on getting confused about. Let me illustrate by first starting out with something we have all had some experience with, intelligence and IQs which Gerard Radnitzky mentioned. People say IQs measure intelligence. They do no such thing. Intelligence is a very abstract concept. It is a very abstract idea. What IQ measures do is to provide a particular definition. In an IQ measurement, intelligence is defined as that thing to which you attach numbers by a certain set of procedures. That's a particular definition of IQ. You can have a dozen such definitions. That definition may be, as David suggested properly the other day, a vector of numbers—you have mathematical intelligence, literary intelligence, and so on. It may be summarized in a single number. The question is, what do we ask about that? Do we ask, is it right? No. That's a meaningless question. Is it

true? No. That's a meaningless question. There is only one fundamental question we ask about it. Is it useful?

What do we mean by, is it useful? By that we mean, does it enable us to make predictions about people's behaviour that we otherwise could not make, or not make so well, or not make so well on the basis of another set of approaches. So what do we do? How do we judge? Mr. Thorndike gives one intelligence quotient. Mr. X gives another. How do we judge which is better? Well, we judge which is better by taking a new sample of people, calculating their IQ accordingly to each definition, predicting something about them we didn't know, like how successful would they be in the next two years in school, or what careers would they go into, or something like that. And if Mr. Thorndike's measure of intelligence on the whole is contradicted fewer times and gives us a larger fraction of successes than somebody else's, then we accept his, at least tentatively. Somebody will come along and work on this and develop other ways of assigning numbers to intelligence, but the crucial thing is that intelligence is not a mountain that we can measure with rulers; intelligence, rather, is that thing which is defined, for this purpose, by the numbers we assign to it.

Now we come to economic freedom. This is a broad concept. I fully agree with Alvin's approach to defining economic freedom. If you look at the Lindsay Wright measures of political liberty and civil liberties, they aren't measuring political liberties. They aren't measuring civil liberties. They are giving particular definitions of civil liberties. The Lindsay Wright definition of civil liberty is that thing to which you assign a number by the whole specified reproducible procedures that she and her colleagues have outlined. The same with political freedom.

I believe their concept of political liberty is a very bad definition. It doesn't lead anywhere. I demonstrated last year that if you held civil liberty constant, political liberty had no relationship either to GNP or to the infant mortality rate. So it isn't serving that function. Maybe it is serving some other function. Maybe there is something else it will enable you to predict. I don't know what the usefulness of that concept is except that it enables people to embody their prejudices and preferences in a number.

Similarly, economic freedom. We all have some vague concept of economic freedom as we all have a vague concept of intelligence. But when setting out on our present procedure, we are not setting out to measure a well-defined, precisely-outlined economic freedom. We are trying to understand what it is all about. We are trying to get a definition of economic freedom which has a property that will enable us to make predictions that we otherwise couldn't make about some subject we are interested in. Remember, you may be interested in different subjects. For one purpose you may want one definition of economic freedom and for another purpose another may be better. We don't use the same definitions for all purposes. In the simplest case in economics, for some purposes it is perfectly okay to regard an industry as competitive. For other purposes you

want to regard the same industry as a monopolist. It depends on what your purpose is.

Our purpose is to get a better understanding of what aspects of institutional arrangements contribute to (a) people's prosperity and (b) people's sense of satisfaction in the sense of providing utility...if we knew how to measure utility in advance. That was my objection today; I don't know how to measure utility. We haven't any idea.

In economics I can give you some other examples. Utility is the same kind of notion as economic freedom or intelligence. Now, when we come to measure utility, what do we do? Von Neumann and Morgenstern defined utility as the number you get by going through a certain set of processes and seeing how people select among various bets. It turns out that this is a reproducible way of obtaining a particular numerical definition of utility. Also it turns out to be useful in predicting what kind of bets people will take or refuse. The concept has been used to study the behaviour of aboriginal tribes with respect to gambling and it has turned out to be very useful.

We want some way of providing an economic freedom index—a process of assigning numbers to economic freedom that will enable us to predict things we couldn't otherwise predict. For example, you give me information about three countries whose income is unknown and you ask me which one of these countries will turn out to have a higher income. Or, country A is making one set of changes and country B is making another. Which of these sets of changes are likely to be more successful in raising the standard of living? Which of these is likely to be more successful in getting a large segment of the population to express their happiness in certain ways, for example, by not emigrating.

Take a simple example. Can we predict external migration? Are the attempts of people to leave countries related to a measure of economic freedom? That would be a very useful and valuable purpose for our endeavour. But we can't judge one measure of economic freedom or another in the abstract and that's why I am not going to take up your silly suggestion, Walter. I have no basis for drawing up a list of what dimensions I want in economic freedom. I haven't done the work. I haven't studied it. After all, when I read the Spindler/Still study I started changing some of my views about how I should treat, for example, military service. If you had asked me offhand in advance, I would have given a very different answer than I will now give you after having gone through what I think is a very interesting bit of work.

Here is a statement from Spindler's paper: "It may be difficult to measure the aggregate value of economic freedom directly." It isn't difficult. It is a meaningless statement. What does it mean to measure the aggregate value of economic freedom directly? We are trying to proceed with a process of defining economic freedom in a useful way. We don't know what it is. That sentence embodies the misleading notion that there is a mountain out there and we are going to send a troop of people there with some rulers to see what size it is.

But that isn't our problem at all. There isn't any mountain out there. There is a set of abstract ideas and we're trying to pin them down. We are trying to see what it is we are trying to measure. There is no such thing as measuring economic freedom directly. What we want to do is to work backwards. We want to take an unobservable thing and convert it into something that has a relationship to observable phenomena of a kind that will make it a useful definition. Just as with IQ. Just as with utility. Just as with personal probability. You can keep on going like this, and the physicist here, I am sure, can give us lots of other examples of unobservable phenomena for which an empirical counterpart is constructed whose function is to be used, not to be observed, not to be contemplated.

Another purpose you might have is to find the concept of economic freedom that is most likely to change Parliament's vote on some issues you are concerned with. That might give you a wholly different definition of economic freedom than any of these other purposes we are talking about.

I am sorry to go on at such length but it seems to me that that is at the core of all of this... why I regard so much of the discussion as having been beside the point.

I want to make only one more comment. This is just more amusing than anything else. It refers to Charles Murray's question about New Zealand. This brings out a very important element. The New Zealand unilateral legislature is somehow or other, it would seem to me, intuitively relevant for our measure...why? Because we want to take a dynamic and not merely a static view; we want to look not only at the state of the institutions now but at what the likelihood is that they will be maintained.

This goes back to Alvin's definition of property. There is nowhere in that definition anything about the stability of property. For example, Alvin, you take that business in Britain about 30-year-old houses. That is less of a restriction, from my point of view, than if it were 30 years one year, 27 years the next, and 40 years the next. Somehow, that dimension of stability is important in order to be able to predict consequences. If I took a period of time in which I had exactly the same average definition of property but in one case it was stable and the other case it was fluctuating, I would predict that in the second case the utilization value of that property would be less, and its market value would be less. Again, I am attempting to show how I am trying to use this to predict, to find out things I can't otherwise know.

Antonio Martino I am not so sure that I want to say anything much after what Milton Friedman has said. I think what we are trying to build is not only for the purpose of prediction but also for the purpose of passing judgement on institutional arrangements in various countries. What we want to do is compare various countries with this index.

Milton Friedman With respect to outcome. With respect to the things that we want to predict.

Antonio Martino One way around it may be this. You could start from the empirical evidence of the nature of restrictions on economic freedom which have always come from government. Instead of trying to measure economic freedom we could try to construct indices of government restrictions on freedom.

Now, of these, I realize that there are pecuniary and non-pecuniary restrictions. For non-pecuniary restrictions, it is very hard to make comparisons. How is a country that has a minimum drinking age and a ban on smoking in public buildings better off than a country that has a ban on smoking in public buildings but no minimum drinking age? I am thinking of Italy. We have no minimum drinking age but we do have restrictions on smoking so it is very hard to make comparisons there.

We could do better with those restrictions that have a pecuniary dimension. Look at the ratio of GNP that goes to public spending and that which goes to other channels. Taxation always limits freedom of choice. This is a restriction on economic freedom. It may be a voluntary restriction if these people have voted and agreed on that kind of level of taxation; they may have voluntarily agreed to have that restriction, but it is, nevertheless, a restriction.

James Ahiakpor In spite of Milton's warning against believing that there is a mountain out there that we are going to measure, I am either not persuaded by his warning or I would like to stick with my own prior conviction that, indeed, there is a mountain out there that we want to measure. We all have notions about what it means to be free or not to be free. Thus, what we are trying to measure here are the restrictions on our choices that affect economic behaviour. Political and economic choices often overlap. There is a fine line between politics and economics, but I believe it is legitimate to try and measure impediments in the way of people's choices that affect their economic behaviour. I think it is much more settled in politics—we can talk about political freedom or lack of it. But I don't see why we cannot attempt to measure the counterpart in economics. If we accept this argument, then we can think about a better way of measuring economic freedom. For example, accept the view that taxes limit individual choices. Therefore, the ratio of taxes to GNP may be an indicator of restrictions on economic freedom. We also may select total government spending out of national income as an indicator. But if we are going to give up the notion that we have a mountain out there that we are trying to measure, then we might just as well go home, because there is nothing else for us to do.

David Friedman I am not certain whether I disagree with what my father believes, but I am certain I disagree with what he says.

Let me start with the case of IQ. Height is very easy to measure. It has predictive ability, especially in predicting success in basketball, but it would seem silly to say we will define intelligence as height in inches and conclude that intelligence is the chief determinant for success in basketball. The word “intelligence” already has a meaning; we want to find a definition that corresponds to what it already means.

Similarly, we could define “economic freedom” as the ratio of petroleum reserves to population. Economic freedom defined in that way would have some ability to predict per capita GNP, but that would not tell us much about economic freedom; it would be a silly definition.

We do not pick definitions at random and then find out what they mean, which is what my father makes it sound as though he believes, although not, I think, what he actually believes. We start with a picture of the world, an imprecise, possibly incorrect, map of what is happening, of what the causal connections are. On the basis of that picture we form the opinion that economic freedom will be associated with other things such as human welfare. We then try, using our picture of the world, to make a plausible guess as to what measurable variables related to economic freedom will, because of the same causal connections, be associated with measures of economic welfare.

It seems to me that the sensible strategy, or at least a sensible strategy, is to first ask, if I could measure everything imaginable, if I could do all hypothetical experiments, how would I measure economic freedom, i.e., what do I mean by amount of economic freedom? Once you have answered that question you have a good starting point for figuring out how to do actual measurements in the real world. This is the same strategy that economists use in defining concepts such as demand curves, supply curves, indifference curves, and utility functions, many of which we could measure if we had infinite ability to do experiments, even though we cannot in practice measure them in the real world. We use those concepts in forming our theories about measurable things such as GNP, unemployment rates, quantity of money, or whatever. So that is why I disagree with at least the verbal form of the methodological assertion my father has made.

Robert Poole It is very important to look at the political context in which this whole exercise is taking place. Probably everyone in this room believes, and for good reason, that there is a direct predictive relationship between economic freedom, as we would gropingly define it, and prosperity. But most of the world doesn't believe that. I don't think Lindsay Wright believes or understands that. Most political liberals don't. Therefore, it is crucial to the ultimate acceptance of what we are trying to do here to be able to come up with a predictive system, of the kind that Milton was outlining, that says, “If you observe certain conditions that are defined by measures of economic freedom and you get scores in the direction of high values on economic freedom, then over time we can predict that

certain kinds of prosperity are likely to follow from that.” If that can actually be empirically demonstrated, it will be a tremendous accomplishment. It is old hat to every single one of us, but it is not old hat in the real political world of governments and United Nations and Freedom Houses and all those people out there. So the ability to predict is crucial to the credibility of this exercise. To it being ultimately accepted and not being seen simply as an expression of the prejudices of a bunch of free market ideologues, but as a serious effort that has external validity.

Gerard Radnitzky I fully agree with Bob. A very important task is spreading the news of the success stories of the *European Miracle* (E.L. Jones), the *Rise of the West* (Rosenberg and Birdzell), and the newly industrialized countries of Southeast Asia. However, in a way, this is already recognized among thinking people, though often implicitly and begrudgingly. An example: Joseph Needham, the authority on the history of Chinese science and technology, claims that as late as the fifteenth century A.D. Chinese civilization was much more efficient than occidental in applying natural knowledge to practical human needs. How does he explain that China, nonetheless, did not achieve economic growth? Needham points to the institutional arrangements that “inhibited the rise of modern capitalism” (*The Grand Titration*, 1969, p. 197). A supreme, because unintended, compliment to capitalism coming from a lifelong Communist.

But let me return to Milton’s example of intelligence testing. The attempt to give an explication of certain aspects of the broad intuitive concept of “intelligence” arose from a practical problem. The French psychologist Binet was asked to develop a procedure for sorting out children who did not possess the ability to follow normal school instructions. The concept of IQ has been, most of the time, grossly misunderstood. Binet offered his IQ-test as a method of comparing individuals with respect to achievements in certain kinds of problem solving. The differential achievements were taken as indicators of capabilities which the individual possessed in various degrees. The question of how the individuals had come to develop these capabilities has not been touched upon. In that context, “measuring” intelligence is used metaphorically. Individuals are placed on a distribution curve that represents the distribution of a very narrow aspect of what we ordinarily mean by “intelligence.” Here, again, it is of paramount importance first to distinguish between explicandum and explicatum, and second to distinguish between concept and methods of ascertaining the presence or absence of the property designated by the concept. It is also important to notice that definitions as such are not important. In the present context, a definition is but one of the possible ways of introducing the refined concept, the explicatum. A definition is nothing more than an abbreviation, a convenience. What matters is the whole process of explication or, more

accurately speaking, that the concept proposed as an improved successor of the old concept is in fact a better instrument for the task at hand than the old one, the explicandum.

The other point I want to return to is Alvin's criticism of the explicatum of "economic freedom" proposed by Freedom House. As mentioned, an explicatum is a spin-off of a theory development. The theory that underlies the explicatum proposed by Freedom House is a confused theory of political democracy, based on the fetishes of unqualified franchise and majority rule. Apparently the Freedom House people have succumbed to what James Buchanan has labelled "electoral fallacy," the idea that, so long as governments act "democratically" in accordance with majority decision by a duly-elected body or something similar, the individual is sufficiently protected against the overreaching of the state. This reflects a monumental confusion with possibly tragic consequences. Democracy appears to have a tendency to erode capitalism and with it individual freedom. The urgent problem is how to return to limited government from a democracy that has turned into a welfare state. This could be done if it were possible—as, e.g., Peter Bernholz suggested—by means of institutional reforms to create interest groups or a political clientele concerned with the limitation of government. Perhaps there is no way from the cancerous growth of the welfare state back to limited government—except after a severe crisis.

A democratic process may have any outcome. Sometimes people agree to sell themselves into slavery, if they are paid for it—witness the example of welfare states like contemporary Sweden.

What about the theory upon which Alvin's explicatum is based? I take it that freedom is a bundle of rights. Hence an explication of the concept of freedom has to be based upon a theory of rights: a theory of option rights—there is no such thing as welfare rights. (The expression "welfare rights" is a misnomer for claims to provisions made upon unspecified addressees). Such a theory has to be a theory of economic freedoms and civil liberties. Following Walter Block, I consider "political freedom" a misnomer for elections at certain intervals—a process that may bring any outcome with respect to real freedom.

As a starting point for such a theory of rights, I would propose a concept that views freedom as a relational property between an individual chosen at random and a particular social system. Following Karl Brunner and William Meckling, I distinguish between scarce rights and non-scarce rights. (An example of a non-scarce right is "freedom of speech" in the sense of being free, in a dialogue situation, to pronounce any opinion, i.e., freedom of speech does not imply that others are obliged to listen to you or to tolerate that you disturb them if they don't wish to listen to you.) Freedom consists basically of the set of activities that are protected from interference by others and by the state—minimized state intervention—of course, as Hayek has always stressed, provided that equal protection is given to everybody.

With respect to scarce rights, the society with the most is the one that offers more freedom than its rivals and solves conflicts with fewer constraints than any other system. With respect to non-scarce rights, that system is freest that passes on to individuals the most full set of opportunities provided by nature. The state must, therefore, have the monopoly of violence and be strong enough to fulfil its protective function. At the same time it must be limited in its scope, i.e., not take on functions that the market can provide more efficiently. Political rights, whatever this means, are not a prerequisite of freedom in the all-important sense of private rights.

Democracy does not necessarily preserve limited government and, hence, does not necessarily preserve private rights. On the contrary, history teaches us that the democratic method, as we have practised it up to now (with unqualified franchise, etc.), has increasingly undermined private rights and individual freedom. Even the Thatcher governments in Britain have not prevented this. Total taxation takes a higher percentage of national income in 1988 than it did in 1979. History also teaches us that those countries grew fastest that were economically freest, such as Hong Kong which prospered because it had no political freedom and was a rather protective state. It is reasonable to assume that the factors that have fostered freedom in the past are the same as those that foster it in the present and will foster it in the future.

Alvin has indicated dimensions or aspects of freedom—economic freedoms and civil liberties—which overlap, as Milton has pointed out in the Michael Walker collection *Freedom, Democracy and Economic Welfare*. These aspects will certainly include such things as the right to low marginal income taxes, the right to sell one's services at any wage (voluntary contracts), the right to unrestricted entry into goods and service markets, and, in particular, the right to freedom of movement, i.e., the exit option, the right to emigrate, and the right to free capital movement. Freedom of movement, capital movement, and movement of human capital appear to me to be the key features of a free country. In the extent to which the right to free movement (human and physical capital) is realized, states will compete with each other for physical and human capital. An open international market of states would be the best climate for individual freedom. Unfortunately, we are very far from such an open world order—which is the contrary of world government as a cartel of states.

Europe appears to be entering a critical period. Postwar European thinking has been under the detrimental influence of French constructivist rationalism, particularly clearly visible in the form of monetary constructivism. Governments find it opportune to form cartels—witness the rhetoric of “harmonization” recently expounded, for instance, by Chancellor Kohl of West Germany. What Europe needs in 1992 is the opposite of “harmonization” or “co-ordination” via some central agency. It needs free competition not only among business enterprises but above all among states, among institutional arrangements, legal systems, tax systems, and so forth.

Henry Manne I would like to continue along the lines of Milton's suggestion that there are a great many dimensions to this whole issue of measurement and liberty.

Any issue of measurement here certainly involves factors that are both on the plus and minus sides—the costs as well as the benefits. It seems to me that Alvin starts off by measuring the inputs into the equation, all of which have negative aspects. That is, he looks at a list of interferences with a thoroughgoing free market, private property, free contract system. This can be done in a variety of ways. Indeed, I can think of one that has been done which nobody has mentioned. That is, every year or so we see a cute little story in the paper about someone who measured the absolute number of pages in the United States Code of Federal Regulation. It started out in 1932 as a small volume; it is gigantic today. That very crude form of measurement is the kind of thing Alvin is talking about.

We all know that the tax rate is precisely that kind of measurement. I am sure that if we look into it, we will find fairly sophisticated forms of measuring the impact of taxation. There may be disagreement about the ultimate incidence of measuring the exact costs on productivity of one thing or another, but there is literature on this subject.

Regulation and public ownership or public taking, which is really at the heart of the kind of thing Alvin is addressing, becomes a little more difficult to measure. What are the marginal social costs of a regime where government can expropriate property? Obviously, you can measure the exact amount on some scale, for example, of the market value of land taken away from individuals each year, and you can see if that goes up or down. Nonetheless, this all falls in the category of inputs into this measurement. The inputs do have a negative sign, however.

What is the impact of all of this? Now you can go back through these individual categories, as Alvin has, and offer to place dollar signs by each of these factors. That is, taxes in the United States cost individuals so much of what would otherwise be private wealth; regulation decreases productivity by so much, etc. You can go through that exercise and come up with some sort of measure. I don't mean to trick anyone. I am suggesting that the only way to do this sort of cost/benefit analysis is to have a common denominator. You can't say that freedom is on one dimension and dollars are on another because then you have no basis for making the measurement at all.

Where you can make more meaningful measurements of this is on the output side generally, at least in the sense that wealth has some significance for the matter of individual freedom. That is, as individuals acquire more private wealth, they can make a greater range of economic changes. No one denies that. The criticism is how significant that is versus other forms of freedom. What I am suggesting is that this may be the only means of measuring economic freedom

that we have. The others are there in some abstract sense but not in any sense that is useful.

There is another factor that comes in here. I am rather surprised it hasn't been raised up to now. There must be some very thoroughgoing Austrians here who would or should raise the issue that all this talk about measurement is nonsense. It has nothing to do with anything. It is a far more subjective concept than even Milton was talking about. He at least suggested that there may be a great range of objective measures for different purposes. But on this subject, a thoroughgoing Austrian would say, "Wait a minute, that's a meaningless concept. All you can look at and see in the outside world is what individuals in fact do." I think that is a very useful concept. It leads us to a notion that all we can look for as a measure, in the sense at least of talking to the Philistines or non-Austrians about this matter, is something like GNP. There may be others—perhaps life expectancy or infant mortality rates—but most other things simply aren't measurable. Let's just talk about a concept like freedom. The only thing you can talk about, and Henri wouldn't even let me go this far, is a measure of some sort of GNP aggregate figure. We don't have very much confidence in it. We know there are all sorts of foolish things in it. We know that if someone takes himself out of the labour force and makes himself better off by retiring and engaging in leisure, GNP goes down. But that is the fault of the measurement system. That doesn't mean that in abstract form the idea isn't correct.

Richard McKenzie Well, I raise again my objection to Henry's view, without further comment.

I have a few questions about measurement. Milton raised the issue of whether or not we should include something on stability and that is an interesting point. Should we do that or should we allow this measure itself to be unstable? If the measure itself is unstable, and Milton is correct, its value would be reflected in GNP. So would you want to include a component for stability?

Milton Friedman That's on the input side.

Richard McKenzie The other thing is, I am trying to follow up on Walter's suggestion of making a list, mainly because I suggested it to him. In trying to compose my list, I keep coming up against the question, how much money do we have to work with? I mean, this measurement problem could encompass the whole Canadian Bureau of Economic Analysis plus the Fraser Institute. Are we talking about a big budget? This is important because if you don't have much money to spend, then I could come up with a fairly simple list; but if you have a lot of money, I will come up with a highly-detailed one.

William Hammett I'd like to approach this for a second as if Alvin were approaching me at the Manhattan Institute with this suggestion. What objections

would I raise? The approach I would take would be to look at the difference between the political freedom index and an economic freedom index. How might they differ? Obviously, the political freedom index of Freedom House works. It's successful. The question is, would a comparable one measuring economic liberties be successful?

A few ideas have occurred to me to explain why the two are different in a way that puts a little more burden of doubt on economic endeavour. First of all, political freedoms are an end in themselves. Political freedom is a good thing to have. Economic freedom is really a means towards an end. I am talking about a popular enterprise here. Not something around this room but something that would fly with ordinary people. If you mentioned economic freedom to someone out there as opposed to political freedom, the right to vote for example, you would have to do a bit of explaining. The benefits of economic freedom are not self-evident to the average person as are those of political freedom. Also, political freedom has a dramatic and romantic edge that economic freedom lacks. There is a big difference between being put up against the wall and shot at dawn and Donald Trump's inability to evict a few rent controlled tenants from his Park Avenue apartment. That is one reason why political freedoms carry the greatest drama possible, like death. That is not the case with economic freedom.

There is a consensus with respect to political freedom. It is a social democratic consensus today. It happens to be very well captured in what Lindsay Wright says. That is one reason why labour unions are included—because that is part of this consensus. There is no comparable consensus, again outside of this room, with respect to economic liberties. Bush and Dukakis differed very little on political freedoms, but very much with respect to economic freedoms. Many people think that entrepreneurship is bad and we are suffering from an overdose of it in this country.

I organized two conferences overseas in the last two years on the topic of growth. Their actual titles were, "London Conference on Taxes and Growth" and "Frankfurt Conference on Taxes and Growth." In both cases we were trying to energize the debate on lowering taxes and encouraging growth and entrepreneurship...the whole George Gilder scenario, supply-side thing. At neither one of those conferences did the topic of economic liberties ever come up. It was treated strictly as a pragmatic thing. Will this produce more growth and more wealth or will it not? It comes back to the Henry Manne versus Milton Friedman debate. We all believe in economic freedoms here, we know what it leads to. But it is almost an impossible chore to try to translate this to the general public who relate much more to the concept of growth, wealth, things like that, which is the end result of economic freedom.

