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Not rocket science

By Richard W. Rahn
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Suppose you were appointed global economic czar, and your task was to bring the world's per capita income up to the level of Ireland's (almost that of the U.S.). Would you:

(A) Insist the world's rich nations transfer substantial wealth though massive foreign aid to the poor nations?

(B) Insist all nations adopt policies that would make them as economically free as the top 10 freest economies today?

If you answered "B," go to the head of the class. This shows you have a good understanding of both history and economic reality about what works and what doesn't.

If you answered "A," welcome to the Kofi Annan, Jacques Chirac, Gerhard Schroeder school of willful economic ignorance. Graduates of this school are well represented among international institutions, such as the World Bank, and the Organization for Economic Cooperation and Development; the political left; and the media elites in such places as the New York Times editorial pages, the BBC and National Public Radio.

Fortunately, in their effort to roll back economic ignorance, the Heritage Foundation and the Wall Street Journal produce an annual "Index of Economic Freedom." Their 2006 Index, the 12th edition, has just been released, and again it shows in stark and unambiguous terms that income, economic growth and opportunity are highly correlated with economic freedom. The economically freest societies are the most prosperous, and the most economically repressive societies are the poorest.

The principal authors of the Heritage/WSJ Index -- Marc Miles, Kim Holmes and Mary Anastasia O'Grady -- use commonly accepted definitions of economic freedom, including trade and capital flow restrictions, levels of taxation, size of government relative to the economy, price stability, levels of economic regulation, protection of private property, etc.

Ireland 30 years ago was among the poorest countries in Europe. It then made a major shift toward freeing up its economy -- e.g., its maximum corporate tax rate is only 121/2 percent (it ranks No. 3 out of 157 countries in the index). As a result, it now has the second-highest per capita income in Europe and is far ahead of the old leaders like

Germany (No. 19) and France (No. 44). (Note, when I refer to per capita income, I do so using the Purchasing Power Parity measure which accounts for local price differences.)

In Eastern Europe, Estonia is economically the freest (No. 7), and Romania the least free (No. 92), though the latter is now making progress. Both countries started out at roughly the same level 16 years ago, but now Estonia has almost twice the per capita income of Romania. Much of the credit for Estonia being the most successful transition country goes to its brilliant and able free-market former prime minister, Mart Laar.

China, Taiwan and Hong Kong make an interesting case study. They are all inhabited by Chinese in the same part of the world. In 1947, they were all equally poor, but Hong Kong (No. 1) started its economic reforms in the 1950s, and a decade later Taiwan (No. 37) began major reforms, but China (No. 111) proper did not begin its reforms until the late 1970s.

The result is that Hong Kong has a per capita income almost threefold that of China (accomplished without natural resources or foreign aid), and Taiwan has more than 21/2 times the per capita income of China.

In central Africa, we have the contrast between Botswana (No. 30) and Zimbabwe (No. 154). Botswana, a relatively free market democracy, has roughly tenfold the per capita income (without U.S. aid) of the repressive Zimbabwe, despite having started at about the same level of development.

Latin America gives the interesting contrast of free Chile (No. 14) and repressed Cuba (No. 150). Chile's per capita income is now about 21/2 times Cuba's, though Cuba was far richer than Chile before Fidel Castro came to power and Cuba received massive aid from the old Soviet Union and now Venezuela.

Mexico (No. 60) has a per capita income about one-quarter the U.S. (No. 9). It is a reasonable bet that had Mexico been as economically free as Canada (No. 12) its per capita income would be high enough that Mexicans would prefer to stay in Mexico rather than move to the U.S.

On the other hand, the biggest recipients of development aid over the last quarter-century, for the most part, have gone nowhere economically. Egypt (No. 129), the biggest recipient of development aid in the last quarter-century, is a prime example, with a per capita income about 5 percent of Ireland's.

The lesson is clear for all who will remove their ideological blinders that the road to prosperity is economic freedom, not development aid. International institutions and major donor countries should stop handouts and pressure laggard countries to make free market reforms. But then, of course, international aid bureaucrats would be jobless. What a pity.

Richard W. Rahn is director general of the Center for Global Economic Growth, a project of the FreedomWorks Foundation.