Evidence on Technological Change

Measures of Economic Freedom

- Heritage Foundation / Wall Street Journal
- Quantifies Economic Freedom
- Look at the Relation between a nation’s income and level of Economic Freedom.

Measures of Economic Freedom

- Trade policy:
  - Are there tariffs and other barriers to trade?

Measures of Economic Freedom

- Trade policy:
- Taxation:
- Government intervention in the economy:
  - Does the government own businesses? What is the size of government consumption relative to the size of the economy?

Measures of Economic Freedom

- Trade policy:
- Taxation:
- Government intervention in the economy:
  - Does the government own banks? Does the government influence who gets loans? Are there other regulations?

Measures of Economic Freedom

- Trade policy:
- Taxation:
- Government intervention in the economy:
  - Banking:
  - Property rights:
  - Is there corruption in the court system? Are there laws governing contracts? Is there protection from government or private seizure of property?
Measures of Economic Freedom

- Trade policy:
- Taxation:
- Government intervention in the economy:
- Banking:
- Property rights:

For each factor, the Heritage Foundation assigns a score of 1 (good) to 5 (bad). The national score is an average of their 10 scores.

Selected Scores

<table>
<thead>
<tr>
<th>Country</th>
<th>Economic Freedom Index</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hong Kong</td>
<td>1.25</td>
</tr>
<tr>
<td>Switzerland</td>
<td>1.65</td>
</tr>
<tr>
<td>United States</td>
<td>1.90</td>
</tr>
<tr>
<td>Japan</td>
<td>2.05</td>
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<tr>
<td>Germany</td>
<td>2.30</td>
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<tr>
<td>South Korea</td>
<td>2.40</td>
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<tr>
<td>Poland</td>
<td>2.95</td>
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<tr>
<td>Bulgaria</td>
<td>3.45</td>
</tr>
<tr>
<td>North Korea</td>
<td>5.00</td>
</tr>
</tbody>
</table>

A Graph

Per Capita Income vs. Economic Freedom

A Comparison

- Before WWII, North and South Korea were united (as a Japanese colony).
  - Today, North Korea has a per capita income of $900.
  - South Korea is $13,193

Caveats

- Some of the factors are questionable.
- A common theme: protection of property rights.

Back to Miller’s Pizzeria

- Miller’s Pizzeria is located in Backwater
- Backwater has low levels of economic freedom and income.
- Suppose that a political revolution bring Backwater’s Index of Economic Freedom up to that of the United States.
  - We would expect Backwater’s standard of living to move up to that of the United States over time.
Applying to Miller’s Pizzeria

• The owner will greet the revolution cautiously.
  – Political revolutions promising "new eras" come and go.
  – People must trust that there is economic freedom.

Applying to Miller’s Pizzeria

• The owner will greet the changes cautiously.
  • The Pizzeria is under capitalized.
  – Its pizza ovens are something from the Dark Ages
  – It has an uninviting appearance; an improved appearance will simply attract the tax collector.
  – All of these problems can be fixed with a capital infusion, but it will take time.

Applying to Miller’s Pizzeria

• The owner will greet the changes cautiously.
  • The owner has not kept abreast of new advances.
  – Why bother? Now, he will. But it will take time.

Applying to Miller’s Pizzeria

• The owner will greet the changes cautiously.
  • Because of the heavy regulation, the Pizzeria is under capitalized.
  • The owner has not kept abreast of new advances.
  • His staff will require time to learn new skills.

A Summary

• Economic Freedom is the key
• Don’t worry too much about Heritage Foundation Numbers.

End

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