Rose Friedman This is in reaction to your comment, Bill. First of all, I am not sure whether people are more concerned about being shot or being slaves. One is economic freedom, the other is political freedom according to your definition.

The only virtue of being a slave rather than being shot is that you hope that maybe one day you will get out of slavery.

Milton Friedman Look at the Vietnamese boat people. You mean it is not a matter of life and death to them whether they have economic freedom?

William Hammett Take Russian dissidents as well. Most of them come to the United States for a job, but the preference is for religious freedom and freedom from persecution, from the Gulag.

Rose Friedman That's the only way they can get here. Bill takes the point of view of the elite who are talking in abstract terms about which is more important, economic freedom or political freedom. I want to talk about ordinary people who don't bother to vote most of the time because political freedom is not that important to them, but who are much more concerned about whether they can get a job, and if they get a job, what ways they will be restricted. Do you judge things from what you read in the media or from talking to ordinary people?

William Hammett But the interesting things about the Freedom House map are not the white parts, or even the grey parts, but the black parts, those parts which are lacking political freedom. That's really where the drama comes in; where you have a Jacob Timmerman or something like that. If it were a matter between white and grey, that map never would have attracted the attention it has.

Rose Friedman It is very easy to measure or judge or whatever you want between zero and a hundred, but I assume what we are trying to do is measure the in-between parts. This is where it becomes much more difficult.

Milton Friedman Just on the same point. I agree with Henri LePage, not Henry Manne, that you can't make distinctions between political and economic freedoms. Is it a violation of your economic freedom or your political freedom if you are prevented from buying a book abroad because of exchange controls?

William Hammett Well I agree with you, but that's the problem with this enterprise here. It is trying to distinguish between things like that.

Milton Friedman I agree with you, but I don't agree with the definition of political freedom that is implicit in the Freedom House rating. I think it is an absurd definition. Precisely because it treats these two as very separate things. But they are not. Economic freedom is simply freedom. Economic freedom is valuable in itself and not simply as a means. You talk to the people on the boats coming from Vietnam and ask them whether economic freedom is just a means. It's a life and death matter.

David Friedman A recent American example of people feeling passionate emotion about economic freedom involved the legislation against marijuana. That was strictly a restriction on economic freedom, the ability to buy a particular substance. A lot of people wanted to use it, many felt it was perfectly all right to use, and therefore they felt that their freedom was being infringed upon. That is at least one counter-example to the claim Bill is making that people don't really intuit the idea that economic freedom is freedom.

Robert Poole Let me draw our attention to the situation in South Africa today as an illustration of the relative importance of economic freedom and political freedom. The whole liberal mentality in this country is that political freedom is the issue, but the Leon Louw/Francis Kendall book has pointed out how crucial the denial of economic freedom has been to the black people in South Africa. This illustrates why people like us need to really make this an issue: to show the vital connection between economic freedom and good lives.

William Hammett That is a perfect example of why the book has never taken off. That entire approach is inefficient. In three years' time it has not captured any bit of the popular imagination in that country.

James Ahiakpor There is evidence that people believe economic freedom is something out there that can be measured. Indeed, the more of it, the greater the economic growth. I cite the works of Danny Landau in *Economic Development and Cultural Change* (1986), where he shows that out of 65 countries, those with higher government spending of national income grew less than those with lower government spending. Keith Marsden, 1983, for the World Bank, also shows that higher taxes lead to slower growth. I have used Milton's own words in a piece. I wrote, "Referring to the U.S. experience up until the Second World War, he shows that federal government spending out of national income was about four percent." Milton then argues that, and I am quoting him, "This remarkable fact should destroy once and for all the contention that economic growth and development require big government and especially centralized government." The same experience applies to Canada. All those who published these theses and have not discussed the evidence in terms of economic freedom may well have had it at the back of their minds; what we are doing here is filling in the gaps. Therefore, we should take seriously the view that yes, there is something out there for us to measure. I am sure Alvin deals with federal spending, especially with taxes, in the category of impediments to economic freedom. The evidence is there. The mountain is out there to be measured. I move that we design the appropriate measures for it and then get out there and do the actual measuring.

Lack of economic freedom really is at the heart of the suffering in many Third World countries. Government there has appropriated more resources to

itself through development levies, has restricted the right to exchange foreign currency, and has increased taxes. As a result, the economy deteriorates sharply. But after the government is overthrown, and the new regime adopts economic liberalization, including lowering the share of government in GNP, the economy quickly recovers. Such evidence is in support of the thesis that economic freedom promotes general economic prosperity.

James Gwartney I would just like to draw a parallel to the discussion here and mention a similar discussion that must have taken place when people first started talking about measuring unemployment. Most of us in the economics area would say that the unemployment rate is fairly easy to measure. The nature of the discussion, particularly today, has projected the view that establishing any kind of quantitative number to this thing, freedom, is virtually an impossible job. We have focused on all the objections, and I am afraid that in doing so we may be losing track of the quantifiability of some things that really are important.

Think of the problem that people who were developing a definition of unemployment must have confronted. Surely someone sitting around the table said, "Well, goodness, we have to draw a distinction between somebody who is laid off and is returning to work next week and somebody who has been unemployed for six months. How do we handle part-time workers? Surely we've got to draw a distinction between somebody who is currently not working on a job but who might take one if it were to come along and another who has worked 70 hours a week for the last six months and is therefore interested in taking a vacation for three or four weeks." All of these questions involve fine distinctions. If the participants focused only on these things they would have thrown up their arms and said, "Let's forget about this whole project." Of course, they didn't do that. It was possible to draw distinctions that were important between people who had a job and who did not have a job.

What happened is that they came up with a definition, to use Milton's term, or a measurement of a concept, because unemployment is concept. It's not something like height. What we do is we play around with the definition. What about some of the refinements that one could perhaps integrate into the definition that usually are not important but that in certain cases might be important? We see if the refinements make any difference. Beginning with their definition of unemployment, we refine it for certain kinds of problems. For example, if we think that comparisons are distorted because in the late 1970s 25 percent of the labour force in the United States was under 25 years of age, whereas in the 1950s that percentage was around 15 percent, then we refine the initial definition. We put together an adjusted index for the changes in the demographic characteristics when making comparisons between the two periods.

There are a lot of parallels here in the discussion of freedom to those kinds of issues. The first step is to come up with a definition emphasizing the things that are really important, like trade restraints, government price-fixing that

interferes with market activity, and the types of things outlined in both Alvin's and Zane's chapters. Then, for example, we would expect that issues concerning the stability of property rights that are provided in the Constitution relative to those not provided in the Constitution would represent refinements. For some kinds of problems these refinements may be very important; for others, they may not be. What about the issue of defence expenditures? If freedom is imminently threatened by an aggressor, defence expenditures of 20 percent of the budget may not be inconsistent with freedom. On the other hand, defence expenditures of 5 percent of the budget might be quite excessive in certain other kinds of instances. So we would expect, depending upon the circumstances in which we were going to apply the index, to make these kinds of refinements.

The same thing relates to the structure of expenditures. Are expenditures conducted in a manner such that people are really, either implicitly or explicitly, giving their voluntary consent. For example, when roads are financed by user charges we can be reasonably sure they are providing value to users. This is less true for roads financed by an income tax. These kinds of refinements may be important in some instances. In other instances, they may not be.

I do think it is important to come up with a starting place, which is what the Spindler paper and the Rabushka papers (especially chapter 4) are about. I don't think that we're in a unique position relative to the development of other measurements. You start, and then you refine the concept.

Just one final note. I chose unemployment which is an easy one. Just think about the problems in terms of quantifying GNP! A number of those things are really controversial in terms of how they are handled. In general they are overlooked today. So if we think of an index of freedom as being the opposite of an index of interferences with private activities, I do not think our task is any more difficult than was the case in some other areas where we have attempted to quantify concepts.

Ellen Paul I am a bit impatient with the direction that this session has been taking. We are reprising debates from yesterday about what is economic freedom, whether we can define it, whether it is useful to define it, whether it will have any effect if we can define it. I thought we were going to examine the categories that Alvin came up with and see whether they were comprehensive. We really haven't done any of that in this discussion and I hope that we can begin doing that at some point.

In that spirit I would like to turn to this paper and preface my remarks by saying that I think Alvin has really done an excellent job. But I would like to focus on one category that should be controversial. Regulation and economic freedom: here he talks about essential, legitimate activities of the state and then goes on to say that he feels that regulating externalities, such as air and water pollution, and imposing safety requirements on food and drugs and regulating transportation carriers and producers of other goods and services that affect

public health and safety, are all essential and legitimate activities of the state. I have a lot of qualms about those being essential functions of the state, particularly the regulation of food and drugs. How did the United States get along without such regulations until well into the twentieth century?

I wonder, Alvin, what your theoretical arguments are. In the first segment of your paper, I really didn't see any justification of any of these as essential functions of government. Adam Smith did talk about some public goods that the state should provide because it is not in any individual's economic interest to do it. I don't really agree with that, but even if Smith is right, you still can't justify your expansive list based on him. He was talking about roads and bridges and various things of that sort and not food and drug regulation. Aren't you conceding too much to regulation? We should have a purer standard and then assess each government's departures from it. You can start with a pure laissez-faire position and then consider everything else a departure. I know in the United States we are regulating common carriers right from the beginning, but I don't think that was the right thing to do, and it was certainly a departure from laissez-faire. I haven't seen an argument in Locke or Smith to justify that kind of standards and price regulation. I am just wondering what your theoretical basis is.

Antonio Martino I could add an item to Ellen's list. Alvin says that "taxation can be used to encourage socially desirable behaviour or discourage undesirable behaviour." I don't think that is a legitimate function of taxation.

Michael Walker I have two small points. One is on Henry's comment about the use of wealth as a proxy. The problem is that it leads people like Lindsay Wright and Raymond Gastil to suggest that redistribution of income can actually be a freedom-enhancing proposition. By doing this you are taking less away from people at the high income levels and giving more to those at low income levels in terms of enhancing their choice set. For no other reason than that, we may want to consider very carefully whether we want to associate ourselves with this view.

Henry Manne I think you want to look at an annual growth figure rather than at wealth redistribution, which will typically affect that in a negative way.

Michael Walker A real problem is that we don't have a common agreement around this table about what it is we are trying to measure. It isn't as though we have any disagreement about what intelligence is. As David says, we know what the concept is and we are just trying to find ways in which we can measure it. But with regard to economic freedom, I don't think we really do have agreement. That has become clear in private conversation with people in trying to get them to agree that what we are trying to do is maximize the choice set and libertarians

will say, “oh, no, that’s not what we are trying to do at all. We are trying to maximize the permitted set of activities.” Well, it can be the case, as Alvin points out, that by limiting people’s choice about the disposal of their income in the form of a tax, you actually increase the set of choices they have. Unless we can come up with an agreement about what it is we are trying to measure, without, as Walter says, getting into a protracted debate about anarchism and minimalism or ‘minarchism’ or whatever, then we are going to have some difficulty in finding good measures, whether proxies or actual measures.

Charles Murray I am trying to pin down whether there has been any progress at all. I would like us to agree that we are mainly interested in economic liberty as an independent variable. The sense that Henry is using, of freedom as indicated by wealth, is uninteresting.

The second comment is that I would go along with Ellen’s implied statement that we want the economic freedom measure to be one which has very little affect embedded in the measure itself. In the case of government regulation, for example, we aren’t worried very much about whether one can regulate in ways that are beneficial. All we really want to express in the measure is that less regulation is “less” on some dimension of interest, and that more regulation is “more,” and not to worry about it being better or worse.

Also, we need to come up with a statement more or less equivalent to what the IQ people do when they say, “Well, this is what I can measure.” Namely, we want to be able to say, “Here we have an interesting, intuitively useful construct to which we are now going to attach the label ‘economic freedom.’” I will give my own candidate statement, very imprecise, as something I have scribbled down in the last five minutes: “I have a bunch of indicators here which I will argue measure the degree to which individuals may engage in voluntary economic transactions and to keep the proceeds from these transactions.”

Alvin Rabushka We didn’t talk nuts and bolts as much as I would have liked. What has come out of this discussion is that, as I said at the very outset, the subject of economic freedom is extremely complicated.

People have talked about it over the years in a casual, intuitive manner. However few steps we have taken here, it has been a first small step in getting people to think about it more rigorously. I see economic freedom more broadly than some of you. I think it’s a means and also an end. One can think about economic freedom as choices, like consumption, but the act of choosing itself has merit. “Better red than dead.” “I only regret that I have but one life to give for my country.” In a number of these cases the act of economic freedom is in and of itself an end; in other cases it is simply a means to some other end.

I hope that people will be encouraged to think about economic freedom both in terms of means and ends, and to use the phrase “economic freedom” in a

more precise manner than we currently do. The more precise we can get, the more useful it will become. At this point, one is hard pressed to use the concept in any kind of precise, predictive, or explanatory way because we haven't anything that is conceptually or empirically precise. If we are going to be able to ever have a concept like this become part of social science, we will have to move in that direction. It is also a value and I see no problems talking about it as such when describing it as an explanatory or predictive tool. Both of those are equally important, equally meritorious enterprises. We should keep straight what we are doing, but after all, most of social science does have value implications. That doesn't stop us from doing social science and it doesn't stop us from applying social science in pursuit of values and policies.

I appreciate some of the points Ellen made, some of the points Antonio made, and I did not intend this to be anything other than a very first small step. It is certainly not the end-all-and-be-all I hoped that we would have come out of this with. I wanted hundreds of amendments, refinements, criticisms, suggestions, variations, deletions, and omissions so that we would have been forced to think our way through a lot of these areas where economic freedom is augmented, or detracted.

Chapter 5

Economic Freedom Ratings*

Zane Spindler and Laurie Still

Introduction

In order for economic freedom to serve as a goal of human endeavour or as a criterion for evaluating human activity and institutions aimed at other goals, it must be measurable in a way that is relatively consistent over time and space, and relatively uncontroversial. This might require an international system of accounts for economic freedom for all countries similar to that currently available for national income.¹ Of course, nothing to this standard currently exists. However, a first step has been taken.

In 1982 Lindsay Wright published her economic freedom ratings for 165 countries. Each country was rated high, medium high, medium, medium low, or low, based on her composite of similar ratings that she constructed for four separate economic freedoms: 1) freedom of property, 2) freedom of association, 3) freedom of movement, and 4) freedom of information.² These ratings represent a very impressive and relatively comprehensive attempt to rate economic freedom systematically. They also provide a focus for discussion about the difficulties and desiderata in measuring economic freedom.

However, while Wright's ratings are available for most countries at one point in time, they are not continuously available, and they are qualitative, rather

* We acknowledge Challenge 88 for financial support, Ben Brown for statistical assistance, Lindsay Wright for providing her unpublished ratings, and Milton Friedman for an extended telephone discourse on measuring economic freedom. We also acknowledge comments on previous drafts by John Chant, Xavier DeVannsay, Herbert G. Grubel, and John M. Munro. Our study was initiated at the request of Walter Block.

than quantitative, and subjectively, rather than objectively, assigned. Moreover, there are some aspects of economic freedom that are not covered by Wright's four freedoms and, consequently, by her overall economic freedom rating. Further, some of her freedoms as measured might be inappropriate for inclusion in an overall measure. In short, there is considerable scope for discussion and improvement of economic freedom measurement.

This chapter is aimed at providing an additional basis for discussion rather than any definitive improvements. In our first section we consider whether we really need to go beyond the information provided by the existing accounts of national income and expenditure in order to find reasonably consistent, uncontroversial, and quantifiable measures of economic freedom. We argue that net national income per capita, or its capitalized value, net national wealth per capita, could be viewed as a measure of the market value of economic freedom.

In our second section we consider whether Wright's ratings should be reweighted in order to provide a more economically relevant economic freedom rating. We find that her overall freedom rating weights freedom of association too high relative to freedom of property. In our third section we discuss our own measurement of two specific economic freedoms: freedom from involuntary military service and freedom of foreign trade and investment. While currently far from perfect in either conception or construction, these measures do provide extra interesting information about other dimensions of economic freedom.

Our final section briefly evaluates economic freedom ratings to date. Most current integer rating schemes appear to provide relatively similar economic freedom ratings. However, integer rating scales may be much too crude to serve as the sophisticated tool required by the evaluators and monitors of economic freedom. Ultimately, a universal, continuous, quantitative, and much more costly measure must be constructed if finer distinctions about economic freedom are required.

Rating Economic Freedom: An Easy Way?

Rating economic freedom for a given individual is, at best, a difficult task, but still much easier than rating economic freedom for a nation. Following a micro approach, we could take an array of specific economic freedoms,³ study the degree to which each one exists for a particular individual, determine the individual's relative preference for each category, and combine these to obtain a unified measure. Producing such a measure for more than one individual would multiply the work required by at least a multiple equal to the number of individuals. Aggregating the individuals' measures, however, would require us to make interpersonal comparisons when choosing how each of the measures would be combined—even if we follow the egalitarian inclination normally extant today and weight everyone equally.

A similar problem arises if a macro approach is taken where specific economic freedoms are directly rated for a nation as a whole.⁴ Any composite of these freedoms would require an implicit or explicit weighting scheme for which there may be no obvious justification.

More importantly, in either a macro or micro approach we would have to explicitly recognize that there are certain interdependencies between individuals as well as categories. For example, as workers gain rights relative to employers—so called “industrial democracy”—employers (especially government) switch from being agents of consumers or stockholders (voters) to being agents for employees. Employee sovereignty replaces consumer sovereignty! Would this increase or decrease overall economic freedom? Employees’ freedom increases while employers’ and consumers’ freedom decreases but the whole may be more or less than the sum of its parts.⁵

The nature of this problem is captured in spirit by the maxim “one man’s meat is another man’s poison.” We could recast this, as indeed Ingmar Stahl (1988, p. 300) has explicitly, as “one man’s right [liberty] is another man’s duty [non-right].” Recognition of the implications of Stahl’s point is fundamental in assessing economic freedom. It is like Coase’s point that recognition of the reciprocal nature of externalities is fundamental in assessing externalities.⁶ Indeed, they are really the same point. In the economic context, both externality and freedom involve reciprocal relations between individuals. Further, the actual value of both an externality and economic freedom depend on the actual structure of those relations.

From an economic standpoint, the structure of such relations matters only because voluntary exchange is constrained by transaction costs. Transaction costs in turn may be determined by the structure as, for example, when voluntary exchange is prohibited or restricted. Each possible structure involves a potential or, in the case of existing structures, an actual total economic value. Moving from a structure with a lower total economic value to one that is higher would constitute a Pareto improvement if the costs of the move could be covered by the difference in economic value.⁷

Normally, economic evolution could be viewed as a gradual and automatic process of discovery and implementation of Pareto improvements—mistakes aside, of course.⁸ Such evolution, being in part accidental and in part determined by initial and evolving institutions, could proceed in widely divergent directions. North (1988), for example, gives an overview of the evolutionary successes—the U.S. deriving its institutional setting from the U.K.—and the failures—Latin America deriving its institutional setting from Spain. The success or failure of any evolution of institutional structures might be judged by many criteria, but surely measures of economic value would be prominent among them. It would be an easy step to take these economic measures as giving valuations of the existing institutional structure or of the economic freedom allowed by that structure.

Further, Coase (1960, pp. 73-74) stressed that production functions should be specified, or be viewed, as containing “rights” as factors rather than actual physical entities. As a natural extension, the aggregate production function itself could be viewed as the structure of rights, freedoms, duties, etc., with respect to the use of natural resources, previously produced goods (capital), labour, and knowledge (as embodied in capital, labour, as well as that available through patents, copyrights, and the public domain). This implies that the economic value of national output, national per capita output, and national wealth could be viewed as yielding, respectively, flow, efficiency, and stock valuations of the economic freedom embodied in the existing and anticipated structure of rights.

By taking this broadest possible macro approach, economic ratings of economic freedom or, alternatively, market ratings of economic freedom could be obtained directly from widely available national accounts data or from yearly rankings based on that data in such popular outlets as *Eurocurrency* or *The Economist*.⁹ Another major advantage is that the interdependency or interpersonal/intercategory comparison problems are explicitly avoided. The market implicitly provides the automatic and arguably the best resolution.

There may be some justification for further adjusting these “gross” ratings by excluding the government sector and/or including the private non-market sector.¹⁰ Also, it may be appropriate to adjust the extremes solely due to identifiable one-shot phenomena such as drought or resource booms. Either gross or net, these market ratings are quicker and less expensive to develop and have a better theoretical rationale than more detailed micro or macro ratings of economic freedom.¹¹

Alternatively, a measure of the redistribution of economic freedom could be given by the rate of inflation¹²—which determines distribution between holders of real and nominal rights, or the transfer ratio (government transfers/national income)—which determines distribution between holders of entitlements and productive rights. While these relative freedom measures may be of interest to specific individuals or groups within a society, the measures of interest to any individual judging from a “veil of ignorance or uncertainty” standpoint would be those that measure the total value of freedom, such as gross or “net” GNP or GNP per capita.

For those who would not go as far as Coase in specifying production functions in terms of rights rather than physical quantities and who believe that physical resource availability substantially determines national output, it may be appropriate to consider the cross-country production function residuals as potential measures of the market value of economic freedom. Or, following Posner’s (1987) argument that wealth maximization is a superior ethical principle of evaluation and nearly equivalent to the competing deontological principle,¹³ it may be appropriate to rate relative economic freedom of nations according to relative net wealth.¹⁴ However, those who strongly believe in inalienable rights would

not accept either approach without strong reservations with respect to equivalent constitutional guarantees of such rights across nations.¹⁵

Since it may be difficult to measure the aggregate value of economic freedom directly with any great precision, it may be more economic to concentrate on some implied or imputed measures such as those suggested above. Whatever we use is bound to be controversial. It may be of pedagogical value to have the controversy swirling around the question of the extent to which market value reflects the value of economic freedom. Many people on both ends of the political spectrum would probably deny that abstract concepts such as freedom or liberty are at all comparable with tangible value or even amenable to quantitative measurement. It might be revealing for them to be challenged to think otherwise.

The Wright Ratings of Economic Freedom

Lindsay Wright's rating of economic freedom for 165 countries is truly impressive—especially when one gets down to the nitty gritty of producing an alternative. Continuous, consistent, and quantifiable data on such a wide range of countries is very difficult and time consuming to collect from an average university library or computerized data base. So before proceeding with what might turn out to be only an inferior duplication of her considerable effort, it may pay to consider whether some manipulation of her ratings might make them more useful to those who might object to them in their current form.

One objection that might be raised concerns her relative weights. In constructing her overall rating from a set of four ratings of separate freedoms (property, movement, association, and information), she implies that she uses equal weights, but it seems that some freedoms are more important than others. For example, freedom of property—including the freedom to voluntarily exchange it—may be more important than freedom of information, especially if the latter is interpreted as freedom of press, since, according to Hayek, market prices efficiently convey the information necessary for free exchange, which in turn generates such informative prices.

Alternatively, it might be argued that some freedoms should be weighted negatively, since their existence might decrease other, and hence total, economic freedoms. For example, the freedom to form restrictive associations impinges on others' rights to free exchange. Such considerations, plus intuition, might lead one to suspect that most participants at this conference would agree that property freedom should be ranked the highest and association freedom the lowest—although there might be considerable difference in opinion if the rankings were to be made cardinal!

This weighty objection brings two questions to mind: What weights were actually used by Lindsay Wright? And, what weights should be used? We used regression analysis to tackle both questions.

Implicit Wright Weights

We found the actual weights for each of the four freedoms by using their numerically equivalent ratings (on a scale of one to five) as the independent variables in an OLS regression with the overall economic freedom rating as the dependent variable. The regression coefficients for the four freedoms as the independent variables can be taken as the actual average weights. If the four freedoms were weighted equally, their weights should be one-quarter each. However, this is not the case, as can be seen below in equation 1 which gives the OLS estimated coefficients (t-ratios) and equation 2 which gives the standardized coefficients (without an intercept) for property freedom (PF), movement freedom (MF), association freedom (AF), and information freedom (IF), with respect to economic freedom (EF).

$$EF = .1384 PF + .2958 MF + .2839 AF + .2369 IF + .1340. CR^2 = .91 \quad (1)$$

(2.68) (5.81) (5.50) (5.04) (1.55)

$$EF = .1216 PF + .3020 MF + .3221 AF + .2862 IF \quad (2)$$

While the estimated regression coefficients for movement, association, and information are not significantly different from one-quarter each, the regression coefficient for property is significantly lower at about one-eighth.¹⁶ So the relative weights are not equal and appear perversely inverse. That is, freedom of property is weighted lowest rather than highest. Finally, the weighted average of the four freedoms was not consistently rounded toward an integer, as evidenced by a scatter plot of predicted versus actual values.

