

What's New in the 2008 Index?

Every year, the editors evaluate the *Index of Economic Freedom* and consider ways to improve the product. This year's edition of the *Index* continues the substance and style of the 2007 edition with a renewed emphasis on a more scientific and objective methodology coupled with an accessible format. There are few dramatic changes in the 2008 *Index*, but there are a number of important refinements.

These changes continue the Heritage Foundation/*Wall Street Journal* tradition of year-by-year improvement. For example, changes in the methodology were instituted in 2000, 2002, 2004, 2006, and 2007 to enhance the robustness of one or more of the 10 factors that are used to measure overall economic freedom. Each time, the entire time series is revised so that all scores are as consistent as possible, dating back to 1995. Our goal is to make the *Index* a resource that is credible, usable, and relevant to a changing world, with new data and knowledge, while also consistent with our heritage.

A more detailed explanation of what has

changed, as well as what has not changed, in the 2008 *Index* follows:

- **Free Downloads at www.heritage.org/index.** The *Index* Web site has been revised to include free downloads of each chapter and even each individual country page. These can be used for briefing books, student handouts, or anything else that readers find useful. The Web site also has new audio and video presentations by *Index* scholars, as well as all of the raw data and related research papers.

- **Non-Tariff Barrier Penalty.** The *Index* methodology is consistent with the revisions made in 2007, measuring the same 10 economic freedoms in each economy and using exactly the same underlying data. The only change is a set of refinements in the equations used for three of the 10 freedoms. One of these refinements is in trade freedom, which has always included a penalty for non-tariff barriers (NTBs). Until now, it has been a binary penalty equal to a reduction of 20 percentage points in the trade freedom

score as calculated by tariffs, and thus a reduction of 2 percentage points in a country's total score. The change is that the NTB penalty now ranges in increments of 5 percentage points, up to a 20-percentage point maximum penalty. As a result, a country with moderate import restrictions will have 10 percentage points subtracted from its trade freedom score. This change was also applied retroactively so that previous penalties of 20 percentage points dating back to 1995 were largely reduced to 15 or 10 percentage points. The effect has been to raise overall scores, since the vast majority of countries utilize NTBs and had the penalty in place. This is an improvement in the level of detail that the *Index* provides, allowing greater differentiation and fairness in reflecting economic policies across countries.

• **Taxes and Expenditures.** The introduction of a new methodology in 2007 produced some results that could not be anticipated until grading was completed. One surprise was that average scores for each of the 10 freedoms varied widely. The "best" score was fiscal freedom, which averaged 82.8, but this sent the unintended signal that the area least in need of reform was taxation. Regrettably, tax reform is badly needed in almost all countries, and the creeping size of government taxation and expenditure is a signature reason for the existence of the *Index*. In fact, most economists would agree that the primary area of success in economic governance has been the rise of stable prices and low inflation, largely as a result of independent central banking, implying that the "best" score on average should be in monetary freedom. To remedy the balance among the 10 economic freedoms in the *Index*, an adjustment was made to two equations with no change in the underlying data. Since the equations to calculate scores for financial freedom and government size were producing overly generous scores, the coefficients were tightened in each case. The same equation is used to calculate scores through the entire time series back to 1995, so these changes were made retroactively and seamlessly in past scores. The effect was to lower scores for every country. The overall effect of the higher average scores for trade freedom and lower

average scores for fiscal freedom and government size was neutral.

• **New 10 Freedoms Chart.** Each country page includes two charts. The first shows how the country's overall economic freedom score has changed from 1995 to the present. The second shows, numerically and graphically, the score of each of the 10 freedoms. New this year, this second chart also includes an "up-or-down arrow" that signals the change during the most recent year. For example, you can see that the United States worsened in four freedoms, improved in one other, and is unchanged in the remaining three freedoms. The overall effect was under a full percentage point decline, but these new arrows help to identify exactly what areas are causing the score to slip.

We hope the changes in the *Index* make it an even better research tool and a more accessible policymaking guide. Whatever changes may be made from year to year, however, our goal remains constant: to advance human freedom. We believe that today's *Index* might even make the transition to a better world faster and surer.

One of the editors' paramount concerns is that the *Index* always remains a useful tool for researchers. This means that the integrity of the current-year scores is crucial. During a period of aggressive improvements, there undoubtedly will be mistakes in the scores, based on our errors and errors in source data. We cannot promise perfection, but we do promise objectivity: Our methods and modifications will always be transparent and duplicable by other scholars.

Moreover, even though the *Index* itself is published in January, based on policies and data available as of the previous June, we remain committed to providing the most accurate and up-to-date measures online and will make any needed corrections in that source file immediately. For researchers who want to weight the *Index* or consider individual components in statistical analysis, the 10 freedoms and even the raw data are also available transparently online. Revised scores of individual factors for all years are available for download at www.heritage.org/Index.