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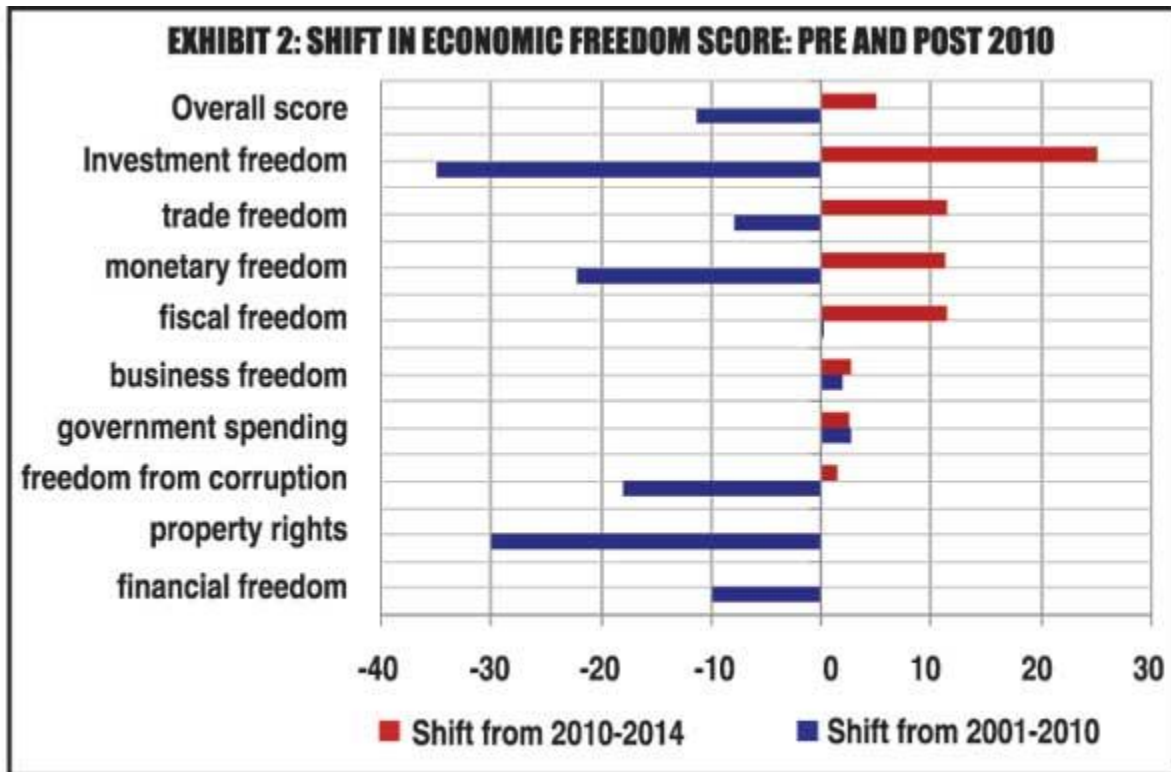
<https://www.dailymirror.lk/features/economic-freedom-in-sri-lanka-changes-and-consequences/185-46798>

Economic freedom in Sri Lanka: Changes and consequences

The US-based Heritage Foundation (HF) has constructed a global index of economic freedom. Sri Lanka's score has improved significantly post-war and declined a bit in 2014. The importance of the index has less to do with overall measures and scores, than the aspects that are changing and the correlation with other important outcomes.

The HF index uses 10 quantitative indicators that are grouped into four broad categories. (1) Rule of Law (property rights, and freedom from corruption), (2) Limited Government (tax burden and revenue and government role in the economy), (3) Regulatory Efficiency (business freedom, labour freedom, monetary freedom) and (4) Open Markets (trade freedom, investment freedom, financial freedom).

Each of the 10 categories is scored out of 100 and the country with the highest average score is ranked one. The average score is used to categorise countries into five groups.



Ups and downs of Sri Lanka’s score on the index

The highest average score that Sri Lanka had was in 2001 (66). Since then the score deteriorated steadily – falling into the “mostly unfree” zone in 2006 and dropping down to a score of 55 in 2010 (Exhibit 1). After the war, Sri Lanka started improving its score getting back up to the “moderately free” zone in 2013, and dropping back down, in the survey of 2014, to the border of the two categories.

Insight 1: What pulled us down was not what pulled us up

The details of what drove these changes provide some insight into changes in the economy in Sri Lanka. From 2001 to 2010 the drop was driven by declining survey results in four aspects: investment freedom, monetary freedom, property rights and freedom from corruption (see Exhibit 2). Post-2010 to 2014 while there was improvement, the areas that improved were not all the same as the areas that had declined.