A major qualification here is that the correlation matrix revealed very high simple correlations between the four freedoms (highest between information and association, next highest between property and movement), suggesting that these indices as constructed may be capturing the same phenomena. As a result, their regression coefficients may not accurately reflect the actual weighting scheme used to construct the overall economic freedom rating.

Another important qualification is that all of Lindsay Wright's ratings were originally listed in five qualitative, rather than numerical, categories, and were definitely ordinal. Treating their assigned numerical rankings as linearly additive may be going well beyond what her qualitative technique would support.¹⁷ Further, the data Lindsay Wright supplied to us were reconstructed from her worksheets and may not have been exactly the same as that used to construct her published economic freedom rating. All of these qualifications also apply to what follows.

Ideal Wright Weights

Drawing on the ideas presented in our first section, one way to answer the question of what weights should be used would be to ask whether individual economic freedoms serve any measurable economic function. Presumably, with such freedoms individuals are better off economically than without them—the same might apply to a country as measured by its GNP or rate of growth of GNP. If one freedom is more important in determining economic well-being than another, it should be given a higher weight. This idea sent us off on a regression tour of a number of specification locales.

The most interesting results found so far involve using the log of private sector income as the dependent variable in a linear specification with the various freedoms as independent variables. For example, equations 3 and 4 below provide for an interesting comparison.

$$Y = -.63 \text{ PF} + .26 \text{ AF} - .52 \text{ MF} + .20 \text{ IF} - .52 \text{ CL} + 2.9 \text{ CR}^2 = .55 \quad (3)$$

(3.2) (1.2) (2.7) (1.1) (4.0) (8.8) n = 145

$$Y = -.63 \text{ PF} + .36 \text{ AF} - .48 \text{ MF} - .46 \text{ CL} + 2.9 \text{ CR}^2 = .55 \quad (4)$$

(3.3) (2.0) (2.5) (3.9) (8.9)n = 145

Here, Y equals the log of private sector income as previously defined, CL is Gastil and Wright's (1988) measure for civil liberties, and the other variables are as previously defined. Compared with specifications without it, CL just improves the performance of AF and IF, while leaving that of PF unaffected. Since the independent variables are integer values ranging from high = 1 to low = 5 while Y is a continuous variable which increases as private sector income increases, a negative sign in equation 3 or 4 indicates a direct relationship between the extent of a freedom and private sector income.

Judging from equation 3, our earlier intuition about the required relative weights of Wright's separate economic freedoms seems to be appropriate. Property freedom appears to have the highest direct effect, while association freedom is actually perverse when all or some of the other freedoms are included in the specification.¹⁸ Equation 4 shows that dropping IF makes this perverse relationship significant. These results could be used to construct a new overall economic freedom measure from the separate freedoms by using the respective regression coefficients as relative weights. However, at this stage we do not feel confident enough with these results to undertake such a construction. We merely offer them as a suggestive exercise.

Other Economic Freedom Ratings

Setting the Wright ratings right may only require a reweighting—as suggested above—rather than a reconstruction. However, we have also investigated constructing new specific measures of economic freedom. One of these is a measure for freedom from involuntary military service, which we will discuss in the next subsection. Following that, we will discuss our measure of freedom of international trade and investment.¹⁹

Freedom from Involuntary Military Service

Perhaps the most fundamental property right anyone can have is the property right to oneself. “Life” and “liberty” have often been cited, and even enshrined in constitutions, as aspects of that right. However, in more technical terms this right must surely include freedom to decide on one’s allocation of time and the rights to the benefits that flow from such decisions. Most taxation by government distorts individuals’ allocation of time, reduces individuals’ net benefit flow, and hence, modifies—indeed, partially confiscates²⁰—individuals’ rights to themselves. Relative to general taxation, specific taxation is the most distorted, benefit reducing (in the absence of offsetting distortions), and confiscatory—especially when it is taxation-in-kind which is specifically on the individual’s own time and which causes hardship, as is the case with military conscription.

Military conscription is not only allocation-distorting and benefit-reducing for the actual individuals conscripted but also for individuals who are only subject to the possibility of conscription or its consequences. Indeed, the full social and economic costs of this particular infringement of such a fundamental economic freedom are difficult to measure.²¹ All we can say here is that they are likely to vary directly with the likelihood and extent of obligation, with the likelihood and extent of hostilities, and with the difference between average military and non-military pay. The latter provides a partial, economic measure of the extent of the confiscation.

From *The Statesman’s Yearbook, 1985-86*, we were able to obtain data that we used to rank countries according to the first two criteria listed above, namely, the extent of obligation in number of years and the likelihood of obligation. “Extent” was specifically taken as the required length of service in years for army privates.²² “Likelihood” was taken as the number of the conscripts divided by the size of the country’s population.²³ We first calculated a score for each country with conscription by multiplying the numbers for extent of obligation by the ratio for the likelihood of obligation. For the 54 countries with military conscription, we obtained values ranging from close to zero to 0.2056, and in table 1 we have arranged these countries in descending order as their numerical scores increase. In most cases, the differences between scores of adjacent countries are

rather small, but there are a few relatively large gaps. We have used most of the larger gaps as convenient break points for categorization into distinct ratings.

We have chosen to rate freedom from involuntary military service from rating 1, the highest rating, to rating 5, the lowest rating. Rating 1 is reserved for those countries that have no conscription and a volunteer army (that is, an army raised on the basis of voluntary exchange). Individuals in such countries are free to either join or not join the military.

There are also a few countries without a military.²⁴ These are placed first in table 1. One might argue that such countries should receive the top rating of rating 1 (or higher) since their citizens are free from involuntary military service in their countries. However, they are not free to enter military service in their own countries and they may be subject to military service in other countries. Casual inspection reveals that several of the countries listed here (Lesotho, San Marino, and Vatican City)²⁵ are contained within countries (South Africa and Italy) that have conscription which might apply to citizens of those contained countries when they work outside their own small labour markets. Other countries listed here are island nations without prospect of military threat and possibly under protectorate arrangements (for example, Montserrat is a British protectorate). On balance, the countries on this list should be placed in rating 1 or in the ratings of the countries with which they have military ties if such ties call for military service by their citizens.

As it stands, the rating in table 1 is subject to a number of general and specific qualifications. Perhaps the most important general qualification is that this rating does not take explicit account of the method of conscription. While most countries would probably exempt the physically or mentally disabled from conscription, some countries may have relatively sophisticated selective service systems that may be designed to minimize economic distortion and economic burdens. It might be argued that countries with such systems should have a higher rating.²⁶ Life cycle considerations might suggest adjustments for different lengths of working lives, different prime age to total population ratios, different service patterns (active versus reserve obligations), and different discount rates between countries. As mentioned above, the difference between military and non-military pay should affect the rating as well as the likelihood and extent of hostilities.

With regard to the latter, we should point out some specific qualifications. Iran, for example, is currently engaged in a rather savage war with Iraq and, given the greater possibility of death or severe injury, the *expected* length of service in both countries is probably a good deal shorter than the legal obligation, while the expected costs of service are a good deal higher than foregone earnings for that period. Iran's higher rating here is due in part to its larger population. However, due to hostilities, both countries should probably be in the lowest rating.

Table 1
Freedom from Involuntary Military Service

Rating 1 (a): Nations with No Military Score = 0

Costa Rica, Iceland, Lesotho, Liechtenstein, Monaco, Montserrat, Nauru, San Marino, Solomon Islands, Turks Caicos, Vanuatu, Vatican City.

Rating 1 (b): Nations with No Conscription Score = 0

Australia, Bahrain, Bangladesh, Bhutan, Botswana, Brunei, Burkina Faso, Burma, Burundi, Canada, Cape Verde, Chad, Comoros, Congo, Cyprus, Djibouti, Dominican Republic, Equatorial Guinea, Fiji, Finland, Gabon, Federal Republic of Germany, Guatemala, Guinea, Guyana, Haiti, India, Ireland, Ivory Coast, Jamaica, Japan, Jordan, Kenya, Korea, Kuwait, Laos, Lebanon, Liberia, Libya, Luxembourg, Madagascar, Malawi, Malaysia, Mauritania, Mauritius, Mexico, Morocco, Mozambique, Nepal, New Zealand, Nicaragua, Niger, Nigeria, Oman, Pakistan, Panama, Papua New Guinea, Philippines, Qatar, Rivanja, Sao Tome, Saudi Arabia, Senegal, Seychelles, Sierra Leone, Somalia, Sri Lanka, Sudan, Swaziland, Syria, Tanzania, Togo, Trinidad, Tuvalu, United Arab Emirates, United Kingdom, United States, Uruguay, Yemen Western Samoa, Zaire, Zambia, Zimbabwe.

Rating 2: Nations with Conscription

| | Score | | Score | | Score |
|--------------------------|-------|----------|-------|-----------|-------|
| China | .0009 | Colombia | .0025 | Brazil | .0032 |
| Benin | .0012 | Algeria | .0026 | Tunisia | .0033 |
| Indonesia | .0013 | Honduras | .0028 | Denmark | .0033 |
| Central African Republic | .0016 | Austria | .0030 | Italy | .0033 |
| U.S.S.R. | .0019 | Bolivia | .0032 | Venezuela | .0035 |

Rating 3: Nations with Conscription

| | Score | | Score |
|----------|--------------|--------------|--------------|
| Portugal | .0043 | Argentina | .0057 |
| Iran | .0046 | Belgium | .0060 |
| Paraguay | .0052 | Chile | .0064 |
| Peru | .0056 | Thailand | .0064 |
| France | .0056 | East Germany | .0064 |
| Rumania | .0056 | Ecuador | .0065 |
| | | Spain | .0066 |
| | | Sweden | .0067 |
| | | Hungary | .0070 |
| | | Yugoslavia | .0077 |

Rating 4: Nations with Conscription

| | Score | | Score |
|----------------|--------------|--------------|--------------|
| Poland | .0087 | Surinam | .0135 |
| Norway | .0089 | Albania | .0145 |
| Afghanistan | .0095 | Turkey | .0146 |
| Netherlands | .0101 | El Salvador | .0147 |
| Angola | .0113 | Bulgaria | .0164 |
| Egypt | .0117 | Greece | .0187 |
| Czechoslovakia | .0130 | Ethiopia | .0188 |
| | | Singapore | .0240 |
| | | Cuba | .0269 |
| | | Taiwan | .0351 |
| | | Mongolia | .0363 |
| | | South Africa | .0369 |

Rating 5: Nations with Conscription

| | Score | | Score |
|--------|--------------|-------------|--------------|
| Iraq | .0857 | Switzerland | .1095 |
| Israel | .1003 | Vietnam | .1350 |
| | | North Korea | .2056 |

Source: Constructed by L. Still from data in *The Statesman's Yearbook, 1985-86*.

The same might hold for other countries with substantial external hostilities (for example, the U.S.S.R.) or even substantial internal hostilities (for example, Angola). Perhaps an adjustment by the relative military to non-military death and disability rates could be made if such data were available. Some countries, such as France, cannot send conscripts to foreign countries (except Germany) or into battle unless officially at war. For such countries the official status of the hostilities would be important for their rating.

Another specific qualification must be made for Switzerland. The only data available for it apply to full mobilization. Since it is a neutral country and not part of any alliance such as NATO, full mobilization may be unlikely. Also, those who are exempted from military service for whatever reason must pay an equivalent tax. This may reduce the overall burden and distortion of conscription to some extent. Thus, a higher rating may be more appropriate.

The high rating for China is rather curious. The formally conscripted army of a few million is minuscule compared to its one billion population. However, in a sense much of China's working population might be considered "conscripted," at least until recently. Even now the labour market is far from free for most Chinese workers. Consequently, if we stated our measure as "freedom from conscripted service," China would be in the lowest rating.

The low ratings of Israel, Vietnam, and North Korea are primarily due to high military requirements relative to population. In addition, North Korea has a rather long service requirement (five years).

Despite these qualifications, table 1 does provide an interesting starting point for judging countries with respect to this particular economic freedom. Since this is an essential economic freedom that is too often abused by many countries—either on a continuous or a crisis basis—it is important to have a measure that tracks it over time and across countries. Such a measure could prove crucial for those who wish to defend this particular freedom.

Freedom of International Trade and Investment

Economic freedom cannot be complete if it stops at the border. Any government restrictions, regulations, or taxes that differ according to the nationality of the trader, goods, or services involved in any domestic exchange represent a partial or total confiscation of citizens' fundamental economic right to trade. This is not usually apparent. In fact, citizens are usually led by their government or special interest groups to think quite the opposite—that foreigners are the ones whose rights are reduced or eliminated. However, this is just another case of fiscal illusion.

Government discrimination on the basis of "foreign status" imposes costs that are eventually shifted onto domestic consumers, entrepreneurs, and factor suppliers. The smaller the economy relative to the world economy, the more complete this shifting of costs. Since such costs may often be in the form of fore-

gone opportunities, they may not be explicitly measured or observed. Further, these costs are not paid to or collected by anyone but are simply lost. That is, the game is negative sum—not constant sum with a redistribution of rights, income, and wealth for the same total. In this case, confiscating the economic freedom of some confiscates the economic freedom of all.

All this, of course, is simply an application of incidence theory from traditional public finance and is well known. Alternatively, we could draw on the case for free trade which is also well known and well supported by most economists—at least in the abstract. The difference here, and also in the last chapter, is the emphasis on foreign trade impediments lowering the value and extent of economic rights and freedoms. This is not only the case for a nation's explicit impediments based on foreign status but also for impediments based on national status when these differ substantially from those imposed elsewhere.²⁷ That is, complete freedom requires foreign status and national status to be the same internally and externally.

With this in mind we have constructed a set of criteria in list 1 which would: a) pertain to the cost of foreign status relative to national status for economic activity within a nation; b) pertain to the cost of a nation's national status relative to national status elsewhere for economic activity within that nation; and c) be suitable for reasonably objective evaluations based on consistent information for a wide array of countries. Some of the criteria are the same as or similar to those mentioned by Rabushka in the previous chapter, such as criteria C, D, L, Q, S, and T in list 1.

We first attempted to evaluate these criteria on the basis of information from the latest issues of "Foreign Economic Trends," which is a series of pamphlets published by the U.S. Commerce Department for each country with a U.S. Embassy. Since an objective of this publication is to encourage U.S. business in nations favoured by U.S. administrations, it might show bias toward different countries at different times.²⁸

For those countries without a U.S. Embassy and, hence, without a "Foreign Economic Trends" issue, we referred to the latest issues of "ABECOR," which is an information sheet published by a group of European banks and distributed by Barclays Bank. The information presented there was more limited than in "Foreign Economic Trends," therefore we could rate fewer criteria for such countries.

For some countries, such as Cambodia and Nicaragua, there were no specialized sources of information and consequently no criteria were rated for them. However, from what one can gather from the popular media, most criteria for these countries should be given the lowest rating.

Generally, on the basis of the above sources, we were only able to rate a few of the 21 criteria. Canada and the U.S., with 12 and 11 criteria rated respectively, represented the upper limit of the number of criteria rated. Usually we were only able to rate three to five criteria. Hence, our initial results were quite limited by the range of criteria actually rated.

Recently we found that the *Exporters' Encyclopedia*, published by Dun and Bradstreet,²⁹ provided more extensive information on a number of previously unrated criteria for more countries. It was particularly useful for rating criteria related to infrastructure, exchange controls, and import licensing. Use of this source allowed us to substantially expand the number of rated criteria, at least doubling it for many countries. It did not allow us to substantially expand the maximum number rated (Canada is still tops at thirteen) or the number rated for those countries that already had a higher number rated. In general, the use of this source has resulted in fewer extreme ratings (i.e., fewer ones and fives) and higher ratings for socialist countries than in our first rating attempt.

Our latest results are presented in table 2. Countries are listed in rows and criteria from list 1 are listed in columns. The row-column intersection gives a country's rating with respect to that particular criterion. Intersections with dashes have not yet been rated. The number of criteria rated = #, a simple average of criteria rated = AVR, and the trade freedom rating = TF (AVR rounded to the nearest integer) for each nation are presented at the end of its row.

Casual inspection of list 1 might suggest that all criteria are not created equal—some are obviously more important than others. However, implications of each for the costs of foreign economic interaction are less obvious. We have made no attempt to apply differential weights in obtaining our overall TF rating, except implicitly in that criteria not rated are weighted by zero. Some of the latter may well be more important than those actually rated. Some countries are still rated on one or two criteria, so it would be best not to take their overall rating too seriously. For example, is Bulgaria with a TF rating of 4 based on a rating of three criteria really freer than Czechoslovakia which has a TF rating of 5 based on a rating of three criteria? Probably not!

However, in general the TF ratings seem to more or less comply with what one might expect based on more general information.³⁰ Small countries that Rabushka specifically mentioned as having relatively free trade, such as Liechtenstein and Cayman Islands, have TFs of 1, as does Singapore. Switzerland has a higher rating with 1 than Sweden with 3. The U.S. and Canada come out about the same on TF at 2, although on the basis of AVR Canada rates a bit lower. Both suffer in these ratings from their tax systems (criteria H).

List 1
Criteria for Rating Freedom of International Trade and Investment

A. PRIVATIZATION

1. No parastatals or nearly complete privatization.
2. Government committed to privatization; programme in progress.
3. Government ambivalent; programme not yet extensive.
4. Many parastatals, some joint ventures, no privatization.
5. Extensive parastatals which dominate economy.

B. PUBLIC SECTOR INVOLVEMENT

1. Government uninvolved in private sector.
2. Government provides a few subsidies and supports to private sector.
3. Many subsidies and price supports.
4. Extensive subsidies, supports, and parastatals.
5. Virtually no private sector.

C. PROFIT REPATRIATION

1. Guaranteed.
2. Guaranteed but needs government review.
3. Allowed but needs permission.
4. Possible but can be denied.
5. Not possible.

D. IMPORT RESTRICTIONS

1. No import restrictions.
2. Delays in customs; few import restrictions.
3. Import restrictions or several items banned.
4. Extensive bans or quotas on imports.
5. Close to a closed economy.

E. FOREIGN OWNERSHIP

1. 100 percent guaranteed; no expropriation in the past.
2. Some minor restrictions on ownership.
3. Limit ownership in certain sectors.
4. Limit equity to less than 50 percent.
5. No foreign ownership.

F. INFRASTRUCTURE

1. Modern telecommunications, postal, and transportation facilities.
2. Limited modern facilities but reasonably efficient.
3. Roadways run down; telephone and postal system inefficient.
4. Roadways, telephone and postal systems poorly developed.
5. Systems collapsed or non-existent.

List 1 (continued)

G. LICENSING

1. No licensing for business or imports.
2. A formality which does not take much time.
3. Some bureaucratic approval in which the license can be denied.
4. Many restrictions on licenses or heavily controlled by government.
5. No licensing possible.

H. TAXES

1. Negligible tax system; a tax haven.
2. No progressive taxes; limited taxation.
3. A progressive income tax system.
4. A complicated, progressive income tax system.
5. A complicated, progressive income tax system; extensive hidden taxes.

I. BANKING

1. An international banking centre; few regulations for banks.
2. Some limits on foreign banks and deposit protection laws.
3. Barriers to entry, restrictions on letters of credit.
4. Banks tightly controlled by the government or corrupt.
5. Banking system in total chaos.

J. MILITARY CONFLICT

1. Neutral.
2. Alliances and/or peacekeeping forces.
3. Threats of a coup, under martial law.
4. Frequent internal or external fighting.
5. Currently in a state of war.

K. GOVERNMENT STABILITY

1. A stable political system; foreigners have same legal rights.
2. Frequent police actions necessary to enforce government policy.
3. Frequent changes in government policy. Unpredictable judiciary.
4. Government unable to enforce laws. Flourishing black markets.
5. Political system in chaos.

L. TARIFFS AND NON-TARIFF BARRIERS

1. A free open economy.
2. Tariffs typically below 10 percent.
3. Tariffs between 10 and 20 percent; non-tariff barriers mentioned.
4. Tariffs above 20 percent; strong influence of non-tariff barriers.
5. Government uses tariffs and non-tariff barriers to totally discourage imports.

List 1 (continued)

M. FOREIGN INVESTMENT INCENTIVES

1. Generous tax holidays and grants to investors.
2. Some tax advantages.
3. Government only encourages foreign investment.
4. No investment code; must go on a case by case basis.
5. Government distrusts foreign investment and prefers local investment.

N. BUREAUCRACY

1. No restraints; streamlined.
2. Complaints of red tape or slow-moving processes.
3. Cumbersome.
4. Delays of up to a year.
5. Completely unresponsive.

O. PAYMENTS

1. No problems with payments.
2. Only administrative delays.
3. Slow but sure; eventual payment.
4. Serious problems; very slow and unsure.
5. Cannot get payments.

P. LABOUR RELATIONS

1. Good and reliable workforce.
2. Strikes occur occasionally.
3. Frequent strikes.
4. Inability to discipline workforce.
5. Workers hold employers hostage.

Q. RESIDENTS ALLOWED TO INVEST ABROAD

1. Residents can invest abroad without penalty.
2. Residents pay a significant tax when investing abroad.
3. Some controls are placed on investing abroad.
4. Investing abroad is restricted.
5. Residents cannot invest abroad.

R. DEREGULATION

1. No regulations.
2. Across the board deregulation of industries.
3. Deregulation of key sectors such as banking.
4. Deregulation of less significant sectors such as airlines.
5. Heavily regulated regime.

List 1 (continued)

S. PRICE CONTROLS

1. No price controls or marketing boards.
2. Some marketing boards.
3. Price controls on some items.
4. Price controls on all or most commodities.
5. Price controls with suppressed inflation.

T. EXCHANGE CONTROLS

1. Own currency floating at market determined rates.
2. Own currency rate fixed to key currency or uses key currency.
3. Frequent intervention in exchange rates by government.
4. Imposes exchange controls; limits foreign exchange.
5. Inconvertible currency.

U. LOCAL REPRESENTATIVE

1. No restriction.
2. National status for foreign representative.
3. Licensing of representative.
4. Local representative required.

Source: Classification devised by L. Still on the basis of types of information available in "Foreign Economic Trends" and "ABECOR."

Table 2
Rating Freedom of Trade and Investment

CODES: A-U from criteria in list 1 (integer rating: 1-5); # = number of criteria; AVR = average of criteria ratings; TF = freedom of trade rating (AVR rounded to the nearest integer—not available for all countries).

| NATION | A | B | C | D | E | F | G | H | I | J | K | L | M | N | O | P | Q | R | S | T | U | # | AVR | TF |
|-------------|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|------|----|
| Afghanistan | — | — | — | 3 | — | 5 | 4 | — | 4 | 5 | — | 4 | — | — | — | — | — | — | — | 4 | — | 7 | 4.14 | 4 |
| Albania | — | 5 | — | 5 | — | — | 5 | — | — | — | — | — | — | — | 1 | — | — | — | — | 5 | — | 5 | 4.20 | 4 |
| Algeria | — | — | — | 4 | 4 | 4 | 4 | — | — | — | — | — | 2 | 4 | — | — | — | — | — | 4 | — | 7 | 3.71 | 4 |
| Angola | — | — | — | 3 | — | 5 | 3 | — | 4 | — | — | — | 3 | — | 3 | — | — | — | — | — | — | 6 | 3.33 | 3 |
| Argentina | — | — | 4 | — | — | 2 | — | 3 | — | — | — | 3 | 3 | 2 | — | 1 | — | — | 4 | — | 4 | 9 | 2.88 | 3 |
| Australia | — | 2 | — | — | — | 1 | 2 | — | — | — | — | 2 | — | 1 | — | — | 2 | 2 | — | 1 | — | 8 | 1.62 | 2 |
| Austria | — | — | — | — | — | — | — | — | — | — | — | — | 2 | — | — | — | — | — | 2 | 1 | — | 5 | 1.60 | 2 |
| Bahamas | — | — | 2 | — | 2 | — | — | 1 | — | — | — | — | 2 | 2 | — | — | — | — | — | 2 | 4 | 7 | 2.14 | 2 |
| Bahrain | — | 3 | 1 | — | 4 | 1 | — | 2 | — | — | 1 | — | — | 2 | 1 | — | — | — | — | — | — | 8 | 1.87 | 2 |
| Bangladesh | — | — | — | — | — | 3 | 3 | — | — | — | — | 4 | 3 | 3 | 2 | — | — | — | — | — | — | 7 | 3.14 | 3 |
| Barbados | — | 2 | — | — | — | — | — | 2 | — | — | — | — | 1 | — | — | 1 | — | — | 4 | 3 | — | 6 | 2.16 | 2 |
| Belgium | — | 3 | — | — | — | 1 | 2 | 2 | — | — | — | 1 | 1 | — | — | — | 2 | — | — | — | — | 7 | 1.71 | 2 |
| Belize | — | — | 1 | 2 | — | 2 | — | — | — | — | — | 3 | 1 | — | 2 | — | — | — | — | 3 | — | 7 | 2.00 | 2 |
| Benin | 1 | — | — | — | — | — | 2 | — | 4 | — | — | — | — | — | — | — | — | — | — | 4 | — | 5 | 2.20 | 2 |
| Bolivia | — | — | — | — | — | 2 | — | — | — | — | — | 1 | — | — | — | — | 2 | — | — | — | — | 4 | 2.50 | 3 |
| Botswana | — | — | — | — | — | — | — | — | — | — | — | 2 | — | — | — | — | — | — | — | — | — | 1 | 2.00 | 2 |
| Brazil | — | — | — | 4 | — | — | 4 | 3 | — | — | — | — | — | — | — | 3 | — | — | — | — | — | 4 | 3.50 | 4 |

| NATION | A | B | C | D | E | F | G | H | I | J | K | L | M | N | O | P | Q | R | S | T | U | # | AVR | TF |
|--------------------|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|----|------|----|
| Brunei | — | 2 | — | — | 5 | — | — | — | — | — | — | — | 5 | — | 1 | — | — | — | — | — | — | 4 | 3.25 | 3 |
| Bulgaria | 4 | 5 | — | — | — | — | — | — | — | — | — | 4 | — | — | — | — | — | — | — | — | — | 3 | 4.30 | 4 |
| Burkina Faso | — | — | — | — | 2 | — | — | — | 3 | 4 | — | — | 1 | — | — | 2 | — | — | 2 | — | 4 | 7 | 2.57 | 3 |
| Burma | — | — | — | — | — | 3 | 4 | — | — | — | — | — | — | — | — | — | — | 4 | — | — | — | 3 | 3.66 | 4 |
| Burundi | — | 3 | — | 3 | — | — | — | — | — | — | — | — | 3 | — | — | — | — | — | — | — | — | 3 | 3.00 | 3 |
| Cameroon | — | 3 | — | — | — | 2 | — | — | — | — | — | — | — | — | — | — | — | 2 | — | 4 | — | 4 | 2.75 | 3 |
| Canada | — | 3 | 1 | — | 2 | 1 | 2 | 5 | 2 | — | 1 | 3 | 3 | — | — | 2 | 2 | — | — | 1 | — | 13 | 2.15 | 2 |
| Cape Verde | — | — | — | 3 | — | 3 | — | — | — | — | — | — | 4 | — | — | — | — | — | — | 4 | — | 4 | 3.50 | 4 |
| Cayman Islands | — | 1 | — | — | — | — | — | 2 | 1 | — | 1 | — | — | — | — | — | — | — | — | — | — | 4 | 1.25 | 1 |
| Central African R. | — | 1 | — | 4 | — | 3 | 2 | — | — | — | — | 4 | — | — | — | — | — | — | — | 4 | — | 6 | 3.00 | 3 |
| Chad | — | — | — | — | — | 5 | 2 | — | — | 3 | 4 | 3 | 1 | — | — | — | — | — | — | 4 | — | 7 | 3.14 | 3 |
| Chile | 1 | 1 | — | — | — | — | — | — | — | 3 | 2 | 3 | 3 | — | 3 | — | — | — | — | — | — | 7 | 2.28 | 2 |
| China, Peoples R. | — | — | — | — | — | 3 | 3 | 4 | — | 4 | — | — | — | 3 | — | 3 | — | — | 4 | 4 | — | 8 | 3.37 | 3 |
| Colombia | — | 2 | — | 3 | — | — | — | — | — | 4 | — | — | — | 3 | — | — | — | — | — | — | — | 6 | 3.16 | 3 |
| Congo | — | 3 | — | — | — | 4 | 3 | — | — | — | — | — | 3 | — | — | — | — | — | — | 4 | — | 5 | 3.40 | 3 |
| Costa Rica | — | — | 1 | 1 | 1 | 1 | 1 | — | — | — | — | — | — | — | — | 1 | — | — | — | — | — | 6 | 1.00 | 1 |
| Cuba | — | 5 | — | — | — | — | — | — | — | — | — | — | — | — | 4 | — | — | 5 | — | 5 | — | 4 | 4.75 | 5 |
| Cyprus | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — |
| Czechoslovakia | — | 5 | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | 5 | 5 | — | — | 3 | 5.00 | 5 |
| Denmark | — | 2 | — | — | — | 1 | 2 | 2 | — | — | — | 3 | — | — | — | — | 1 | — | 3 | 1 | — | 8 | 1.87 | 2 |
| Dominica | — | — | — | — | — | 3 | — | — | — | — | — | — | 2 | — | — | — | — | — | — | — | — | 2 | 2.50 | 3 |
| Dominican R. | 4 | 4 | 4 | — | 4 | — | — | — | — | — | — | 1 | 1 | — | 3 | — | — | — | — | 3 | — | 8 | 3.00 | 3 |

| NATION | A | B | C | D | E | F | G | H | I | J | K | L | M | N | O | P | Q | R | S | T | U | # | AVR | TF |
|------------------|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|----|------|----|
| Ecuador | — | — | — | 3 | — | — | 4 | — | — | — | 3 | 3 | — | — | — | — | — | — | — | 4 | — | 5 | 3.40 | 3 |
| Egypt | — | 4 | 3 | — | — | 2 | — | — | — | — | — | 3 | 2 | 4 | 2 | — | — | 5 | 4 | 4 | — | 10 | 3.30 | 3 |
| El Salvador | — | — | — | — | — | — | — | — | 4 | — | — | — | 1 | — | — | — | — | 3 | 4 | — | — | 4 | 3.00 | 3 |
| Ethiopia | — | 4 | — | — | — | 5 | 4 | — | 4 | 4 | — | 5 | — | — | 1 | — | — | — | 4 | — | — | 8 | 3.87 | 4 |
| Fiji | — | — | — | — | — | — | 2 | — | — | — | — | — | 1 | — | 1 | — | — | — | 2 | — | — | 3 | 1.50 | 2 |
| Finland | — | 3 | — | — | — | 1 | 2 | 3 | — | — | — | 4 | — | — | — | — | — | — | 3 | — | — | 6 | 2.66 | 3 |
| France | — | — | — | — | — | 1 | — | — | — | — | — | 3 | 2 | 1 | 1 | — | — | — | 1 | 1 | 4 | 8 | 1.75 | 2 |
| Gabon | — | — | — | — | — | — | 2 | — | — | — | — | 3 | 1 | — | — | — | — | — | 2 | — | — | 2 | 2.00 | 2 |
| Gambia | — | — | — | — | — | 2 | — | — | — | — | — | 3 | — | — | 4 | — | — | — | 1 | — | — | 5 | 2.40 | 2 |
| Germany, Fed. R. | — | 2 | — | — | — | 1 | 2 | — | — | — | — | 3 | — | — | — | — | — | — | 2 | 1 | — | 6 | 1.83 | 2 |
| Germany, D.D.R. | — | 5 | — | — | — | — | — | — | 4 | — | — | 4 | — | — | — | — | — | 5 | — | — | — | 4 | 4.50 | 5 |
| Great Britain | 1 | 1 | — | — | — | 1 | 2 | — | — | — | 2 | — | — | — | — | — | — | — | 1 | — | — | 5 | 1.33 | 1 |
| Greece | — | — | 4 | — | — | 2 | 2 | — | — | — | — | — | — | — | — | 4 | 4 | — | 5 | 4 | — | 7 | 3.57 | 4 |
| Grenada | 1 | 2 | — | — | — | — | — | 2 | — | — | — | — | — | — | — | — | — | — | — | — | — | 3 | 1.66 | 2 |
| Guatemala | — | 1 | — | — | — | 2 | — | 2 | — | — | — | — | 1 | — | — | — | — | — | 1 | 4 | — | 6 | 1.66 | 2 |
| Guinea | 1 | — | — | — | — | 2 | 2 | — | — | — | — | 1 | 3 | — | — | — | — | 3 | — | — | — | 6 | 2.00 | 2 |
| Guyana | — | — | — | 4 | — | 4 | — | — | — | — | 4 | — | 3 | — | — | — | — | — | — | — | — | 4 | 3.75 | 4 |
| Haiti | — | — | — | — | — | 4 | 4 | — | 4 | — | — | 4 | 1 | 5 | 3 | 1 | — | — | — | — | 4 | 9 | 3.33 | 3 |
| Hong Kong | — | 1 | — | 1 | — | 1 | 2 | — | — | — | — | 1 | 1 | — | — | — | — | — | — | — | — | 7 | 1.14 | 1 |
| Honduras | — | 4 | — | — | — | 3 | — | — | — | — | 4 | 3 | 4 | 4 | — | — | — | — | — | 4 | — | 7 | 3.71 | 4 |
| Hungary | 4 | — | — | — | 4 | 2 | 4 | — | 3 | — | — | 4 | 2 | — | — | — | — | — | — | — | — | 7 | 3.28 | 3 |
| Iceland | — | 2 | — | — | — | 2 | 2 | — | — | — | — | 3 | — | — | — | — | — | — | 3 | 4 | 2 | 7 | 2.57 | 3 |

| NATION | A | B | C | D | E | F | G | H | I | J | K | L | M | N | O | P | Q | R | S | T | U | # | AVR | TF |
|---------------|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|------|----|
| India | 4 | 3 | 1 | — | — | 3 | 4 | — | — | 4 | — | 4 | — | 3 | — | — | — | — | — | 4 | — | 9 | 3.33 | 3 |
| Indonesia | — | 3 | — | 1 | — | — | 2 | — | — | — | — | 4 | 3 | — | — | — | — | 2 | — | 4 | — | 7 | 2.71 | 3 |
| Iran | — | 4 | — | — | — | — | — | — | 4 | 5 | 5 | — | — | — | — | 5 | — | — | — | — | — | 5 | 4.60 | 5 |
| Iraq | — | 4 | — | — | — | — | — | — | 4 | 5 | — | 4 | 5 | — | 4 | — | — | — | — | 4 | — | 7 | 4.28 | 4 |
| Ireland | — | — | — | 2 | — | — | 2 | 2 | — | — | — | 1 | 1 | — | — | — | — | — | 4 | 3 | — | 7 | 2.14 | 2 |
| Israel | — | — | — | — | — | 1 | — | 3 | — | 3 | — | 4 | 3 | — | — | — | — | — | 4 | 2 | — | 7 | 2.85 | 3 |
| Italy | — | — | — | 3 | — | 1 | — | 3 | 2 | — | 1 | 3 | — | — | — | — | — | — | 3 | 1 | — | 8 | 2.12 | 2 |
| Ivory Coast | 1 | — | 2 | — | — | — | — | — | — | — | — | 2 | 3 | — | — | — | — | — | — | 2 | 3 | 6 | 2.16 | 2 |
| Jamaica | 1 | 3 | — | — | — | 1 | 2 | — | 2 | — | — | 4 | — | — | — | — | — | 3 | — | 4 | — | 8 | 2.50 | 3 |
| Japan | — | 2 | — | 3 | — | 1 | — | — | — | — | — | 2 | — | — | — | — | — | — | 3 | 1 | — | 6 | 2.00 | 2 |
| Jordan | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — |
| Kenya | — | 4 | — | — | — | 3 | 3 | — | — | — | — | 4 | — | 4 | — | — | — | — | 2 | 4 | — | 7 | 3.42 | 3 |
| Korea | — | — | 2 | — | — | — | 2 | — | 3 | — | 2 | 4 | — | — | 3 | — | — | — | — | — | 4 | 7 | 2.42 | 2 |
| North Korea | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | 5 | — | — | — | 1 | 5.00 | 5 |
| Kuwait | — | 4 | — | 3 | — | 2 | — | — | — | 3 | — | 4 | — | — | — | — | — | — | — | 1 | 4 | 7 | 3.00 | 3 |
| Laos | — | 5 | — | — | — | 4 | — | — | — | — | — | 4 | 5 | — | — | — | — | — | — | 4 | 4 | 6 | 4.33 | 4 |
| Lebanon | — | 4 | — | — | — | 5 | — | — | — | 4 | 5 | 1 | 2 | — | — | — | — | — | — | 2 | — | 7 | 3.28 | 3 |
| Liberia | — | — | — | — | — | 2 | — | — | 3 | — | 3 | 1 | — | — | — | — | — | — | 3 | 2 | — | 6 | 2.33 | 2 |
| Libya | — | 4 | — | 3 | — | — | 4 | — | — | 3 | — | 5 | — | 4 | — | — | — | — | — | — | — | 6 | 3.83 | 4 |
| Liechtenstein | — | — | — | — | — | — | — | — | 1 | — | — | — | 1 | — | — | — | — | — | — | 2 | 1 | 4 | 1.25 | 1 |
| Luxembourg | — | 2 | 1 | — | — | 1 | 1 | — | 2 | — | — | — | 3 | 1 | — | — | — | — | — | 2 | — | 8 | 1.62 | 2 |
| Madagascar | — | 4 | — | — | — | 3 | 3 | 2 | — | — | — | 4 | — | — | — | — | — | — | — | 4 | — | 6 | 3.33 | 3 |

| NATION | A | B | C | D | E | F | G | H | I | J | K | L | M | N | O | P | Q | R | S | T | U | # | AVR | TF |
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| Malawi | 4 | 1 | 2 | — | — | 3 | 4 | — | — | — | — | 4 | 1 | — | — | — | — | — | 3 | 4 | — | 6 | 2.30 | 2 |
| Malaysia | — | — | — | — | — | 2 | — | — | — | — | — | — | — | — | — | — | — | — | — | 3 | — | 2 | 2.50 | 3 |
| Mali | 1 | 2 | — | — | — | 4 | 1 | — | — | — | — | — | 3 | — | — | — | — | — | — | 2 | — | 6 | 2.16 | 2 |
| Malta | — | 4 | — | — | — | 2 | 3 | — | — | — | 3 | 3 | 2 | — | — | — | — | — | — | 4 | — | 7 | 3.00 | 3 |
| Mauritania | — | — | — | — | — | 3 | 4 | 4 | 3 | — | — | — | 1 | — | — | — | — | 3 | — | 4 | — | 7 | 3.14 | 3 |
| Mauritius | — | 2 | — | — | — | 2 | — | 3 | — | — | 1 | 3 | — | — | — | 1 | — | — | 4 | — | — | 7 | 2.28 | 2 |
| Mexico | 2 | — | — | — | 4 | 2 | 2 | — | — | — | — | 2 | — | — | — | — | — | — | — | 4 | — | 6 | 2.66 | 3 |
| Monaco | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — |
| Mongolia | — | 4 | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | — | 1 | 4.00 | 4 |
| Morocco | 3 | — | — | 2 | — | — | — | 2 | — | — | — | 3 | — | — | — | — | — | — | 4 | 3 | 3 | 7 | 2.85 | 3 |
| Mozambique | 1 | — | 1 | — | — | 5 | — | — | — | 5 | — | 4 | 2 | — | — | — | — | — | — | 4 | — | 7 | 3.14 | 3 |
| Nepal | — | 4 | — | — | 2 | — | — | — | — | — | — | 3 | 1 | — | — | — | — | — | — | — | — | 4 | 2.50 | 3 |
| Netherlands | — | — | — | — | — | — | 1 | 2 | 3 | — | — | 3 | 3 | — | — | — | 1 | — | — | 1 | — | 7 | 2.00 | 2 |
| New Zealand | 1 | — | — | — | 3 | 2 | 3 | 2 | — | — | — | 4 | — | — | — | — | — | 2 | — | — | — | 7 | 2.42 | 2 |
| Niger | 2 | — | — | 4 | — | 3 | — | 4 | — | — | — | 4 | 2 | 3 | — | — | — | — | 2 | — | 8 | 3.00 | 3 | |
| Nigeria | 3 | — | 3 | 4 | 3 | 3 | 3 | — | — | — | — | — | 2 | — | — | — | — | — | 1 | — | 8 | 2.75 | 3 | |
| Norway | — | 4 | — | 3 | — | 2 | — | — | 4 | 2 | 1 | 3 | 3 | — | — | — | — | — | — | 3 | — | 9 | 2.77 | 3 |
| Oman | — | 2 | — | 3 | 4 | 2 | 4 | 3 | — | — | — | 2 | — | 3 | — | — | — | 3 | — | — | 4 | 10 | 3.00 | 3 |
| Pakistan | 1 | — | 1 | 3 | — | 2 | 3 | 2 | 3 | — | — | — | 3 | — | — | — | — | 2 | — | 3 | — | 10 | 2.30 | 2 |
| Panama | 2 | 2 | — | 3 | — | 2 | — | 1 | 5 | 3 | 2 | 2 | 3 | — | — | — | — | — | — | 2 | — | 11 | 2.45 | 2 |
| Papua New Guinea | — | 3 | — | 1 | — | 3 | 1 | — | — | — | 3 | 2 | 2 | — | 1 | — | — | — | — | 4 | — | 9 | 2.22 | 2 |
| Paraguay | 5 | — | — | — | — | — | — | 4 | 5 | — | 4 | — | — | — | — | — | — | — | — | 4 | — | 4 | 4.40 | 4 |

| NATION | A | B | C | D | E | F | G | H | I | J | K | L | M | N | O | P | Q | R | S | T | U | # | AVR | TF |
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| Peru | — | 4 | 5 | 4 | — | — | — | — | 4 | — | 3 | 4 | — | — | — | — | — | — | 5 | 4 | 2 | 9 | 3.88 | 4 |
| Philippines | 1 | — | 1 | 2 | — | 3 | 1 | — | — | 3 | — | 4 | 1 | — | — | 3 | — | — | — | 4 | — | 10 | 2.30 | 2 |
| Poland | 4 | 4 | — | — | 4 | — | 4 | — | — | — | — | — | — | — | — | — | — | 5 | — | 5 | — | 6 | 4.33 | 4 |
| Portugal | — | — | — | 2 | — | 1 | 2 | — | 4 | — | — | 1 | 2 | 1 | — | 1 | — | — | — | 3 | 4 | 10 | 2.10 | 2 |
| Qatar | 4 | — | — | 3 | 4 | 2 | 4 | — | — | — | 3 | — | 1 | — | 3 | 1 | — | — | — | — | — | 9 | 2.77 | 3 |
| Romania | 5 | — | — | — | — | 2 | — | — | — | — | — | — | — | — | 3 | — | — | 5 | — | 5 | — | 5 | 4.00 | 4 |
| Rwanda | 1 | — | — | — | — | 4 | — | 2 | 4 | — | — | 4 | — | — | — | — | — | 5 | 3 | — | — | 7 | 3.28 | 3 |
| Saudi Arabia | — | 1 | — | 3 | — | — | 4 | — | — | — | — | 3 | — | 5 | — | — | — | 5 | — | — | 4 | 7 | 3.57 | 4 |
| Senegal | — | — | — | — | — | 2 | 3 | — | — | — | — | — | 2 | 3 | — | 4 | — | 3 | — | 2 | 4 | 8 | 2.87 | 3 |
| Seychelles | — | 3 | — | — | — | — | 3 | — | — | — | — | — | 4 | — | — | 4 | — | — | — | 1 | — | 5 | 3.00 | 3 |
| Sierra Leone | — | 3 | 3 | 3 | — | 3 | 2 | — | — | — | — | 3 | 2 | — | — | — | — | 5 | — | 4 | — | 9 | 3.11 | 3 |
| Singapore | — | — | 1 | 1 | 1 | 1 | 2 | — | — | — | — | 3 | 1 | — | — | — | — | — | — | 1 | — | 8 | 1.37 | 1 |
| Somalia | 4 | — | 4 | 1 | — | 4 | 1 | — | 4 | — | — | — | — | — | — | — | — | — | 1 | 4 | — | 8 | 2.87 | 3 |
| South Africa | — | — | — | 5 | — | — | 4 | — | — | 3 | 2 | 3 | — | — | — | — | — | — | — | 4 | — | 6 | 3.50 | 4 |
| Soviet Union | 4 | 4 | — | 3 | — | — | — | — | — | 2 | — | — | — | 3 | — | — | — | 3 | — | 5 | — | 7 | 3.42 | 3 |
| Spain | — | — | 2 | — | — | — | 2 | — | — | — | — | — | 3 | — | — | — | 1 | — | 3 | 1 | — | 6 | 2.00 | 2 |
| Sri Lanka | — | — | — | 2 | 2 | 2 | — | — | — | — | — | 2 | 1 | — | — | — | — | — | — | — | — | 5 | 1.80 | 2 |
| St. Lucia | — | — | — | 1 | — | — | — | 2 | — | — | — | — | 1 | — | — | — | — | — | — | — | — | 3 | 1.33 | 1 |
| St. Vincent | — | — | — | 2 | — | 3 | — | 2 | — | — | — | — | 1 | — | — | — | — | — | — | — | — | 4 | 2.00 | 2 |
| Sudan | 2 | — | — | — | 3 | 3 | 4 | 3 | 4 | — | 3 | — | 2 | — | — | — | — | — | 3 | — | — | 9 | 3.00 | 3 |
| Suriname | — | 4 | — | — | — | 2 | 3 | — | — | — | — | 4 | 4 | — | 4 | 4 | — | — | — | 4 | — | 8 | 3.62 | 4 |
| Swaziland | — | — | — | — | — | — | — | — | — | — | — | 2 | 1 | — | 2 | — | — | — | — | — | — | 4 | 1.25 | 1 |

| NATION | A | B | C | D | E | F | G | H | I | J | K | L | M | N | O | P | Q | R | S | T | U | # | AVR | TF |
|----------------------|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|------|------|----|
| Sweden | — | 2 | — | 2 | — | 1 | 3 | 5 | — | — | 1 | 1 | — | — | — | — | — | — | 5 | 3 | — | 9 | 2.55 | 3 |
| Switzerland | — | — | — | — | 2 | 1 | 2 | — | 1 | 1 | 1 | 2 | 1 | — | — | 1 | — | — | — | 1 | — | 10 | 1.30 | 1 |
| Syria | — | 4 | — | — | — | — | 4 | — | — | — | 4 | — | — | 5 | — | — | — | 5 | 4 | — | 6 | 4.33 | 4 | |
| Taiwan | — | 2 | 4 | — | — | 2 | 3 | — | — | — | — | 3 | — | — | — | — | — | 3 | 3 | — | 7 | 2.85 | 3 | |
| Tanzania | — | — | 5 | — | — | 2 | — | 5 | 4 | — | 4 | — | 4 | — | — | — | — | — | 3 | 4 | — | 8 | 3.87 | 4 |
| Thailand | — | 2 | — | — | — | — | 3 | — | — | — | — | 3 | 2 | — | — | — | — | — | — | 1 | 3 | 6 | 2.33 | 2 |
| Togo | 1 | — | 2 | — | — | 3 | — | — | 1 | — | — | — | — | — | — | — | — | — | — | 2 | 4 | 4 | 1.83 | 2 |
| Trinidad | 4 | — | — | — | — | 3 | — | 4 | — | — | — | — | — | — | 4 | — | — | — | — | 4 | — | 5 | 3.80 | 4 |
| Tunisia | 4 | 4 | — | — | — | — | 3 | — | — | — | — | 3 | 2 | — | — | — | — | 3 | 3 | — | 4 | 8 | 3.25 | 3 |
| Turkey | 1 | 1 | — | 2 | — | 2 | 2 | — | — | — | — | 4 | — | 3 | — | 2 | — | — | — | — | — | 8 | 2.12 | 2 |
| Uganda | — | — | — | 3 | — | 3 | 4 | — | 1 | 4 | 4 | 3 | 1 | — | — | — | — | — | 3 | 4 | — | 10 | 2.50 | 3 |
| United Arab Emirates | — | — | — | — | 4 | 1 | 2 | 1 | 1 | — | — | 2 | — | — | — | — | — | 1 | — | — | 4 | 8 | 2.00 | 2 |
| United States | — | 2 | — | 3 | 1 | 1 | — | 4 | 2 | 2 | 1 | — | — | — | — | 2 | 1 | — | — | 1 | — | 11 | 1.81 | 2 |
| Uruguay | — | 2 | 4 | 1 | — | 2 | — | — | 3 | — | — | — | 1 | 2 | — | 3 | — | — | — | 1 | — | 9 | 2.11 | 2 |
| Vanuatu | — | — | — | 2 | — | 3 | 2 | 2 | 2 | 1 | — | — | 5 | — | — | — | — | — | 3 | 2 | — | 9 | 2.55 | 3 |
| Venezuela | — | — | — | 3 | — | 2 | 4 | — | — | — | — | 4 | — | 3 | — | — | — | 5 | 2 | 4 | — | 8 | 3.37 | 3 |
| Vietnam | — | 4 | 3 | — | 4 | — | — | — | — | — | — | — | — | — | — | — | — | 5 | — | 5 | — | 5 | 4.20 | 4 |
| Yemen Arab R. | — | 3 | 3 | 3 | 1 | — | 4 | — | — | — | 1 | — | 3 | — | — | — | — | — | 5 | 4 | — | 9 | 3.00 | 3 |
| Yugoslavia | 4 | 4 | — | — | — | — | — | — | 4 | — | — | — | — | — | 3 | 3 | — | — | 5 | 4 | — | 8 | 4.00 | 4 |
| Zaire | — | — | 1 | 2 | — | 3 | 2 | — | — | — | — | 4 | 1 | — | — | — | — | 2 | 2 | 3 | — | 9 | 2.22 | 2 |
| Zambia | 4 | 4 | — | — | — | 2 | 3 | — | — | — | 3 | — | 2 | — | — | — | — | — | 4 | 3 | — | 5 | 3.12 | 3 |
| Zimbabwe | — | — | — | — | — | 1 | 3 | — | — | — | — | 4 | 4 | — | — | — | — | — | — | 4 | — | 5 | 3.20 | 3 |

Summary and Conclusion

In table 3 we present the ratings we have constructed (PYC = private sector income per capita; DF = draft freedom; and TF = trade freedom) along with those constructed by Gastil and Wright (GNP = total GNP per capita; EF = economic freedom; PF = property freedom; AF = association freedom; MF = movement freedom; IF = information freedom; PR = political rights; CL = civil liberties; SF = system freedom; and ES = economic system) for a side by side comparison. Scanning down the rows—and bearing in mind that the first two columns are in thousands of U.S. dollars per capita (where higher numbers indicate a higher freedom rating, which is the opposite of the next eleven columns), the next seven columns use a 1-5 rating scale, the tenth and eleventh columns have a 1-7 rating scale, the twelfth column has a 1-3 rating scale, and the thirteenth column has a 1-9 rating scale—there do not seem to be large differences in the way each rating system rates each nation.