Recovery areas: Investment freedom which fell from 50 to 15 points (2001-2010) recovered back to a total of 40 points (by 2014). Monetary freedom, which had declined from 79 to 57 points, recovered to 68 points. But the recoveries end there.

No recovery areas: Property rights, which had declined from 70 to 40 points, remained at 40 points even in 2014 and freedom from corruption, which declined from 50 to 32 points; remained in that place at 33.4 points in 2014.

New improvements: However, separately, trade freedom, and fiscal freedom showed significant improvements and helped to improve the overall score; but that is overall in the post-2010 period. Both of these also dipped a bit from 2013 to 2014. The dip in trade freedom is corroborated by a previous Vérite Research Insight titled ‘Sri Lanka’s Trade Liberalisation: What you see is not what you get’. It showed how taxes on international trade applied by Sri Lanka have increased significantly in the recent years.

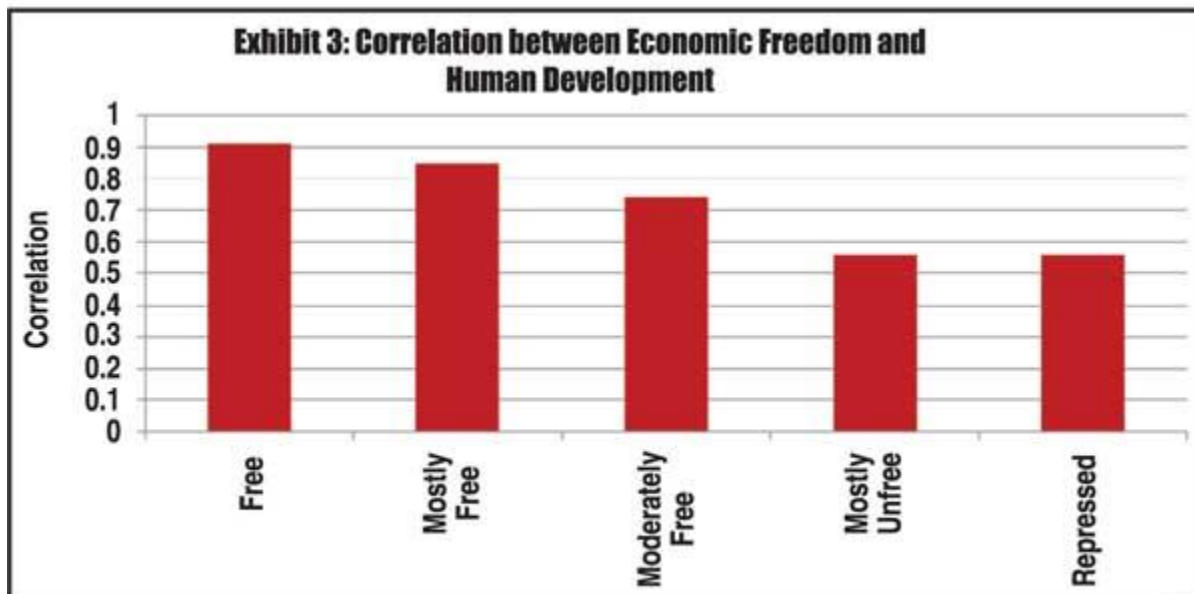
Insight 2: Economic freedom matters for human development

Whatever we make of HF’s economic freedom index, it is important to recognise that higher scores in the index are positively correlated with certain desirable outcomes (Exhibit 3). For instance, countries that fall into the categories of free and mostly free also tend to do much better in the United Nations Human Development index (HDI), than those that fall into the category of mostly unfree (which Sri Lanka is on the border of). And this pattern holds with gross domestic product (GDP) per capita as well.

And indeed, the economic freedom ranking is mostly consistent with Sri Lanka’s GDP per capita and HDI: compared to other South Asian countries it is doing better on its economic freedom score and rank. However, when its economic freedom score is compared to the dynamic economies in South East Asia (with higher HDI and GDP) Sri Lanka ends up being ranked at the bottom of the pile.

ECONOMIC FREEDOM INDEX: COUNTRY CLASSIFICATION

Score	Group	No of Countries	Examples
Above 80	Free	6	Hong Kong, Singapore
Between 70 - 80	Mostly Free	28	USA, South Korea
Between 60 - 70	Moderately Free	56	Thailand, Malaysia
Between 50-60	Mostly Unfree	61	Indonesia, Cambodia
Below 50	Repressed	27	Burma, Zimbabwe



Source: 2014 Index of Economic Freedom, The Heritage Foundation

**Exhibit 1: Declining Economic Freedom:
Sri Lanka moving down from a moderately free
country to a mostly unfree country.**



Source: Economic Freedom Index, the Heritage Foundation

(Verité Research provides strategic analysis and advice for governments and the private sector in Asia. Comments welcome, email insights@veriteresearch.org)