Indeed, a slightly more sophisticated means of comparison, the Spearman rank correlation matrix, shows that there is a significant correlation at a level of significance of 0.05 for almost every pair of rating scales (the two exceptions are between GNP and TF, and between DF and SF).³¹ However, this is not to say that each rating system is rating the same thing, since very few of the correlation coefficients given in table 4 are anywhere near one (indicating identity). On the other hand, Lindsay Wright's economic freedom rating (EF) does have a fairly high correlation coefficient with all other rating systems except our draft freedom (DF) and Gastil and Wright's system freedom (SF). A final exercise of interest is to see how all these freedom ratings perform in a regression with Y as a dependent variable. Again, equations 5 and 6 are representative. Excluded freedom ratings did not reach significance in any linear specification when combined with other freedoms.

$$\begin{aligned}
 Y = & .22 \text{ DF} - .25 \text{ TF} + .35 \text{ AF} - .42 \text{ PF} - .47 \text{ MF} & (5) \\
 & (1.95) (1.77) (2.08) (2.13) (2.46) \\
 & - .35 \text{ CL} - .21 \text{ ES} + 3.0 & \text{CR}^2 = .59
 \end{aligned}$$

$$\begin{aligned}
 Y = & -.31 \text{ TF} -.27 \text{ EF} -.32 \text{ CL} - .25 \text{ ES} + 3.1 & \text{CR}^2 = .55 & (6) \\
 & (2.13) (1.35) (2.70) (3.68) (8.4)
 \end{aligned}$$

A comparison of equation 5 and 6 shows that EF does not perform as well as the best combination of some of its component freedoms such as PF, MF, and AF. Our TF performs marginally well with the expected direct relationship. Our DF, however, has a perverse effect on Y, suggesting a trade-off between freedoms.

Concluding Remarks

On balance, such integer rating schemes are not appropriate for making fine distinctions on a concept as complex and crucial as economic freedom. On the other hand, the necessarily subjective and limited methods of constructing such ratings may not justify a refined, continuous measure. The crudeness of these integer ratings should serve as an implicit warning about their approximate and tenuous nature. Finer distinctions could be made with economic freedom ratings derived from existing national accounts. However, these measures are unlikely to satisfy non-economic philosophers. A more refined, periodic rating scheme that would completely satisfy and appeal to deontologists would be very time consuming and costly to construct and maintain. That is not to say it is not worth doing, as the benefits may be very large. However, it will require a large and ongoing commitment to funding.

Table 3
Summary of Ratings of Economic Freedom

LEGEND: The first column is GNP = GNP per capita in thousands of 1980 U.S. \$ (source: Wright 1982, table 9). The next column is PYC = private per capita defined as $x(1 - G/GNP)$ (source: IMF Government Financial Statistics Yearbook, 1985). The next seven columns contain integer ratings for various economic freedoms defined as follows: high = 1; medium high = 2; medium = 3; medium low = 4; low = 5. DF = draft freedom rating (source: table 1). TF = freedom of trade rating (source: table 2). EF = economic freedom rating (source: Wright 1982, table 9). PF = freedom of property ratings; AF = freedom of association rating; MF = freedom of movement ratings; and IF = freedom of information rating (source of previous ratings: Wright 1988). The last four columns have integer ratings with ranges varying as follows (1 = high or most freedom): PR = political rights rating (1-7); CL = civil liberties rating (1-7); SF = status of freedom rating (1 = free; 2 = partially free; 3 = not free); and ES = economic system rating (1 = capitalist inclusive; 2 = capitalist non-inclusive; 3 = capitalist-statist inclusive; 4 = capitalist-statist non-inclusive; 5 = mixed capitalist; 6 = mixed socialist inclusive; 7 = mixed socialist non-inclusive; 8 = socialist inclusive; 9 = socialist non-inclusive) (source of previous four ratings: Gastil and Wright 1988, appendix 1 and 2).

| NATION | GNP | PYC | DF | TF | EF | PF | AF | MF | IF | PR | CL | SF | ES |
|-------------|------|------|----|----|----|----|----|----|----|----|----|----|----|
| Afghanistan | 0.1 | — | 4 | 4 | 5 | 4 | 4 | 5 | 5 | 7 | 7 | 3 | 9 |
| Albania | 0.8 | — | 4 | 4 | 5 | 5 | 5 | 5 | 5 | 7 | 7 | 3 | 8 |
| Algeria | 1.9 | — | 2 | 4 | 2 | 4 | 5 | 3 | 4 | 6 | 6 | 3 | 8 |
| Angola | 0.4 | — | 4 | 3 | 5 | 4 | 5 | 5 | 5 | 7 | 7 | 3 | 9 |
| Argentina | 2.3 | 1.86 | 3 | 3 | 3 | 2 | 3 | 2 | 2 | 2 | 3 | 1 | 3 |
| Australia | 9.8 | 7.14 | 1 | 2 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 |
| Austria | 10.2 | 6.35 | 2 | 2 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 5 |
| Bahamas | 3.3 | 2.66 | 1 | 2 | 1 | 1 | 1 | 1 | 2 | 2 | 2 | 1 | 1 |

| NATION | GNP | PYC | DF | TF | EF | PF | AF | MF | IF | PR | CL | SF | ES |
|--------------------|------|------|----|----|----|----|----|----|----|----|----|----|----|
| Bahrain | 5.5 | 4.27 | 1 | 2 | 3 | 2 | 4 | 1 | 4 | 5 | 5 | 2 | 3 |
| Bangladesh | 0.1 | 0.09 | 1 | 3 | 3 | 4 | 3 | 3 | 3 | 5 | 5 | 2 | 4 |
| Barbados | 3.0 | 2.07 | 1 | 2 | 1 | 1 | 1 | 1 | 1 | 1 | 2 | 1 | 1 |
| Belgium | 12.1 | 6.01 | 3 | 2 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 |
| Belize | 1.0 | 0.74 | 1 | 2 | 1 | 1 | 1 | 1 | 2 | 1 | 1 | 1 | 1 |
| Benin | 0.3 | 0.23 | 2 | 2 | 4 | 4 | 4 | 4 | 5 | 7 | 7 | 3 | 9 |
| Bolivia | 0.5 | 0.43 | 2 | 3 | 3 | 3 | 4 | 2 | 3 | 2 | 3 | 1 | 4 |
| Botswana | 0.9 | 0.59 | 1 | 2 | 2 | 2 | 1 | 1 | 1 | 2 | 3 | 1 | 2 |
| Brazil | 2.0 | 1.62 | 2 | 4 | 3 | 3 | 3 | 2 | 3 | 3 | 2 | 1 | 3 |
| Brunei | — | — | 1 | 3 | — | — | — | — | — | 6 | 5 | 2 | 3 |
| Bulgaria | 3.6 | — | 4 | 4 | 5 | 5 | 5 | 5 | 5 | 7 | 7 | 3 | 8 |
| Burkina Faso | 0.1 | 0.08 | 1 | 3 | 3 | 2 | 3 | 2 | 3 | 7 | 6 | 3 | 7 |
| Burma | 0.1 | 0.08 | 1 | 4 | 4 | 3 | 4 | 4 | 5 | 7 | 7 | 3 | 7 |
| Burundi | 0.2 | 0.16 | 1 | 3 | 4 | 3 | 4 | 3 | 5 | 7 | 6 | 3 | 5 |
| Cameroon | 0.6 | 0.50 | — | 3 | 3 | 2 | 4 | 3 | 5 | 6 | 7 | 3 | 2 |
| Canada | 10.1 | 6.35 | 1 | 2 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 |
| Cape Verde | 0.3 | — | 1 | 4 | 3 | 3 | 4 | 2 | 2 | 6 | 7 | 3 | 7 |
| Cayman Islands | — | — | 1 | 1 | — | — | — | — | — | — | — | — | — |
| Central African R. | 0.3 | 0.23 | 2 | 3 | 3 | 2 | 4 | 2 | 4 | 7 | 6 | 3 | 4 |
| Chad | 0.1 | — | 1 | 3 | 4 | 3 | 4 | 4 | 5 | 7 | 7 | 3 | 2 |
| Chile | 2.1 | 1.51 | 3 | 2 | 3 | 2 | 3 | 3 | 3 | 6 | 5 | 2 | 1 |
| China, Peoples R. | 0.2 | — | 2 | 3 | 5 | 5 | 5 | 5 | 5 | 6 | 6 | 3 | 6 |

(continued on next page)

| NATION | GNP | PYC | DF | TF | EF | PF | AF | MF | IF | PR | CL | SF | ES |
|-------------|------|------|----|----|----|----|----|----|----|----|----|----|----|
| Greece | 4.5 | 2.90 | 4 | 4 | 1 | 2 | 1 | 1 | 1 | 2 | 2 | 1 | 5 |
| Grenada | 0.6 | — | 1 | 2 | 3 | 2 | 3 | 2 | 5 | 2 | 3 | 1 | 3 |
| Guatemala | 1.1 | 0.94 | 1 | 2 | 4 | 3 | 4 | 3 | 4 | 4 | 4 | 2 | 2 |
| Guinea | 0.2 | — | 1 | 2 | 4 | 4 | 4 | 3 | 5 | 7 | 5 | 3 | 7 |
| Guyana | 0.6 | 0.24 | 1 | 4 | 4 | 4 | 4 | 4 | 5 | 5 | 5 | 2 | 6 |
| Haiti | 0.2 | 0.16 | 1 | 3 | 3 | 3 | 4 | 3 | 5 | 7 | 6 | 3 | 2 |
| Hong Kong | — | — | 1 | 1 | — | — | — | — | — | — | — | — | — |
| Honduras | 0.5 | 0.40 | 2 | 4 | 2 | 2 | 2 | 1 | 1 | 2 | 3 | 1 | 2 |
| Hungary | 3.8 | — | 3 | 3 | 4 | 4 | 4 | 4 | 5 | 5 | 5 | 2 | 8 |
| Iceland | 11.3 | 8.02 | 1 | 3 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 |
| India | 0.2 | 0.17 | 1 | 3 | 3 | 3 | 2 | 3 | 4 | 2 | 3 | 1 | 4 |
| Indonesia | 0.4 | 0.31 | 2 | 3 | 3 | 3 | 3 | 3 | 4 | 5 | 6 | 2 | 4 |
| Iran | 2.3 | 1.51 | 3 | 5 | 4 | 3 | 2 | 3 | 3 | 5 | 6 | 2 | 4 |
| Iraq | 3.0 | — | 5 | 4 | 4 | 4 | 5 | 4 | 5 | 7 | 7 | 3 | 9 |
| Ireland | 4.8 | 2.54 | 1 | 2 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 |
| Israel | 4.5 | 1.95 | 5 | 3 | 2 | 2 | 1 | 2 | 1 | 2 | 2 | 1 | 5 |
| Italy | 6.4 | 3.37 | 2 | 2 | 1 | 2 | 1 | 1 | 1 | 1 | 1 | 1 | 3 |
| Ivory Coast | 1.1 | 0.76 | 1 | 2 | 3 | 2 | 3 | 1 | 4 | 6 | 5 | 2 | 2 |
| Jamaica | 1.0 | 0.59 | 1 | 3 | 2 | 2 | 1 | 1 | 2 | 2 | 3 | 1 | 3 |
| Japan | 9.8 | — | 1 | 2 | 1 | 2 | 2 | 1 | 1 | 1 | 1 | 1 | 1 |
| Jordan | 1.4 | 0.70 | 1 | — | 3 | 2 | 3 | 1 | 4 | 5 | 5 | 2 | 1 |
| Kenya | 0.4 | 0.29 | 1 | 3 | 2 | 2 | 3 | 1 | 3 | 6 | 5 | 2 | 2 |

(continued on next page)

| NATION | GNP | PYC | DF | TF | EF | PF | AF | MF | IF | PR | CL | SF | ES |
|------------------|------|------|----|----|----|----|----|----|----|----|----|----|----|
| New Zealand | 7.0 | 4.48 | 1 | 2 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 |
| Niger | 0.3 | 0.24 | 1 | 3 | 3 | 1 | 2 | 2 | 5 | 7 | 6 | 3 | 2 |
| Nigeria | 1.0 | — | 1 | 3 | 2 | 3 | 2 | 2 | 2 | 7 | 5 | 3 | 3 |
| Norway | 12.6 | 7.81 | 4 | 3 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 5 |
| Oman | 4.3 | 2.64 | 1 | 3 | 3 | 2 | 4 | 2 | 5 | 6 | 6 | 3 | 4 |
| Pakistan | 0.3 | 0.25 | 1 | 2 | 4 | 3 | 5 | 2 | 5 | 4 | 5 | 2 | 4 |
| Panama | 1.7 | 1.14 | 1 | 2 | 2 | 3 | 2 | 1 | 3 | 6 | 3 | 2 | 3 |
| Papua New Guinea | 0.7 | 0.45 | 1 | 2 | 1 | 2 | 1 | 1 | 1 | 2 | 2 | 1 | 2 |
| Paraguay | 1.3 | 1.17 | 3 | 4 | 4 | 3 | 4 | 4 | 4 | 5 | 5 | 2 | 4 |
| Peru | 0.9 | 0.71 | 3 | 4 | 2 | 3 | 1 | 2 | 2 | 2 | 3 | 1 | 4 |
| Philippines | 0.7 | 0.61 | 1 | 2 | 3 | 3 | 3 | 2 | 3 | 4 | 3 | 2 | 4 |
| Poland | 3.8 | — | 4 | 4 | 5 | 3 | 5 | 4 | 4 | 6 | 5 | 2 | 6 |
| Portugal | 2.3 | — | 3 | 2 | 2 | 3 | 1 | 1 | 2 | 1 | 2 | 1 | 5 |
| Qatar | 26.0 | — | 1 | 3 | 3 | 2 | 5 | 2 | 5 | 5 | 5 | 2 | 3 |
| Rumania | 1.9 | 1.05 | 3 | 4 | 5 | 5 | 5 | 5 | 5 | 7 | 7 | 3 | 8 |
| Rwanda | 0.2 | 0.17 | 1 | 3 | 3 | 1 | 4 | 3 | 3 | 6 | 6 | 3 | 7 |
| Saudi Arabia | 11.2 | — | 1 | 4 | 3 | 3 | 4 | 3 | 5 | 6 | 7 | 3 | 3 |
| Senegal | 0.4 | 0.30 | 1 | 3 | 2 | 3 | 2 | 1 | 2 | 3 | 4 | 2 | 5 |
| Seychelles | 1.7 | — | 1 | 3 | 4 | 3 | 4 | 3 | 5 | 6 | 6 | 3 | 6 |
| Sierra Leone | 0.2 | 0.14 | 1 | 3 | 3 | 2 | 3 | 2 | 4 | 5 | 5 | 2 | 2 |
| Singapore | 4.4 | 3.52 | 4 | 1 | 3 | 2 | 4 | 3 | 4 | 4 | 5 | 2 | 5 |
| Somalia | 0.1 | — | 1 | 3 | 4 | 4 | 4 | 5 | 5 | 7 | 7 | 2 | 7 |

(continued on next page)

| NATION | GNP | PYC | DF | TF | EF | PF | AF | MF | IF | PR | CL | SF | ES |
|----------------------|------|-------|----|----|----|----|----|----|----|----|----|----|----|
| South Africa | 2.2 | 1.73 | 4 | 4 | 4 | 5 | 5 | 5 | 5 | 5 | 6 | 2 | 3 |
| Soviet Union | 4.1 | — | 2 | 3 | 5 | 5 | 5 | 5 | 5 | 7 | 7 | 3 | 8 |
| Spain | 5.3 | 3.86 | 3 | 2 | 1 | 2 | 1 | 1 | 2 | 1 | 2 | 1 | 1 |
| Sri Lanka | 0.2 | 0.12 | 1 | 2 | 2 | 3 | 1 | 2 | 2 | 3 | 4 | 2 | 3 |
| St. Lucia | 0.8 | 0.51 | 1 | 1 | 1 | 2 | 1 | 1 | 1 | 1 | 2 | 1 | 1 |
| St. Vincent | 0.5 | 0.34 | 1 | 2 | 1 | 2 | 1 | 1 | 1 | 2 | 2 | 1 | 1 |
| Sudan | 0.4 | 0.32 | 1 | 3 | 3 | 3 | 3 | 3 | 4 | 6 | 6 | 3 | 7 |
| Suriname | 2.8 | — | 4 | 4 | 4 | 3 | 4 | 3 | 4 | 6 | 6 | 3 | 1 |
| Swaziland | 0.6 | 0.46 | 1 | 1 | 3 | 3 | 4 | 2 | 3 | 5 | 6 | 2 | 2 |
| Sweden | 13.5 | 7.79 | 3 | 3 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 5 |
| Switzerland | 16.4 | 13.07 | 5 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 |
| Syria | 1.3 | 0.68 | 1 | 4 | 4 | 4 | 4 | 3 | 5 | 6 | 7 | 2 | 6 |
| Taiwan | 2.1 | — | 4 | 3 | 3 | 2 | 4 | 2 | 4 | 5 | 5 | 2 | 3 |
| Tanzania | 0.2 | 0.14 | 1 | 4 | 4 | 4 | 5 | 3 | 5 | 6 | 6 | 3 | 9 |
| Thailand | 0.6 | 0.48 | 3 | 2 | 2 | 3 | 2 | 1 | 2 | 3 | 4 | 2 | 2 |
| Togo | 0.4 | 0.27 | 1 | 2 | 4 | 3 | 4 | 2 | 5 | 6 | 6 | 3 | 7 |
| Trinidad | 4.3 | 3.00 | 1 | 4 | 1 | 3 | 1 | 1 | 1 | 1 | 2 | 1 | 3 |
| Tunisia | 1.3 | 0.88 | 2 | 3 | 3 | 3 | 3 | 3 | 4 | 5 | 5 | 2 | 5 |
| Turkey | 1.4 | 1.06 | 4 | 2 | 3 | 3 | 4 | 3 | 4 | 3 | 5 | 2 | 3 |
| Uganda | 0.2 | 0.19 | 1 | 3 | 4 | 4 | 4 | 4 | 5 | 5 | 4 | 2 | 4 |
| United Arab Emirates | 30.0 | 26.36 | 1 | 2 | 3 | 3 | 4 | 2 | 4 | 5 | 5 | 2 | 3 |

| NATION | GNP | PYC | DF | TF | EF | PF | AF | MF | IF | PR | CL | SF | ES |
|---------------|------|------|----|----|----|----|----|----|----|----|----|----|----|
| United States | 11.3 | 8.64 | 1 | 2 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 |
| Uruguay | 2.8 | 2.19 | 1 | 2 | 4 | 3 | 4 | 3 | 4 | 2 | 2 | 1 | 5 |
| Vanuatu | 0.5 | — | 1 | 3 | 2 | 1 | 1 | 1 | 3 | 2 | 4 | 2 | 4 |
| Venezuela | 3.6 | 2.81 | 2 | 3 | 1 | 2 | 1 | 1 | 2 | 1 | 2 | 1 | 3 |
| Vietnam | 0.1 | — | 5 | 4 | 5 | 5 | 5 | 5 | 5 | 7 | 7 | 3 | 8 |
| Yemen Arab R. | 0.4 | 0.25 | 1 | 3 | 3 | 3 | 4 | 3 | 4 | 5 | 5 | 2 | 2 |
| Yugoslavia | 2.6 | 2.34 | 3 | 4 | 3 | 3 | 3 | 3 | 4 | 6 | 5 | 2 | 6 |
| Zaire | 0.2 | 0.14 | 1 | 2 | 4 | 3 | 4 | 3 | 4 | 7 | 7 | 3 | 4 |
| Zambia | 0.5 | 0.31 | 1 | 3 | 3 | 3 | 4 | 2 | 4 | 5 | 5 | 2 | 7 |
| Zimbabwe | 0.6 | 0.39 | 1 | 3 | 3 | 3 | 2 | 2 | 4 | 4 | 6 | 2 | 5 |

Notes

1. Rabushka appears to be calling for measures of economic freedom to at least this standard in that he wants “a rating system that permits quantitative comparisons across nations and over time.” Of course, the current international system of national accounts is not consistent and uncontroversial. See Kravis, et al. (1975).
2. These concepts and their measurement might be given more meaning by the following quotes from Gastil and Wright (1988), pp. 102-3. “A country received a high rating for freedom of property if taxes were not confiscatory, or if there was not undue concentration of ownership of either land or industrial property.” “Freedom of association is measured in terms of the evident ability of workers, owners, professionals, and other groups to form organizations to pursue common interests...” “Freedom of movement and information are basic civil rights that have a special meaning in the economic arena.” They involve freedom “to change employment, or to seek work elsewhere, even in other countries” and “to learn about conditions elsewhere in the country or world, or...to know what the government is doing and contemplating, or...to learn what others think and plan.” Economic freedom for an individual involves an absence of involuntary, arbitrary, and artificial constraints on the pursuit of economic activity. Constraints imposed by nature or by the existence of others with similar freedom or natural rights are generally regarded as natural constraints. In the previous chapter, Rabushka provides a more extensive discussion of the meaning of economic freedom.
3. For example, we could use the seven distinct categories given by Rabushka: private property, the rule of law, taxation, spending, regulation of business and labour, monetary policy, and free trade. We might note here that only a few of these categories appear amenable to straightforward, unequivocal, quantitative measurement.
4. An Austrian economist should find this approach doubly bothersome because it ignores the individual as the unit of analysis and proposes non-market measurement.
5. The relationship between workers’ rights and economic freedom might be quadratic. Economic freedom might first increase and then decrease as workers’ rights increased, implying there is an optimum level of workers’ rights.
6. See Coase (1960). For example, my right to breathe fresh air would impose a duty on you not to smoke. Your right to smoke imposes a duty on me to breathe smoky air. If my right prevails, you suffer an externality. If your right prevails, I suffer an externality. From the standpoint of wealth maximization, the one willing to pay the most should have his mutually exclusive right prevail. This would be the natural result from unfettered exchange, since one would buy the other’s compliance. Transaction costs, arising from bargaining over the division of the gains from trade or from imperfections in the “three D’s” of property (definable, defendable, divestible, see Anderson and Hill [1988]), may prevent such private deals and require a court or legislatively imposed deal to achieve wealth maximization.

7. That changes in economic freedoms might constitute Pareto improvements was recognized by some anonymous "Voice" in the Stahl "Discussion." Walker (1988, p. 313).
8. See Toumanoff (1984) for an exemplary treatment of this perspective. Also, see Carroll, et al. (1979) for an alternative and less benign evolutionary perspective.
9. For the sake of comparison, we include Wright's per capita GNP measure in our summary table 3. We should note here that this view of market evaluation of economic freedom would require that the national accounts be measured with market clearing prices and wages. Wage, price, and quantity controls would obviously distort this measure as would the measurement of government output at factor cost rather than market value. The former would tend to lower the measured value, which may be appropriate, while the latter would tend to raise the measured value, which would definitely be inappropriate.
10. For example, this could include household production valued at opportunity cost at the margin. See Posner (1987), Stahl (1988), or Spindler (1982) for justification of these adjustments.
11. However, consistent information on net measures is available only for a much more limited range of countries than those listed by Wright. We do include a net measure of sorts, private sector income per capita (PYC), in table 3. Private sector income per capita = PYC is obtained by multiplying the GNP column by one minus government expenditure as a proportion of GNP which was obtained from IMF (1985). This, of course, ignores household production, while including the value of output from nationalized industries (which may not be valued at market clearing prices).
12. This should be the unanticipated rate of inflation rather than the actual rate.
13. The principle of human duty in its widest possible extent, encompassing ethical and legal principles as criteria of evaluation.
14. Which under certain circumstances moves monotonically with private sector income. See Spindler (1982).
15. See Pilon (1988) and Posner (1987).
16. We present our most recent OLS results here which differ slightly from the OLS results alluded to in the original draft. Those results showed the coefficient for association close to one-third and the coefficient for property at about one-sixth. The differences are either due to different computer programmes or recording errors in the data, but since we do not have access to the data for the original results, we have not specifically checked for data errors. The corrected R^2 seems low given the supposed nature of the relationship. We have checked the TOBIT results which do not significantly differ from those for OLS.
17. Indeed, she makes this point in her discussion in Walker (1988, p. 126).
18. This also applies to specifications with other dependent variables such as logged and unlogged GNP and unlogged PYC. However, whenever AF or any other individual economic freedom is the only independent variable, it has a highly significant direct effect.
19. This is one of the seven categories discussed in chapter 4.
20. See Pilon (1988).

21. Although American economists did much work on this prior to the elimination of the draft in the U.S. in the early 1970s. For example, see Oi (1967).
22. No information was given on conscription for other ranks or services.
23. Age structure and gender would also be important considerations in determining the likelihood for specific individuals but not necessarily for the nation as a whole.
24. Although some make provision for a militia in case of national emergency and in some cases this might amount to an emergency draft.
25. Vatican City would be a special case where the residents are probably originally citizens of countries with other ratings. Most citizens of Lesotho are black and South Africa only conscripts whites.
26. However, this might not be appropriate from the standpoint of a prospective citizen judging from behind the veil of ignorance or uncertainty. That is, if one does not know whether one will have the characteristics that increase the likelihood of qualifying or disqualifying for military service, one's estimate of likelihood in prospect, in other words the ex ante likelihood, will be unaffected by the method of selection. The same rationale might apply for not adjusting the likelihood of obligation by the sex ratio or age composition in countries that conscript only young men.
27. Both foreigners and residents are harmed, and their economic freedom constrained, by differential national impediments. For example, the National Energy Programme imposed by Canada in 1980 drove both domestic and foreign oil drilling firms and workers and oil investors south of the border.
28. For a given administration, however, it may be more consistent and comprehensive than alternative sources.
29. As a private information gathering firm, it may have an incentive to provide more objective and economically relevant information than "Foreign Economic Trends."
30. However, my colleague J.M. Munro claims the ratings seem too favourable for two countries (Turkey and Indonesia) with which he is familiar. (Having just read a two-part *New Yorker* article on Indonesia, we are inclined to agree.) We expect others might give us similar feedback. We can only caution such critics that their judgements are made without having comparable information on the countries with which they are not familiar. It is a bit like the fabled German prince who gave the opera prize to the second singer upon only hearing the first.
31. Of course, with 110 observations the Spearman Rank correlation does not have to be very large (about 0.17) for this result.

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Discussion (Chapter 5)

Milton Friedman Michael and I were talking at the break and apparently we have different perceptions as to what our homework assignment is. Consistent with everything else that has gone on, I just assumed that we were looking for actual measures, the kinds of real world things you would want to include in some sort of index. Michael had an impression that it was more or less to add to Alvin's philosophical discussion. Quite frankly, what I have done is tried to figure out what kind of index I could come up with for the United States with my own resources, plus a grant from the Fraser Institute which would likely be in the magnitude of four or five dollars.

I am assuming we already have the computers. What I have done is just put down a listing of percentages. Percentage of property held privately—that seems to be fairly simple, easily obtained; percentage of GNP spent privately, that's GNP minus government outlays and spending mandated by government regulation; percentage of foreign trade not affected by tariffs, quotas, or subsidies; percentage of domestic trade not regulated...now that gets into money, I'd have to increase the grant for that one; percentage of the labour force not members of unions or forced military or, for other countries, not slaves; percentage of people who believe they are free, if you go out there and start taking some sort of survey. All of these are rough and ready but they should give some sort of grand index that I could then link to GNP and see if in fact it works pretty well with Henry's idea that freedom and prosperity are somehow related. Then I might come back and adjust it.

The economics of the whole thing is really going to restrict what we are talking about here and that has to be held clearly in mind.

Robert Poole If we come up with workable predictive values, who would find that useful? It occurs to me that there is a line of business called political risk consulting which assesses countries in terms of whether they are a good place to invest or not. Firms of this sort ought to be very interested in our deliberations, as some of these empirical correlations already suggest that, at least over the long term, there is a strong correlation between measures of economic freedom and ultimate prosperity and things that go along with that. Other interested groups would include the World Bank, various international lending agencies, multinational companies, the Chase Manhattans, the Citicorps, and all those people who have gotten into so much trouble investing overseas, perhaps out of ignorance, perhaps out of misguided notions, or for various other reasons. Rather than just an ideological crusade to change Freedom House, there is potentially some very practical and useful implications of this work, if indeed the world works the way we think it does.

Henri LePage Consider the very first paragraph of Zane's paper where he explains that we might require an international system of accounts for economic freedom. I immediately paled at the phrase "an international." Do we need only one international system of accounts? Why not a competitive system of evaluations? Behind any system of measurement there is always an implicit theory, so it is fruitless just to try to refine an existing system if you don't share the same basic underlying framework. We have to present an alternative system of evaluation and then make explicit the theory that lies behind it. This will give us the opportunity to present it to the people. Maybe one day, if we succeed in convincing everybody, we will end up with one system of measurement. But I would prefer first to go through the provisional stage of competition.

Consider Zane's discussion of separate freedoms: property, movement, association, and information. Here, again, appears our problem of separating political and economic freedoms. I strongly object to these four separate freedoms because it is absolutely clear that freedom of property or the private right to property is a pre-condition to both freedom of association and freedom of information.

Further on in Zane's paper there is a very interesting sentence: "the freedom to form restrictive associations impinges on others' rights to free exchange." No. That is something often asserted, but it cannot be. If you have freedom of association, and people exercise their rights, you cannot impinge on others' rights unless you pretend to give the others a right to have freedom of access to what you have created with your own rights, your own labour, and your own association. This is very topical. Take, for example, the case of the computer networks that are being developed all over the world. Many people complain that they are deprived of free access to these private computer networks. This same misconception arises in the field of exclusive dealing distribution systems. People say that where there is exclusive dealing, people are impinging on my right to distribute. This is nonsense.

This brings me back to Alvin's statement: "the freedom to have and use property is not absolute. It is limited by concern for the rights of others and the requirement that the state extract..." and so on. I mention this for one very simple reason. If you have a clear, precise, and consistent definition of individual rights, then you don't need to have any concern for the rights of others, because you cannot have conflicts between rights. If you do, it is only because of a very fuzzy definition of rights. So I return to what I was saying yesterday: The main issue in the whole debate is not so much the notion of liberty, it is the notion of rights.

Milton Friedman I think the opinion here that somehow or other there is no agreement is a bunch of nonsense. We have a great deal of agreement. I agree with David's interpretation of what I meant rather than what I said. In every scientific process you start from a beginning point and what you argue about are

the small changes you are going to make to go to your next approximation. That's what I was talking about. Of course, we have an initial idea developed over 2,000 years ago of what we mean by economic freedom. But we are trying to construct a better hypothesis, one that will have more content, and that is what we are talking about.

Now I want to go to the particular attempt that I think is very interesting. The one area that was most thoroughly developed, of course, was the international area which I think is a very important one. I at least had some of my own ideas clarified by going over what Zane had done. I don't mean to be excessively critical in saying it was schizophrenic, because I think it was. That isn't a critical comment. It's a descriptive comment.

The reason I am particularly interested in it is because it ties in with, as Zane pointed out, the correlations I constructed last year. Once again we find that civil liberties are by all odds the most important single item. That raises a fascinating question—which is cause and which is effect? Are high income countries capable of providing extensive civil liberties because they can afford to do so, or does the existence of the civil liberties help account for the high income? Offhand, I don't see how to distinguish between those two. But I am sure that if we think about it, we will find a way to try to get some idea about the direction of influence.

At any rate, it shows how silly it is, in my opinion, to talk about civil liberties as something other than economic liberties. This classification into civil, political, and economic, while useful for some purposes, is also a very confusing distinction. What we have is liberty and some aspect of it we like to refer to as economic, some as civil, some as political, but this reinforces the evidence that the civil liberties ought to enter into our concept of economic freedom. It is really an economic freedom for me to be able to speak freely. Really, it is not the freedom to speak that is the civil freedom or the economic freedom, it is the freedom to listen. It would be much more important to talk about freedom to listen and not listen. I don't think it is freedom of speech when a loudspeaker blares down the road and I can't stop listening. It is freedom to listen that is crucial. It is freedom to hire a hall to persuade people to come and listen to you. All I am saying is, that's economic freedom. In order to defend that economic freedom for myself I have to buy soundproof glass to protect myself against violations. That seemed to be very interesting, especially the direction of influence.

Look at Zane's table 4, the correlation matrix. This is fascinating because it immediately suggested to me that what you needed to do for both this and for your other listing, the international trade one, is to apply some factor analysis to it. If you look at those correlations and pick out the high ones, you find that there is a great cluster. There are two, three, or four of these elements that are really the same thing in disguise. As you know, factor analysis is a technique that, as it happens, was developed very extensively in the case of intelligence measures,

whereby you try to separate a whole set of variables into clusters. They are measuring the same thing in different ways. I need not go into the technical analysis of how you identify the clusters from among them, it is a complicated and sophisticated thing. Unfortunately, nobody will understand it anymore because there are now computer programmes whereby you can do it without understanding it. That is one of the great costs of computers to set against the advantages. At any rate, this material is crying out for factor analysis.

An eye-ball investigation of the clustering suggests that one of those clusters is between association freedom, information freedom, and movement freedom. The highest correlation coefficient is the 0.89 in the final column, third one down. And this is association freedom correlated with economic freedom. Since economic freedom is a linear combination of the four others, any decent factor analysis will throw out that collection of four as one cluster. What you really want to do is to leave out those that are already composites of others and get the clusters of the elements of these various things.

James Ahiakpor My comments relate to Milton's on the technical side. As he has pointed out, some of those things separated are really part of what we should call economic freedom. Although Zane interpreted the results of freedom of association as perverse (he expected such freedom to work counter to economic prosperity), I don't see why that should be so. The ability to associate with other people to enhance one's economic prosperity should be a good thing, or at least should be considered a positive part of economic freedom.

What I think Zane really has in mind is the restrictive aspect of trade unions. For that we need to find a way of capturing government legislation that makes it possible for trade unions to interfere with the free market and produce the negative consequences he has in mind. Indeed, there are co-operatives that function very well. So association freedom, as his results show, is most highly correlated with economic freedom and that should have been anticipated.

Similarly for freedom of movement. If people can move around and better themselves economically, that should enhance wealth. This should not be competing with economic freedom, however you define it, in the same regression analysis. I also think use of integers should be avoided. After using all those cross-multiplications to produce a final average, we rather obscure the differences between countries by again rounding off the results. For example, we find that Zaire, on total freedom, scores one, Russia three, Canada two, Egypt four, Trinidad and Tobago four, and Uganda three. I know that Uganda ought to be further behind. Zaire ought not to have a rank of one, above Canada, in terms of economic freedom, so these results just strike me as odd.

Zane Spindler No, that is trade freedom. But when you look at Zaire, nine of these characteristics were rated which is pretty high for that sort of country.

Milton Friedman Maybe it has a lot of trade freedom.

Zane Spindler It may have.

James Ahiakpor In any case I think your rounding obscures the distinctions between countries.

Zane Spindler I know, but I was trying to get something consistent with Lindsay Wright's ratings.

James Ahiakpor The bunching that Zane wants can still be done within the ones, twos, and threes and we will see how the countries actually stack up in order of significance. Also, the weights ought to be assigned from either a theoretical or philosophical discussion of how important these things are, or else be derived from a regression estimation. Either you want regression coefficients to speak or you want a priori to design the weights.

I also wonder, now I am entering into a debate here, why Zane wants to use military expenditure as an indicator of restriction of freedom, although I know he actually used existence of the draft. If the first duty of government is national defence—I know some people would dispute that—if it is, then what we really want to be talking about is whether the draft is less efficient than a voluntary army. We should be careful not to use existence of the draft simply as producing a negative effect on economic prosperity or economic freedom. Because the government still has to provide defence.

Zane Spindler A lot of people see conscription as building positive economic freedom because it trains people for a very important job function; and that is to be able to get up in the morning and punch a time clock.

James Ahiakpor What I am getting at is this. It has been demonstrated that a conscripted army is less efficient for the economy than a voluntary army because some conscripts may be more efficient in other areas and would be willing to pay others to go render military service for them. That argument should be separated from the fact that we have an army, which may be considered undesirable.

Using the private sector national income as an indicator of economic freedom is a little confusing because whatever the government appropriates is ultimately spent on individuals also. So what you probably have in mind is government control, or government spending, or government allocation of some portion of the national income.

Zane Spindler No. What I have in mind is Niskanen's model of bureaucracy which, at the extreme, completely exploits all the sponsors' surplus so that there is no net wealth created by government.

James Ahiakpor But the government is simply redistributing wealth.

Zane Spindler That's all it is. Just shuffling money from one place to the other without creating any net wealth and possibly destroying it.

James Ahiakpor Which is why simply taking the private sector spending ignores the fact that whatever is taken by government also gets spent by individuals.

Zane Spindler But that's illusory. Government spending is calculated on a factor payment basis which is not the same basis as for market output.

James Ahiakpor Whatever the level of national income, however we define it, it is produced by individuals and ultimately spent by individuals. The part appropriated by the government is simply taken from one group and given to another within the same community. So whatever is spent by government is not lost. It is still within the economy.

Milton Friedman How did you define private sector income? Did you simply subtract government spending from national income as defined?

Zane Spindler That was the quick way that we did it, yes.

Milton Friedman Well, I think that was a mistake.

Zane Spindler Yes, I know.

Milton Friedman I am returning to Zane's case because it has to do with the definition of national income. Under that definition, government spending can be more than 100 percent of national income. It happened once, in Israel. From an accounting point of view, it is possible that total government spending can exceed national income. The reason is because government spending includes transfer payments and national income does not. I have always argued that a better measure would be one minus the ratio of government spending to a denominator that would be national income plus transfer spending. Government spending divided by national income plus transfer spending cannot exceed one and that seems to me a much more meaningful construct. I always try to defend it by saying, "suppose you just do this. Everybody who gets transfer spending is automatically going to be called a government civil servant assigned to the task

of either taking care of children or enjoying leisure or whatever; these are tasks assigned to them by government.” Then they would be included in national income. That is the easiest way to raise national income, and it can be substantially raised simply by calling all of these people civil servants.

Zane Spindler Two points. First, the reason we didn’t use Milton’s suggested measure was that the data were not available to us in that form. We had a proportion available that gave us a quick measure for all of these countries, and finding Milton’s measure would have been a bit more costly.

Second, with respect to James’s point as to why I would exclude government spending even though the money goes to people: I am relying on the public choice idea that there is no net value created by government spending. Net value is produced in the private sector with consumer surplus, producer surplus, and factor surplus. Leviathan government extracts and wastes all surplus, and therefore if you want something that is monotonically related to net wealth, which Henry Manne and others might be interested in measuring, you would exclude the government sector.

James Ahiakpor Two things are being conflated in the last statement Zane just made. They are the estimation of national income and the consequences of its distribution. We can talk about government spending producing less wealth or almost nothing compared with private spending. But whatever the government spends must have been created initially. What I am saying is that excluding government spending as if it doesn’t belong to the economy is a mistake.

Getting back to Milton. Transfer payments come from taxes unless we have, as in the case of Israel, foreign transfers. Thus, indeed, there is private sector spending and government sector spending, but government sector spending is withdrawn from private income initially created, and the two together have to be equal to national income. So when you say national income plus transfers, I think you are adding something over and above what has been created.

Milton Friedman No, sir.

David Friedman I may be misunderstanding James’s point. It would seem to me that if you have a society where the government taxes a billion dollars and spends it hiring people to build cars that they then dump in the ocean, that society is a billion dollars a year poorer than if they had never taxed it in the first place. The real income of that society is one billion dollars lower. If you believe that the marginal productivity of government expenditure is zero, which is sometimes a low estimate and sometimes a high one, then in calculating national welfare you should write off government expenditures, and the taxes that pay for them, as a loss.

Zane Spindler Just to make clear why I agree with Milton's point on this, consider unemployment compensation. I view that as a payment for work not as a transfer. It is payment for looking for work but not finding it. That's a job. That's what people are being employed to do and it is a very important job and it should be included in terms of creating income as measured in the national accounts, but it doesn't create any net wealth compared to what those people could have done if they were assigned to a real productive job in the private sector.

James Ahiakpor But what was paid to the unemployed was wealth previously created.

Zane Spindler What we paid to our bartender who by his activity creates wealth we originally created too. We also worked to create wealth that we paid to the guy who has his hand out on the street but in that case nothing else is created.

James Ahiakpor Which is why I am saying that you are concerned with the second stage of the argument, that is, the consequences of different uses of wealth. But by maintaining to that concern you are ignoring the fact that for wealth to be transferred, it first has had to be created.

James Gwartney My point is really very minor. It relates to this issue of whether or not government expenditures should be valued at zero or at cost and under what circumstances. The reason why, within the framework of the Niskanen model, one might argue they should be valued at zero is because when the government is a monopolist, it will tend to expand output until all consumer surplus is eliminated. In contrast, this will not be the case in a decentralized setting. Why would you want to value not only government expenditures but any other expenditure at, say, its purchase price? Because people would not have purchased it, if in fact they did not value it by the amount of the purchase price. In a decentralized setting with local governments the argument for treating government as a monopoly is much weaker. Therefore, I would argue that one probably should add at least the local government expenditures, if not the state government expenditures, to provide output because then if government is taking all of your value from you, you could go to some other location. You have a type of competitive process, albeit not as strong as within the market framework, but a type of Tiebout model present where there would be some reason to expect that the consumer is getting value from the government expenditure.

James Ahiakpor You can look at national income as rewards in the form of wages, interest, rent, and profits. It is out of these that some part is being spent by the private sector and another by the public sector or government. What is spent

by government is a diminution from these four categories of income earning groups. To simply delete what is spent by government from the income originally produced by these four classes is a mistake because you are now under-valuing what was produced.

Milton Friedman I agree with what he is saying but not for the purpose we are now discussing. We are asking ourselves, What is a measure of economic freedom? The measure of economic freedom is the part of this grand total that is available to individuals to spend according to their own desires and wishes as opposed to what is not. Even taking total income plus transfer expenditures and subtracting from that the total government expenditure overstates greatly the resources available for people to spend freely, because some of those expenditures are forced on them by government and they have no choice about it. So it is a very approximate measure. But I don't confuse the questions of what is the total output of the country with what is the fraction of it that is available to private people to spend, which is what Zane is trying to measure.

Charles Murray Just a few quick comments on the general problem of making indices, especially cross-national ones. I would just forget about most of the Third World because the quality of data is so bad that it obscures real variance captured with our indicators. I would stick with real clean data with a much smaller sub-set of countries and use longitudinal data for the countries with good data rather than worrying about a larger sample.

It is also very important to focus on the countries with the best data for purposes of checking the face validity of a lot of these things. Some examples have been pointed out where you have crazy ratings just on the face of it. If you concentrated on a few countries, you could get a much better sense of whether you are really measuring what you think you are measuring.

I would also point us to a body of literature that is not very well known but that is very useful for this. A lot of what we are doing with this kind of index calls upon non-econometric traditions rather than factor analysis. Louis Guttman, who developed the Guttman scale, has done work in the last 15 to 20 years on a thing called facet analysis and a statistical procedure he uses called "smallest space analysis." You might want to take a look at it.

Gerard Radnitzky In Zane's table 1, West Germany is listed among "nations with no conscription." Such things make one suspicious of the accuracy of the tables. West Germany has the largest conscripted army in Europe, about 206,000 conscripts per annum, and the time of military service is about to be increased from 15 to 20 months.

If you check table 2 with respect to West Germany, you conclude that it projects a misleading overall picture. Perhaps it might be applicable to West Germany's performance in the early period of the so-called economic miracle.

From about 1966, after the “socialist” take-over with Willy Brandt, the situation changed drastically: state expenditures rapidly increased to about 50 percent of the GNP. The average tax burden has been rising since, even under a conservative-liberal government that came to power with the promise of a turnaround. Social security taxes have skyrocketed: while remuneration for work effort tripled from 1966 to 1984, the non-wage benefits increased sixfold. Last year, non-wage benefits in industry, on average, amounted to 83 percent of the effective salary. Germany has the highest rate of taxation on corporate profits in the world—in 1986 it was almost 71 percent. German industry has the shortest working hours of all industrial nations—1,633 hours per annum, while the U.S. has 1,966 and Japan has 2,133. The wage structure is determined by centralized collective bargaining, and a corporative climate prevails throughout. With respect to productivity, Germany has become the last among the seven leading industrial nations. While the Kohl government vowed to cut subsidies, they have actually risen 25 percent. If we include rules and regulations as part of the infrastructure, then the good mark Germany gets on this point in table 2 is grossly misleading. Investors face a tangle of laws, regulations, taxes, and other restraints on growth. Some months ago, I saw a long interview of Milton on West German state television. As usual, he epitomized the situation best. He concluded with the remark, “The Germans are living on their fat.”

I have been so explicit in my discussion of the example because the various categories I have mentioned are all relevant to a comparative description of countries with respect to economic freedoms and civil liberties which, in many cases, cannot be disentangled. Second, I guess that at present we are not yet in a position to produce a comparative description of countries that would help the potential investor in assessing comparative interlocational competitiveness and the relative attractiveness of governments.

Zane Spindler But who are these Germans who are complaining? After all, they would have higher standards.

This sounds like an excellent source of data for revising these ratings if they do it for a series of countries.

David Friedman I just have a couple of brief comments on the paper. One point about the draft is that Zane suggested it was a greater restriction on freedom if the military pays very much below market wages. Whether that is the right way to look at it depends on whether you are including taxes as a restriction on economic freedom. Consider two countries with exactly the same drafted army and good capital markets. In one country they pay draftees \$5,000 a year and in the other \$20,000, but there is an extra \$15,000 annual tax per draftee in the country that pays the higher wages. Assuming there is a good capital market so that the draftee can borrow against his future income, and assuming that everyone gets drafted, everybody is exactly as well off in both countries. So if

you leave taxes out in calculating economic freedom, then you also ought to leave out the low wage of draftees, otherwise you are saying that the first country is less free than the second.

But that is true of other taxes as well. They're still a restriction on economic freedom. The point is that if you are including taxes as a restriction on economic freedom, then you want to include this as well, otherwise you don't.

My second point is that if we look through Zane's table in the unrevised version, the most striking thing is that all of the countries that have low freedom and high income are oil states. This is clearly messing up the regression results. One way of controlling it which doesn't involve worry about oil in particular would be to include some weighting by population. Resources are not an important determinant of real income in the real world. They only matter in countries that have a lot of resources and nobody living there: places like Saudi Arabia, Kuwait, maybe Canada and Australia. The easiest way of getting rid of the problem is not to over-emphasize the importance of resources by counting a country with 100,000 people and a lot of oil reserves just as much as a country with 100 million people. It would be interesting to rewrite the regression in some way in which you weight countries by population—maybe by square root of population, I don't think it matters very much—and see whether that gives you much cleaner results.

Zane Spindler We have used the oil countries and industrialized countries as dummy variables. This yields some marginal improvements in fit, but there are interactions with other variables, as you point out.

Milton Friedman Two comments. I want to point out the interaction between what David said and what Charles said because, in principle, you would like to weight your observations by their accuracy and that would kick out most of the Third World. Their accuracy would be zero. It would also kick out most of the oil states as the little states so that taking Charles's suggestion would go a long way toward resolving the problem that David has raised.

Zane Spindler What good would the index be then?

Henry Manne You have two different issues. One is that you are trying to get an index, and in the course of doing that, why don't you stick with the best data? Then, once you have an index you are satisfied with, tackle the problems of how high up you want to go.

Milton Friedman It depends, Henry. Suppose it turned out that a pretty damned good index could be obtained by such a number as a percentage of the population that was employed in domestic service. Well, with that figure you might be able to get a very accurate estimate for Third World countries. On the other hand, if it

turned out that in order to get a good estimate, rather than use something that you liked as an index of economic freedom, you had to use something like, say, the ratio of government spending to total income plus transfers, then you would be in a terrible position with respect to these countries. So I don't think you want to prejudge the issue as you do when you say something or other is not measurable.

Henry Manne I'm not alone.

Milton Friedman Oh, there is more than one person who makes the same error. But surely your position as a scientist ought to be, "we don't know." This is all technical. Maybe it will turn out that it is not measurable, but you can't say "of course it's not measurable." In the same way, once you get some kind of a sensible hold on it, maybe it will be possible to get that kind of data for many countries. So, I have a great deal of sympathy with Charles's suggestion that you ought to concentrate on those countries for which you have decent data, where you know something about them, where you can have some sort of non-quantitative qualitative judgements about what is going on. You have a way of checking whether the results you are getting are sensible or not. If you get a result that shows Zaire as having a high degree of economic freedom, you know you have made a mistake.

Robert Poole I would like to suggest that one way of not necessarily excluding a lot of Third World countries for which quantitative data may be very spurious or unreliable would be to look at yes/no indicators. The presence or absence of certain types of restrictions and controls—rent controls, some trade barriers, etc.—may be much more measurable than precise numerical quantitative continuous variables. The former are specifiable by one or zero and a lot of those kinds of things can be available for many Third World countries where a numerically quantified measure would not have any reliability.

David Friedman One problem with that is the distinction between a law that exists and a law that is enforced. I am thinking now of a piece by Sam Peltzman on the question of prescription drug regulations. One of the interesting things on the international scene was that, as I remember, all countries in the world have American-type requirements for getting prescription drugs. However, half the countries in the world ignore the requirements. Peltzman asked people whether they could in fact get such drugs without a prescription and the answer in many countries was yes.

Robert Poole Narcotics laws are another example.

Walter Block Also death penalty laws. Isaac Ehrlich did some very interesting work on this subject.

Milton Friedman How about the number of prisoners in jail? Is that a good statistic for these Third World countries?

Robert Poole Is that an economic freedom?

Milton Friedman Sure.

Robert Poole I doubt that it is reliably available.

Henry Manne It shows very nicely the problem of trying to distinguish economic freedom from these other freedoms.

Milton Friedman Absolutely.

James Ahiakpor Let me speak for the Third World since evidently I am from there.

Milton Friedman You're talking about Canada? [laughter]

James Ahiakpor Actually Ghana, although I take your point. The problem is that the outcome of this exercise may be more relevant for the Third World than the more developed countries. It would be pretty sad if, in fact, although they constitute the majority in the world, they would not benefit from this kind of exercise. They need, more than others, to be convinced that there are certain things they can do better to promote their own interests. I don't think most of the governments out there really intend to hurt their people with the policies they have adopted. They simply happen to have chosen inconsistent and wrongheaded policies. Therefore, a solution may be to first build a table according to our ability to measure certain indicators. But when you have a table that includes some countries with two things measured and other countries with five and so on, and then derive an average, that table distorts reality. Rather, we may group countries according to the categories that can be measured and then see how they stack up.

Second, we need more diligent work, much more than now exists. The numbers have been assigned too loosely. For example, "Do you have free trade or is the government planning to go free trade?" gets a score of 1. "Do you have private enterprise or is the government proposing to do that?" is given the same score. Altogether, such alternatives are too loose. This explains why Britain and some others fall within the same ranking when they should be separated. I think we want to get tighter in our distinctions.

Finally, I think institutes, including the Fraser Institute, would be interested in the results of estimating economic freedom in Third World countries. Such results would be helpful for testing hypotheses about what makes a country grow. As Adam Smith would ask, is it low taxes, honest government, and individual liberty that promote growth? So we should not leave out Third World countries.

Rose Friedman My comment is also a reaction to this. It seems to me that we would get a lot further with instructing the Third World if we had a good measure that compared economic freedom with the results in terms of utility or prosperity or whatever for those countries where you have good data. That would be a much better lesson than trying to use Third World countries to get the measure when you don't have any relevant data for them. I don't think you need to include the Third World countries in an attempt to demonstrate to them that certain things lead to prosperity.

Charles Murray The first objective is to get a good index, because if it is not good, then you don't have anything. It seems possible that when you are done with the entire exercise, you will find that relatively few measures do a really good job. But we don't know that to begin with, and so we should focus on the best data to get to that point. If at the end we have a measure that can be applied to other countries, fine. But don't start out by trying to apply it everywhere. I am thinking more about the development process than anything else.

Milton Friedman I fully agree with Charles.

James Ahiakpor I don't want to go on record as saying that all Third World countries should be included, regardless of the fact that they don't have measurable or accurate statistics. No. I thought Charles's point was going to lead to too many deletions. World Bank or IMF statistics have much useful data that we can employ to measure or get a sense of what is going on in a country; this can be complemented by reading history. Obviously, some knowledge of a country's history would improve the measurement process.

Milton Friedman One of the great virtues of restricting the research as Charles is suggesting is that instead of using so many of these qualitative variables, you have much more ability to use a few more informative, quantitative variables. We are talking about the ratio to income which you can't do for most Third World countries. The World Bank gives estimates, but they're not worth the paper they're written on for many of these countries. Or again, if you are going to investigate freedom in international trade, the variability over time in purchasing power based on actual exchange rates would be, in my opinion, a better index of the extent of free trade than would be many of the elements of this whole big

listing. I understand why you do the listing in a rating form to get numbers like one, two, three...but I agree with Charles. If you really do a good job on this, you are going to end up, if done imaginatively, with a very small number of indices. I wasn't joking when I was suggesting the number of people in domestic service as a fraction of the population. That might turn out to be an excellent index of economic freedom. Just as it turns out to be a good measure of the degree of inequality in a country.

All I am trying to suggest is that one of the great virtues of restricting the summary to where you have data is that though one ought to investigate the country and its history, you can't do so for 150 countries. Not even Zane and his assistant's enterprise and determination were able to do that. But he can do it for 20, 30, or 40 of the really major countries for which he knows a great deal to begin with.

Antonio Martino I just have two small points. One, shouldn't we include government inefficiency as one of our basic economic liberties?

David Friedman You mean the less efficient the government is, the more free we are?

Antonio Martino What I mean is that if a country has a formal restriction on trade while it also has extensive smuggling, then you are not as constrained in your freedom as you would be if the restriction was enforced. I come from a country where this is a case.

The second point is that I don't understand why you put Vatican City under nations with no military. They have a fairly large army—the Swiss Guard.

Zane Spindler I know that from being there several times but that is the way it is.

Milton Friedman I don't know why you have Vatican City listed at all.

Antonio Martino Or San Marino, for that matter.

Walter Block As you know, the Liberty Fund frowns upon the chairman taking a substantive role in the proceedings. But, as there are now no people on the list for the first time in the conference, I would like to pose a question for our consideration.

A statistical issue that has been puzzling and disturbing me is that if we come up with good criteria for freedom but have no explicit weighting system, then we'll have an implicit one. That is, if we have, say, 100 criteria, each will be in effect weighted at 1 percent. This would be weighting by indirection.

Milton Friedman No, no. If you do what he is suggesting you will correlate it with the things you are interested in and derive a weighting from the data.

Walter Block I was going to ask about just that point. If we correlate it, say, with income or infant mortality rates or whatever, are we not guilty of fudging? That is because we are later going to try to see if there is a correlation between our measure of economic freedom and these measures of wealth or income. If we start off by weighting our criteria based on these things, there would appear to be a serious problem.

Charles Murray It is important that we come up with an index that is satisfactory to the sense of the construct we are trying to make operational, independently of any knowledge about correlations at that point.

This is one of the problems I have with factor analysis: you get a lot of data dredging with it. The reason that I pointed to Guttman's work is because that is the most rigorous way I know of forcing the person who is constructing an index to say, "Here's the way I believe these indicators relate to the thing I am trying to measure." In a sense, what we are trying to come up with is an index that permits us to say to an audience, "Here's a thing I want to put into operation. Here are my measures for it and an intelligent audience will look at the measures and look at the construct and say, yes, they correspond."

There are statistical ways of pushing the proxy measures and adjusting their reliability, but that is down the road.

Milton Friedman The answer to Walter's question is that this is a way we are deriving it. It is not a way we are testing it. One way we can test it is by taking data we haven't used in that correlation.

David Friedman There are two possible ways around the problem Walter has raised. One is to develop your index on one body of data and test it on another. The other is that the test you use is not to ask how well this particular weighted average performs, but how likely it is for this number of variables that the best weighted average of them would perform this well if there were not a real relationship. So you can do your confidence test allowing for your fudging, as it were. The confidence test is in effect saying, "We have five variables, the experiment we are going to do is to find the best fit. How likely is it that the best fit will be as good as the one that we got?" You can report that result as a legitimate non-fudged answer.

Chapter 6

Open Roundtable Discussion

Walter Block Welcome to the sixth and last panel of the Rating Economic Freedom Conference. This session is somewhat of a departure from our usual practice because we are not now considering any specific paper. Rather, we shall have an open discussion. The planning committee felt that we might appreciate a chance to speculate on some things that couldn't be said during the previous panels. As well, this session should help us in the future planning of this on-going project.

I would like to start the ball rolling by commenting on a point Milton Friedman made. He said that liberty is a fruitful topic for discussion, but once you start to rate or measure it, then ideas are elicited that would not have otherwise come to the fore. As a result, we obtain new understanding and insight. I agree. This discussion certainly does provide a new perspective.

I would also like to forcefully resist the notion that this enterprise is a sort of public relations gimmick, and that we would be better off hiring a public relations team instead of discussing this issue ourselves. In my view we are embarked upon a scientific study. Hopefully, one day our present efforts will engender Ph.D. dissertations on this topic and create a journal for rating economic liberty. Of course, there are ideological or public policy implications in what we are discussing. But the same is true when we study rent control, minimum wage, or tariffs. It is no contradiction to say that we can study these topics—all of them—from both normative and positive viewpoints.

Let me address the issue of consensus. Seemingly, there was a lot of disagreement expressed in the last few sessions. This is more apparent than real. We might have different ways of articulating our views but there is a core of agreement. Many people have had difficulty in articulating their analysis of economic liberty, but this might be because the question of empirical rating is so new to us. Then there is our natural tendency to emphasize the things we disagree on. If we focused on things of which we all agree, we would go around the room saying, "yes, yes, yes, I agree with Professor X, yes, yes, Professor X is right on." We

wouldn't have much of a conference. It would be pretty boring. So the natural tendency is to emphasize disagreement, not agreement.

Of course, there are some grey areas. And for these cases I would like to suggest a few aphorisms. "When in doubt, leave it out." Or admit that our theory is not yet developed well enough to determine the proper answer. When we at the Fraser Institute are faced with the problem of one of our leading lights, say, Friedman, saying one thing, and another, say, Hayek, saying something else, we merely allow that the theory is not that well determined and that there isn't one answer representative of our free market school of thought.

Another aphorism: "If it is worth doing, it is worth doing imperfectly." I think this is going to be the subtitle of any book we might publish on this topic. At least it is an organizing tool in my own mind. It is so important that I am going to repeat it. "If it is worth doing, it is worth doing imperfectly." The present task before us is worth doing. I know we are going to do it imperfectly, but we should at least try it, and see if it has any use or not. Will the world be better off for our efforts? Will our understanding be enhanced by having this economic freedom rating? That's something we can only tell after we do it. At present, we can determine if it is worthwhile pursuing solely in our own minds.

I very much wanted to agree with Jim's point about the difficulties of defining unemployment or measuring unemployment and GNP and all these other kinds of things he mentioned. They all have conceptual problems. They all yield some benefits. We have as good a chance of making empirical sense of economic freedom as those cases, and of having our ratings as widely used.

One last point I wanted to emphasize is the analogy of measuring economic freedom to measuring IQ. I submit that we are now in roughly the same position as Stanford or Benet before they developed their IQ measure. We are trying to come up with a list of questions that we will operationally define as economic freedom. This will be as close as we can meaningfully get to that concept. That is why the homework was asked for. In no particular order, the following lists the results provided by participants at this conference:

Measures of Freedom

1. Restrictions on international trade
2. Restrictions on immigration
3. Restrictions on emigration
4. Government spending, including what funds are used for:
 - mandatory costs imposed on industry
 - regulations and restrictions by government such as seat-belts, etc.
5. Education—whatever the state monopolizes
6. Freedom of travel, freedom to relocate one's domicile, absence of internal passports

7. $\frac{\text{Total Government Spending}}{\text{Net National Product} + \text{Transfer Payments}}$
8. Measure of economic freedom is sum of
 - a. $K1 \times$ government expenditures percent of GNP
Direct cost of government to taxpayer
 - b. $K2 \times$ percent of labour force in forced labour
[military draft, forced jury duty, etc.]
If measurable, add to term the numerator of term (a) (wage difference between market wage and forced labour wage multiplied by the number of forced labours, e.g., the implicit tax on forced wages)
 - c. $K3 \times$ tariff collections/GNP \times tariff collectors/total imports subject to tariff (c-e are c, e proxies for excess burden of taxes)
 - d. $K4 \times$ percent of population in jobs that require substantial government permission to enter
 - e. $K5 \times$ (average marginal tax rate) (averaged over people)
 - f. $K6 \times$ percent of all market transactions that take place under binding price controls
If measurable multiply by $\frac{P_{\text{market}}}{P_{\text{controlled}}}$
 - g. $K7 \times$ percent of all market transactions that are illegal but not coercive multiplied by $f(P_b/P_m)$ where
 P_b = black market price (average)
 P_m = free market price (estimate and average)
 $f > 0$ (not sure of best functional form)
An attempt to measure magnitude of restrictions. Percentage term represents magnitude of restrictions. f has two purposes: strong enforcement may decrease percentage but will increase P_b , so f compensates. And P_b/P_m measures damage done.
9. Tax measures
 - a. aggregate tax rate
 - b. ratio of the top marginal income tax rate to the average income tax rate
10. Reaction index—sum of government deficit and the underground economy as a ratio to GNP
11. Ratio of government debt to total debt outstanding
12. Ratio of the exchange adjusted price of a standard basket of commodities in the domestic economy to the world price of those same commodities
13. Price relatives as a measure of regulatory restriction—domestic prices relative to world prices
14. Fraction of total income devoted to various expenditures by the median household
15. Fraction of total agriculture output marketed by government agencies
16. Emigration rate as a ratio to the birth rate

17. Marginal tax rate of person with an income twice the mean
18. Highest marginal tax rate minus the base marginal tax rate
19. Government expenditures as a share of GNP
20. Tariff revenue divided by total value of trade
21. Inflation rate during last five years
22. Share of aggregate output subject to price controls
23. Government employment as a share of total employment
24. Property rights

Ellen Paul I am intensely interested in what you will be doing at the subsequent conferences. What plans are for them? Could you just give us an overview of that.

Walter Block My own answer is that Alvin's third paper would be the core of what we would be doing in the next year. Namely, taking six or eight or ten topics and asking six or eight or ten specialists in areas of labour or expenditure or taxes or trade or what have you, to write a paper that would take what we have deliberated upon here plus what was done last year and get us one step closer to what an empirical measurement might be like. What kind of data exists? What kind of data might be fruitfully sought? I would ask Alvin to add to that answer.

Alvin Rabushka Let me elaborate on Ellen's question. What I hoped to do in the third paper was find the smallest number of general categories encompassing the largest amount of material in a way that would let us ask a series of questions on which we would try to collect evidence, come up with a better qualitative understanding, and hopefully move in the direction of something more quantitative. Then I was interested in seeing whether people would be proposing alternatives, other sets of classifications or additional ones, or reconstituting them in different ways. The next step was to design a sensible classification scheme, and then find people knowledgeable in these specific areas who would be very sensitive to the issues and questions that would arise in each category. In the process, we move from philosophical to conceptual notions. From there, to empirical indicators that link those concepts back to our philosophical understanding. Then, when we talk about economic freedom, we can talk about any of its dimensions in any country, find a rating for it, and see how it compares with other countries.

Milton Friedman I don't disagree with anything either Walter or Alvin is saying. But I want to suggest a different kind of approach. Start with something simple and work up to something complicated. You work up to something more complicated as you find out what's wrong with one sample. I was the one who

suggested this construct of one minus the ratio of government spending to government spending plus transfers. [Point 7 above—ed.]

All the time we have been sitting here I have been looking at that blackboard and thinking what a shame it is that nobody used it. So I am going to use it to suggest hypotheses that might lead us to the next step. I want to draw a couple of graphs. I want to rate countries here by their per capita real income which we'll call PYC. Private per capita income or total per capita income. For my purpose it isn't going to matter. Then I want to put up here this particular measure. The fraction of GNP plus transfer expenditures equal government spending. Then I predict that if you do this you will find that very poor countries have a very low ratio. And immediately that suggests two things are at work: capacity on the one hand, the role of incentives on the other. Poor countries can't afford to spend much on government and transfer payments because 90 percent of their income is going to agriculture and food. As they get richer they start spending more. All the way through you have these two forces at work and that immediately raises the question, how do I separate these two things?

The second thing I want to do is to plot along here the percent rate of increase of GNP. The percent change of PYC and again we plot the same measure here and I predict there you will again have an inverse "u." The stagnant countries will have a very low grade because they will mostly, though not all, be poor. But beyond this point it will again go down sharply over a long period.

Antonio Martino Wouldn't it become negative at one point?

Milton Friedman Yes, it might become negative, but I am not sure what it would look like on the negative side. The two things that we are really interested in if we are going to try to use this as somehow connected with welfare or growth, are the level and the rate of change. It seems to me that if we start with some simple ratios like this—and this isn't the only one, maybe there are some others in the homework list that would do—it will lead us to ask the right questions about what's wrong with this. In looking over the list, the things that are repeated over and over again are government spending as a fraction of income or government spending including funds for mandatory costs, and so on. So everybody automatically and intuitively thinks that's right. And yet in a certain sense it is wrong if what I say here is right. And then you start wondering how to add other things to it that can improve the measure.

It seems to me, and this is where I disagree with Alvin, that if I start along his route and have these eight boxes I am trying to fill all at one time, I really don't know where I am going. I don't have any sense of what is most important. What is it that I am missing? I am just fishing in the dark. Just talking about research strategy, not about getting anywhere. Maybe this process will ultimately lead to a list of 50 characteristics. But I don't believe it. I think that to get somewhere the process is going to have to be pretty damned simple.

Zane Spindler Your suggested experiment has already been performed. McCallum and Blais in *Public Choice* find that the relation between growth rate and the size of the welfare state is non-linear with an optimum size implied at some rather low fraction of GNP.

Henry Manne Consider the issue Milton raises about simplifying. It is even more acute than he has already suggested. I say that because a realistic list would be so very much more full and more difficult to compile (if not impossible) than this one is.

The list is very peculiar in one regard. There is just one reference to regulation and it is number four. It is government spending, including regulations and restrictions by government. Presumably, this means the amount of money the government spends to incur these regulations. But even to put regulation on that list doesn't raise it to the level that needs to be considered.

Milton Friedman Let's suppose you are required to put in seat-belts. I can regard the money you spend on that as government spending.

Zane Spindler Or taxation.

Henry Manne But Congress's adoption of the Williams Act, which cost shareholders around \$30 billion according to one estimate, didn't cost the government anything.

Milton Friedman Of course it did. It costs \$30 billion. Some people lost \$30 billion...and I should include that as indirect government spending.

Henry Manne That's what I am saying. But I had read this to mean that you were looking at direct government spending.

Walter Block Could you please briefly describe what the Williams Act is?

Henry Manne The Williams Act regulates corporate take-overs. But this is only the tip of the iceberg. Let's go through some of the better known agencies and think of things that they do: the SEC [Securities Exchange Commission], making less efficient markets for information, markets for corporate control, brokerage services, any number of other things—that's a tiny bit of the whole picture, and yet there are enormous sums that are lost due to the SEC.

Look at the Federal Trade Commission when, in years past, it had a significant cost effect on American goods, to say nothing of anti-trust law. I am not sure which of those, quantitatively, was larger, but neither was insignificant. The NLRB [National Labor Relations Board] doesn't merely authorize the existence of unions, it regulates the whole employment relationship. Affirmative action

laws do the same thing. There are large amounts of money lost due to these regulations.

I realize that it seems like nothing compared to the problems of total government budgets, but I am not sure that the figures don't loom large even compared to those figures if you do the calculations correctly.

Then look at state regulations that cover a lot of the same things. There are an enormous number of regulations for zoning and land use planning. I have never heard an authoritative estimate of what the total real cost of land use planning in the United States is, but I would bet that it is in the order of \$10 billion a year.

And there are all the things the courts do. In recent years, they have gone absolutely crazy with product liability and medical malpractice, just to name two things. Under no stretch of the imagination can these be seen as efficiency-producing rules. They have been extremely costly. They need to be included in here.

There is the whole range of constitutional law which has been very costly. A lot of it gets talked about in terms of civil liberties or political freedoms or what have you. It also has gigantic costs that are far-reaching.

Well, the list could go on indefinitely. Pick up a catalogue of any modern law school and you will see what's involved.

Just mentioning that kind of issue brings to the fore the great difficulty in making comparisons along cross-cultural, cross-national lines. Even getting the absolute figures for one economy is going to be difficult enough. Standardizing it in some way...it is just hard to imagine. This is why I constantly return to a different kind of measure entirely. One that doesn't look at these inputs, but looks in an aggregate sense at some sort of wealth measure as probably the closest we are going to come.

I realize now after the discussion, particularly of this morning, that there is another agenda here, and that merely coming up with the best measure, even if I were right in saying that it's a wealth measure, doesn't accomplish what we are aiming at here. We are looking at these inputs, as I call them, as goals that we would like to see maximized or minimized.

Henri LePage I would like to make a modest proposal. I propose a semantic change of this list's title. What strikes me when I look at the list is that I don't think it is really "measures of freedom" in the strictest sense. I would rather call it measures of how countries perform relative to freedom. We are not really measuring freedom...I don't want to reopen a whole discussion that we have had for these two days, but I personally believe that people in this room ought to sum up the issues and debates that we have had yesterday.

David Friedman I want to do something related to the strategy my father was suggesting. Whether this strategy is likely to work will depend on one of two conditions. Either the different elements that go into restricting economic freedom are so closely correlated that measuring the most easily measured one does pretty well for all of them, or the easily measured one is such a large part of the total that it dominates the results. You can determine whether the first condition holds by taking all measurable things you can think of and running correlations among them to see if they are highly correlated or not. If they are, just pick whichever one is likely to be the easiest to measure. On the second condition, one thing that was not included in the handout was that in addition to my set of eight different elements, I also gave values for the constants K1 through K7. Those are guesses, conjectural weights that I found by introspection, a good Austrian method. I asked myself in each case questions such as, if I had to choose between having the government tax away 20 percent of my income or getting my full income but having to spend one day out of five at a job chosen by the government, such as being in the army, which would I prefer? My answers give me a rough measure of the size of the cost to me of forced slavery (putting aside the underpaying), as opposed to taxes. That's an interesting exercise, and after doing that it might be fun to see whether government expenditure is going to be 80 percent of the loss of freedom when all is added up. If so, let's forget about the rest and just measure that.

Milton Friedman Don't you want to make an inverse measure?

David Friedman A measure of loss of freedom?

Milton Friedman As the measure of all these things gets higher, you have less freedom.

David Friedman You're right. They are a measure of loss of freedom.

Robert Poole I want to comment on the political acceptability of what may come out of this process; this is a subject that has come up a few times today and is very relevant in terms of the Freedom House context.

Among the long list of things that Henry recited, which most of us here would agree are restrictions on economic freedom and have significant costs, there are many things considered controversial today even in parts of the economics profession, and certainly in the world of public policy they are not considered established or accepted. It is crucial to begin improving on Freedom House's measure of economic freedom. I suggest, therefore, that we look at this whole process as something that is planned to evolve over time. Not simply getting more accurate as Milton suggests, but also consciously starting with measures that are widely accepted within at least the economics profession—such as

free trade and private property, which even Freedom House accepts as relevant, and a handful of other things—and try to come up with a relatively small number of indicators that can be measured, for which there are data available.

That would be a giant step forward compared to what Freedom House has done. It would not get us involved in controversies over whether things like securities regulation are good or bad and a loss to the economy, which is going to greatly hamper widespread initial acceptance of the exercise.

James Ahiakpor I want to put forward reactions to some of the measures so that those who will work on them might give them more detailed consideration. One is number 16, emigration rate as a ratio of the birth rate. I suspect that the emphasis behind this is the thought that people leave because things are terrible at home. But there could also be pull factors. Things may be happening so well outside that they would decide to move. So emigration need not necessarily imply terrible conditions at home.

David Friedman And one reason for people not leaving may be that they are shot if they try.

James Ahiakpor Another one, number 21, inflation rate during the last five years. Again I suspect the thinking behind this is that the government may have been using inflation as a tax. Yet if inflation was open, it might be much better than if suppressed and therefore statistically it appears to be small. And so, when suppressed, we have an additional restriction on exchange through the price control mechanism. Therefore, the inflation rate per se should not be used as an indicator of restriction on economic freedom.

Number 13, price relatives as a measure of regulatory restriction. I don't know why relative prices should be used as any indicator of economic freedom or lack thereof. Differences in productivity across countries may explain price relatives.

Milton Friedman Not if you have a unified world. They may explain which countries produce what.

James Ahiakpor The wedge may be coming from tariffs, and if so, let's use tariffs rather than price relatives. Take the case of wages. Some people may think wage differences indicate a lack of economic freedom. They may have the notion that there is such a thing as a labour theory of value and that labour on the streets of Nigeria should command the same as on the streets of New York. But such reasoning ignores the fact that labour productivities are different because there are different amounts of capital in the two places.

Milton Friedman That's because you don't have free movement of labour. If you had free movement of goods, then only transportation costs would prevent the same price from prevailing all over. Tariffs and import restraints are very hard to measure. You have a much better measure of the freedom of foreign trade by some measure of how far you are from a one-price world than you do by looking at tariffs directly.

James Ahiakpor Therefore, the existence of non-tradeable goods, like services, would be creating ambiguities.

Milton Friedman Yes, sure.

James Ahiakpor Lastly, on property rights, I think we want to find some measurements that follow what Bob has just said. It is a concept. How are property rights guaranteed or violated? Let's find some indicators for that.

Richard McKenzie It seems to me that there is a good deal of consensus that somehow government involvement in the economy is a key indicator of freedom. Perhaps the Fraser Institute might back off a bit from the freedom thing and measure just how big government is to see if, in fact, one can come up with the total cost of government, including expenditures, some things that Henry listed, and foreign trade. It seems to me that would be an immensely useful thing. Not only for the future development of a freedom index but it would also be something that would solve Bob's problem. Once you start throwing anti-trust into a freedom index, it is immediately an explosive sort of thing. But if you just try and say, "all we want to know is how much does government account for in the economy," it becomes a kind of scientifically neutral adding process. And then you can use that figure, of course, to relate to GNP and growth rates.

Henry Manne You can allow people to put plus signs on some government involvement.

David Friedman The problem, it seems to me, is that if you use the net cost, you are then back with all the political arguments that we are trying to avoid. Henry and I may agree that the Williams Act has a high negative cost but Congressman Williams wouldn't agree with that proposition.

Milton Friedman Why? He's in jail. (laughter)

Robert Poole Just add up those things that people are doing at the behest of government.

David Friedman But what about the benefits? Take the person who says that the Williams Act prevents take-over bids that wreck well-established firms merely to make short-run gains for wicked, greedy speculators, or whatever the current line is. I don't see how you are going to do anything about persuading people who don't agree with us if you build an index that has all of our debatable political opinions built into it.

Henry Manne The other side lists affirmative action as a plus. Same thing.

Voice But I don't think our objective is to pick a fight.

Henry Manne I don't think we should advance it as a fight. We should advance it as the best scholarship available for measuring the cost of what the government is doing.

Robert Poole It may be too expensive to come up with this figure. Even if you take the total government budget, you have already picked a fight right off the bat, because there are some things government does that I would agree with.

David Friedman That gets to the point that I was making a long time ago—that what you want to try to do is to have some way of separating costs and benefits rather than netting them. Everybody would agree, it seems to me, that the time and effort businesses spend complying with regulations are costs, even to those in favour of the regulations. Suppose you had a definition of cost where you didn't say the Williams Act was a cost, because although it wrecks the market for corporate control, not everyone agrees that it does. You just said, “what is the total amount of resources directly spent either by government or people doing things the government tells them to do.” The liberals think that for each billion dollars of that, we get, say, \$10 billion in benefit. Fine. If they are right then we will observe that countries in which that cost is higher are rich countries. We think it is the other way around and we expect to observe the opposite.

Robert Poole You are saying what I was trying to say.

David Friedman But all I am saying is that many of the things that Henry wants to include on a net basis must be left out because they represent our opinions about negative benefits for things that others think are positive. But we can both agree on positive costs.

Henry Manne Where is this list of things that we can all agree on?

Ellen Paul Dick, I wonder how you are going to measure the cost of government in communist countries? How do you measure 30 or 40 million people slaughtered under Stalin? How do you measure where the Soviet Union, or rather, where Russia would be today had it not been for the Bolshevik Revolution?

Milton Friedman That's easy.

Ellen Paul Do you have a number for us?

Milton Friedman Sure, I could get you one if you give me a few minutes. I simply extrapolate the rate of growth between 1890 and 1913, which was very rapid, and extrapolate that for another 70 years and you'll be roughly where they would have been.

Henry Manne Nobody maintained that rate for that long.

Milton Friedman I don't believe that's right. I don't believe it was that large.

Henry Manne Theirs was the fastest.

Milton Friedman Fastest for Russia?

Henry Manne No, one of the fastest in the world.

Milton Friedman I didn't think it was. Okay, take the profile of the rate of growth of the United States and superimpose it on that segment of growth and then extrapolate it.

Henry Manne Now you are coming very close to the test I suggested at the very outset.

Milton Friedman That's a test of a different question. Ellen is asking what their GNP would be, not what their freedom would be.

Henry Manne She has raised the point of how you are going to make cross-national comparisons.

Ellen Paul Especially for alien, barbaric, or communist systems.

Richard McKenzie I just want to refresh our memory of Walter's maxim. That is, "anything worth doing is worth doing imperfectly." All I am suggesting is that we seem to agree that somehow government involvement is important, so we

could start off by using government outlays as a proxy for government involvement, and then the first step that the Fraser Institute might want to undertake is determining what ways seem fairly reasonable and fairly economical and what can be improved upon.

Ellen Paul How can you compare things in countries that are de facto slave labour camps?

Richard McKenzie We rule them out for the same reason we rule out the Third World. The data is pretty sloppy or things get too difficult or they are just incomparable. I would think that the Fraser Institute would want to start off by calculating this measure for Canada, then maybe expanding it to the United States and the OECD [Organisation for Economic Co-operation and Development].

Ellen Paul But how is that going to apply to Cambodia where you have a regime that murdered half of its population?

Rose Friedman It just seems to me that the examples you are giving are so obvious that you don't need a measure to prove that Russia is not a free country.

Ellen Paul Then what are we doing all this for?

Rose Friedman Well, because there are a lot of countries in between the purely free and slave status. This includes the United States, Canada, and a lot of other countries where you have a significant amount of freedom. The question is, what elements in these countries produce more freedom and what produce less. You don't have to go to Russia.

Henry Manne I am very much warming up to Dick McKenzie's suggestion. It seems to me that the notion of preparing some kind of a government cost index might be, even from a pragmatic point of view, more interesting than an economic freedom index. We realize it may be the same thing, in large measure, but it also suggests that you could encourage economists the country over, the world over, to begin to spend their time costing out some of these things. We don't do it now.

Milton Friedman There's a lot of it being done. It has been done for tariffs. It has been done for business regulation.

Henry Manne In some areas there is. But entire areas of business regulation remain untouched.

Milton Friedman You have Weidenbaum's estimates of the total cost of regulation of other kinds.

Henry Manne He was very successful with a bad job. What I am suggesting is a much better job. A much broader concept. Not just looking at regulation but also looking at some of the broader consequences of tax laws, tariff laws, and everything else.

Milton Friedman And there have been some estimates of the amount of time people spend filling out forms. Which is far from trivial.

Henry Manne You could create something that would get press every year, because once you created a base number you could then create an index for the year that the government cost us more or less on the index this year. Sort of like the inflation rate.

Milton Friedman We have one of those. I invented it and it has been developed as Tax Freedom Day.

Zane Spindler Milton just made one of the points that I was going to make. Mike Walker and Sally Pipes already calculate a tax freedom day for Canada. That gives a very simple and understandable way of measuring economic freedom. One could conceive of enticing researchers in other countries to undertake that same sort of calculation. However, it seems to me that even though the costs may now be much less than they were originally, it is still a fairly costly estimate to produce.

The second thing I would like to do is ask Henri LePage to elaborate on what he thinks should be measured with respect to his concept of property rights as liberty or freedom. That is, if he were to choose the sole indicator, or the set of indicators, of whether a country met his standard, what would he choose?

Robert Poole A quick comment on Ellen's point. Although things like mass murders and slave labour impinge on economic liberty, they are already incorporated into Freedom House's ratings of political freedoms and civil liberties. The Soviet Union and those other countries are all rated in the black category on those indicators now, so I don't think that's what we really need to worry about. We need to be worrying about whether in a country like the Soviet Union one can own property or not and whether one can start a business or not.

Ellen Paul I agree with you. But in Dick's model it does make a difference, because we want to calculate the costs of government. Well, putting 30 million people in slave labour camps is a cost of government. Taking the land of 6

million kulaks and driving them to their deaths in Siberia is an economic cost. If you are going to calculate economic costs, you have to add these in too.

Michael Walker Just a simple point. There seems to be two different kinds of measures that have been suggested. One is direct measures of the size of government relative to the economy. The other is indirect, for example, price relatives that are a kind of reduced form. We should bear in mind that we are more likely going to achieve success and acceptance with those kinds of measures, as well as have more luck in calculating them. For example, it is almost impossible to calculate the total burden of agricultural regulation. But it is very simple to calculate what the consequences of this policy are, relative to the regulated world price for commodities. Rather than moving in the direction of trying to calculate the total burden of regulation and the total cost of government, we are going to have to look at what the consequences of those things are.

Richard McKenzie I cannot go along with Michael on that. The reason for this measure is to ask how it relates to consequences. But if you include the value of the consequences in the measure, then you are going to have a problem. We have to be a bit more neutral on this. When you start calculating the cost of government, you are talking about consequences right there, right off the bat.

I am really suggesting that we ask such questions as, can we improve upon government spending divided by GNP as an indicator? Can we improve upon that by simply adding in some other things? What other things can be added in fairly easily? I personally could find that kind of measure immensely useful in a lot of contexts and I might find it useful in the further development of the Fraser Freedom Index.

David Friedman At this point we are talking about creating an index that most people, including those who disagree with us about the value of economic freedom, will agree measures economic freedom. Any disagreement with us will then show up in different predictions about what the index measures imply about countries.

We want to measure the cost of government in a way that does not depend on our opinion that Russia would be better off if it were capitalist, and the U.S. would be better off if it were capitalist too. We want something that everyone agrees is a sort of accounting measure. What did government spend? What did people spend complying? Things like that. Then the political argument becomes one about whether countries with high economic freedom are well off or badly off as a result. Since, to a considerable degree, both sides agree on how to measure the standard of living—GNP, life expectancy, etc.—the argument then becomes an empirical one. We don't want to start by asking what, in our opinion, is the full cost of government, because in order to answer that question we would

first have to settle the argument that the index we are creating is supposed to help us settle.

One particular problem on this question of cost relatives is that if you are including government spending, if there is a tariff on rice, and if you include your cost relative, then you are double-counting on the imported rice. The extra dollar that the Japanese citizen pays for imported rice is just a tax going into government expenditure, while the extra dollar a Japanese citizen pays for domestic rice is not a net burden. So you have a bit of a problem doing your calculations correctly for tariffs. You really want to look at the higher price for domestic goods but not the higher price paid on imported goods. In principle, you would also like to include the excess burden on the goods that, because of the tariff, are not insured, but I don't know how to measure that.

Milton Friedman I don't think you want to combine these. You are talking about two dimensions of freedom—domestic and international.

Michael Walker Just to respond to Richard's point, I don't think that the fact that you are using price relatives necessarily means that you are going to get involved in the problem of measuring a thing that you then want to compare it to. Suppose you are going to a sectoral indicator, let's say of how free the agricultural sector is and how free the market for corporate control is or whatever, prices in those sectors relative to a free market price convey information about the extent of interference. This is particularly useful for measuring interference in very underdeveloped countries where typically the government is getting most of its tax revenues through the aegis of a marketing board. It buys the agricultural product and places an implicit tax on the difference between the price at which it buys and the price it sells. The difference in the prices is a barometer of the restraint that the government is imposing on the system without in any way double counting.

Henry Manne I think David has left us with an empty box. Apart from the tariff issue, you will find no manner of government expenditure, direct or indirect, that some people won't justify and defend.

David Friedman I am not arguing about whether you justify it, I am arguing about whether it's a cost. When I buy dinner we can both agree that it's a cost, even if it wasn't a good dinner.

Henry Manne You will find more agreement on the cost of the Williams Act, for instance, than you will on affirmative action. On affirmative action, people begin to bring in a variety of subjective matters that you really can't argue about. That's why I say I'd go very strongly with Dick's proposal to publicize what these government activities cost. We shouldn't deny that there may be benefits. I

realize what I am saying, that we're not giving a net answer. But at least from year to year you have some base on which you could describe whether it was getting worse or better. In that way there would also be some possibility of extending the analysis to other countries.

Richard McKenzie Maybe this will clarify what I had in mind. It seems to me that we started out with the proposition that somehow government expenditure is related to wealth and growth in wealth. What we want to do is include the government expenditures in the agriculture sector. I don't think we want to necessarily include the impact of those expenditures, i.e., the negative impact of output in the agriculture sector, simply because we would then be incorporating into our measure of government that which we are trying to link to government. The impact of government expenditures should be related to the impairment of growth that is reflected in agriculture.

What I have in mind is to include in government those rules that require people to do something that government could have done by simply paying them to do. We don't want to necessarily include all the ramifications, all the negative consequences, of what people are required to do. We see people out there filling out forms, we want to include that because it is a use of time that could have been bought by government expenditures and it is a reasonable cost of government. But we don't want to include all the lost GNP filling out forms. I may be being fuzzy on this...and the reason is because if we include all the loss of GNP and all the ramifications of that, then we have the problem of linking this cost of government to wealth maximization or whatever.

William Hammett One thing I am curious about and Antonio might know: in Italy there is a welter of economic regulations, but people seem to get around them. What is the secret there?

Antonio Martino That's why I was saying that inefficiency of government is an essential component of economic freedom.

William Hammett Italy has a lot of entrepreneurship. It seems to percolate throughout the country, even though on paper the economy looks quite bad.

How would our rating system work? In the early years of running this survey, could you hedge it by just doing the colour-code thing—black, grey, white, purple, or whatever, and then refine your measurements over the first two or three years but basically use these categories? Would people ask how you derived the categories? We may use a number of measurements, but basically the categories would be: free, relatively free, relatively unfree, and definitely unfree, or something on that order.

Henri LePage I propose another measure: the ratio of the number of tax audits to the population of taxpayers. I do this for one very simple reason. The cost of the time we use for filling out government forms was mentioned. But there is also another heavy cost—psychological manipulation. I have personal experience of this through my wife, who had a small company and a long-lasting tax audit. People can go bankrupt just because of the psychological strain that is imposed upon them by tax audits.

Charles Murray After this long discussion about government spending I want to state for the record that I am still very excited by the notion of putting together a rating of economic freedom based on trying to measure the degree to which people are free to engage in transactions and keep their money. I simply want to tell Alvin that some of us still think that it is a good idea and don't agree with the notion of relying on government expenditures.

Milton Friedman As far as Charles is concerned, what he just said is that one minus the ratio of government spending to income is what he is asking for. What fraction of money can people spend on their own? From that point of view government spending ought to include mandated expenditures.

We must remember that there is another wholly different kind of evidence that we haven't been looking at. That is qualitative evidence. Ellen is clear about whether communist countries are free or not. So am I. Lots of people have had direct experience with more than one society. We have people like James, who has lived in Canada and Ghana. If I ask him, which is freer?, how long will it take to give me an answer?

James Ahiakpor One second.

Milton Friedman If I was doing this research, I would begin in a direct way along the lines I suggested earlier, with some preliminary measure to get me started; next, I would talk to informed people and get a qualitative ranking of pairs of countries that people know. I would try to find people who know a good deal about both France and Germany, France and England, and so on, and ask them their considered opinion. Then I would look at my charts and ask, where do I have points that don't fit into this ranking?

Let's suppose Canada has a much higher ratio of government spending to income than Ghana does and James tells me I am nuts if I think that means Ghana is freer than Canada. Then I know there is something wrong with my method of measurement and I have to do something about it. I am then led to ask the right questions. What is there about Ghana that restricts freedom that doesn't show up in my measure? It might turn out to be the ratio of the size of the top marginal tax rate or something else. At least it will get me going in the right direction. But if I just stick to these numbers, I am going to get enmeshed in them. I have to have

some kind of outside, qualitative information that will tell me whether I am going in the right direction or not. That's all I was suggesting. It seems to me that is an enormously important part of any such project.

David Friedman I have a comment based on this particular line of thought. There are two different strategies we might take. One is to tell the world that what we are measuring is a good thing that everybody likes. Economic freedom sounds good and it turns out to relate to other good things. The problem with this strategy is that after we construct our definition of economic freedom, people on the other side will say, "why didn't you include the right to a decent house?"

The other strategy is to describe it as something everyone knows that people with our political bias are in favour of, call it market freedom. We are in favour of the free market. Many liberals would say that they are not entirely in favour of free markets. Everybody can agree that this is what *laissez-faire* types are in favour of, and come to an agreement of how *laissez-faire* can be measured. Then we point out that countries that measure high in this also have high rates of economic growth. And that will be evidence in favour of our position.

I just want to make the distinction between those two kinds of strategies. In one you try to gain widespread acceptance by calling what you measure something even those who oppose you think they favour. The problem with this is that you have to cheat because you will be using a definition that has some of your biases in it. The other way, you make it explicit that you are defining a particular view of what economic freedom is, a view you know perfectly well they don't agree with, and you therefore call it something different. Then both sides agree about the measurement, and the interesting question is whether what you measure correlates with things they like, such as high incomes.

James Ahiakpor Just to add to Milton's point. I have been documenting information on Ghana, and have found that when it was really not free—people were being shot for all kinds of things in 1982—government spending was around 10 or 11 percent. Thus, what I have found is that using the share of deficit spending to total government expenditure might help to compensate for what is missing. Sometimes government restrictions on marketing activities, like price controls, would lead to government revenue shrinking and driving the economy underground. It is therefore important not to rely solely on the published numbers.

Milton Friedman What about the number of people who are shot or are in prison as a fraction of the population?

David Friedman Is that political rather than economic?

Milton Friedman No. That's economic freedom. My life is my property.

James Ahiakpor Well, sometimes you don't get an accurate count of the number of people shot or imprisoned. But for deficit spending, you can easily take it from the national financial statistics published by the IMF. You might say that this is also a little fuzzy, but it is more accurate than the number of people who might lose their lives in times of turmoil.

So now the share of government spending in Ghana has increased because there has been more freedom in marketing activities. The government can now collect more revenue, and deficit spending has also shrunk along with increased economic growth.

Milton Friedman You see, Ghana is in the first part of the table. It is way back down there...low per capita income, low ratio of government spending.

James Ahiakpor The other part is that if you look at World Bank publications, middle and high income countries have higher government spending than really poor countries. So that makes a strong case for using qualitative sources to embellish the analysis.

Alvin Rabushka Walter, I want to take over your role of chairman for about 20 seconds and see if I can get Antonio to tell the conference what he said to me privately, about the fact that no one has mentioned money during this entire conference.

I tried to include the monetary system as a dimension to consider, and would like to know what the people here think about the relationship of a particular monetary system to economic freedom. That is, does a monetary system enter into a government cost system in some way? Would any particular monetary system be more conducive to less government cost or to more freedom?

Antonio Martino I think the abuse of the monetary system is a way to raise government revenues and to interfere with economic freedom, so that should enter into our index.

Also, let me mention two alternatives to the national currency, whether in the form of holding foreign currencies or investing in foreign countries. Those should enter into the picture as well. If we had competing private currencies, it would be nice to see departures from that kind of model. Unfortunately, we don't, but we do have internationally competing currencies. The possibility of having part of your assets in foreign currencies is certainly a dimension of freedom. That was what I really had in mind.

Zane Spindler What my paper states on this is that basically the inflation rate is a measure of redistribution between individuals within the country and hence is not of as much concern in aggregate unless, of course, it is not stable, and not anticipated.

Milton Friedman It is not a measure of redistribution. Only if it is unstable.

Zane Spindler That's right. But if it is unstable and therefore not predictable, it may also lead to an extra tax on cash balances as people shift from holding money. So unanticipated inflation is at one and the same with extra taxation. But it is also confiscation of private property. Thus, any property measure has to consider inflation as affecting the value of the property just the same as regulation or other takings.

Milton Friedman You can only count confiscation if it is not expected.

Zane Spindler That's what I am talking about. The unexpected component.

Milton Friedman But not so far as Antonio's suggestion is concerned; if you use government spending instead of taxes, you have included what he is talking about.

Antonio Martino What I really had in mind was the profitability of inflation; the fact that income brackets are indexed for tax purposes. We must also consider the availability of long- or short-term bonds that act as protection from inflation.

James Ahiakpor Regarding Alvin's points on the monetary systems, this question is like opening Pandora's box because monetary experts are not decided on it. I don't think, and this is going to provoke some eyebrow raising, that government control of the issue of money is really that much of a violation of freedom. Those who want private banking merely oppose government's use of the monetary system to collect taxes that they cannot collect openly, namely the inflationary tax. When you think about it, financial institutions are in effect issuing their own medium of exchange in the form of credit cards and chequing facilities. The fact that we can all use those media, ultimately redeemable in cash, and sometimes not even redeemable, simply means that the banking system can credit or debit people's accounts using a plastic card or other pieces of paper. What we really ought to be concerned about is whether we have exchange controls, regulation of banks, and regulation of interest rates according to categories of financial assets. Those would easily imply a diminution of economic freedom. It's irrelevant that it's only the government that prints currency.

Michael Walker We all took note when James said that the number of people who were killed in Ghana wasn't altogether evident, and that the people who prepared the statistics had incentive to hide this. I think we are silly not to recognize that we have exactly the same problem in trying to calculate the amount of agricultural subsidy. Similarly, the people who are using that process to rent-seek have been very skilful in manipulating the process so that they don't leave any smoking guns. For that reason we may have a lot of these cases, particularly if we are interested in calculating an impact of the regulatory burden. We may have to rely on indirect rather than direct measures.

Alvin Rabushka Compared with the first session, in which we heard a number of impossibility theorems and/or undesirability theorems and/or just wrong-headed theorems, what happened in this last session is that we have picked the minds of the best and the brightest, and we now have a number of alternative strategies and approaches expressed with some conviction and enthusiasm. These include government cost indices or some simple notions that can be added to it in a variety of ways to calculate data sets. We have come up from the bottom and more or less are going out on top of the cloud. I am quite happy with the thrust of the discussion of this last session.

Walter Block Although this is not strictly in keeping with the usual practice of the Liberty Fund, I'd like to call on Dub Hill to make some closing remarks.

Dub Hill I enjoyed listening to the discussions. At times I could relate to how frustrated you may be in seeking some consensus. Though most of us feel a strong commitment to a society of free and responsible individuals, it is sometimes difficult to define that exactly. Most of us are committed to a system of private competitive capitalism. This system is the one that will provide the highest standard of living and the best chance for a society of free and responsible individuals. Like Walter and Alvin, I am inclined to believe that if we could focus attention on economic freedom, we might get more of it. And if we had some sort of an index that had a measure of credibility, it might focus attention on this issue. People might begin to argue over who has the most economic freedom. This perhaps is expecting too much. I don't know what will come of this. Although I can't speak for the Board yet, I think the Liberty Fund would be interested in pursuing this matter. I hope you have enjoyed the conference. Perhaps it will produce some meaningful result. Thanks for being here.

Walter Block Thanks Dub. I hereby declare that this conference is at an end.