

# WebMemo



Published by The Heritage Foundation

No. 2523  
July 6, 2009

## G-8 Can Stimulate Economic Recovery by Restoring Freedom

*Anthony B. Kim*

In his meeting with President Obama on June 15, Italian Prime Minister Silvio Berlusconi, who will host the G-8 Summit July 8–10 in L'Aquila, Italy, suggested the need to develop “a body of rules and principles” to keep the current economic crisis from repeating in the future.<sup>1</sup> Berlusconi remarked, “We agree that the G-8 itself will not be able to create that body, but, as the Pittsburgh G-20 approaches, we must work to arrive at joint solutions that will not curb the free expansion of the economy.”<sup>2</sup>

The current period of global financial and economic turmoil is a great opportunity to ponder the principles that can revitalize economic growth. Indeed, the urgency to set forth and adhere to sensible principles has increased as a wave of interventionism has seen governments take more control of private companies and even entire industries, wearing away economic freedoms hard won through years of reform.

Policy choices made at this critical juncture of the economic crisis will unquestionably shape the growth trajectory for the world economy in coming years. If Berlusconi and other leaders of the G-8 are serious about developing a set of principles that address the international economic situation in a constructive way, they should begin with a renewed commitment to enhancing economic freedom. After all, the best and most principled approach to move beyond the current crisis is to generate more economic growth and opportunity as quickly as possible.

Exemplifying such commitment, German Chancellor Angela Merkel, who has fended off calls from

the Obama Administration pressuring her government to spend more money to deal with the current crisis, defended her plan to cut taxes in her June 29 speech. Merkel rightly noted that “it would be wrong not to do what is right and necessary for growth, and so prevent ourselves emerging quickly from this crisis.”<sup>3</sup>

Advancing economic freedom is the way not only to fix the institutional infrastructure essential for more vibrant growth but also to swiftly transform today's financial downturn into greater prosperity for the future.

**Time to Stop Expanding Government's Heavy Hand.** By empowering people with unprecedented opportunity, economic freedom has in recent decades generated tremendous success stories around the world. Unfortunately, this success is now at risk. In light of the current financial storm, many have stepped up their direct and indirect campaigns against the free market system. Whether through ideological zeal or simple ignorance and fear, some seem ready—even eager—to abandon the economic freedoms on which world prosperity has been built. Though decades of evidence highlight the negative results of increasing regulatory

This paper, in its entirety, can be found at:  
[www.heritage.org/Research/TradeandEconomicFreedom/wm2523.cfm](http://www.heritage.org/Research/TradeandEconomicFreedom/wm2523.cfm)

Produced by the Center for International  
Trade and Economics (CITE)

Published by The Heritage Foundation  
214 Massachusetts Avenue, NE  
Washington, DC 20002-4999  
(202) 546-4400 • [heritage.org](http://heritage.org)

Nothing written here is to be construed as necessarily reflecting  
the views of The Heritage Foundation or as an attempt to  
aid or hinder the passage of any bill before Congress.

burdens, massive government spending, and nationalization of industry, in a time of crisis some, incredibly, seem to yearn for the heavy hand of government.

That heavy hand, more than any market factor, is the greatest risk to economic dynamism. Governments' rush to fix the perceived causes of the current crisis is increasingly demonstrating the danger that government interventions, rather than fixing economic problems, can actually exacerbate them. Proponents of various bailout programs for troubled companies and industries have argued that those programs are indispensable short-term steps to prop up stock markets and help economies make a swift recovery. Yet the long-run effect of such programs will be counterproductive. Those government interventionist measures essentially rescue and reward those who took irresponsible risks, severely undermining the discipline of the market and eroding economic freedom.

Furthermore, those measures impose an unfair burden on people and businesses that behaved responsibly. They undoubtedly encourage similarly reckless choices in the future. Worse, the bailouts will give the government more political power over the efficient allocation of capital, a detrimental course of action that will surely further undermine overall economic efficiency.

**The World Needs More Economic Freedom, Not Less.** Given the efficiency of the free economy in allocating resources to their most productive use, the most reliable economic recovery can be best achieved by unleashing rather than further constraining market forces. Governments' most effective stimulus package will therefore be about improving the incentives that drive entrepreneurial activity, not undermining it with more layers of regulation.

Although past performance may be no guarantee of future outcomes, it remains the best available guide. Over the past decades, the free market system that is rooted in economic freedom has fueled unprecedented economic growth around the world. From 1980 to 2007, the world economy achieved real GDP expansion by around 145 percent,<sup>4</sup> lifting hundreds of millions of people out of poverty.<sup>5</sup>

A key driver of such economic growth and prosperity has been the high levels of flexibility and resilience that come with economic freedom. In continuously cultivating such freedom, many governments have ensured the free flow of goods and services, improved the ease of conducting business, controlled inflation, and cut taxes while emphasizing greater transparency and accountability under the strong rule of law. The powerful forces of economic freedom have fostered the spirit of entrepreneurship and innovation that creates new products and more jobs, spreading the benefits of a dynamic economy around the globe.

Despite some setbacks, the system still remains not only viable—with its core features such as private property rights, openness, and flexibility almost uncontested—but uniquely able to promote prosperity. As the financial and economic crisis has been unfolding into an unemployment crisis, it is imperative to pick up the pace of economic reforms to facilitate business startups and overall economic growth, which supply jobs and income for more people.

**Enhancing Economic Freedom: A Key Pillar of Exit Strategies.** Although it is not easy to accept the cyclical nature of economies, there can be found some parallels between the 1997 Asian financial crisis and today's difficulties.<sup>6</sup> The Asian

1. "Washington: Prime Minister Silvio Berlusconi Meets President Barack Obama," G8 Summit 2009, at [http://www.g8italia2009.it/G8/Home/News/G8-G8\\_Layout\\_locale-1199882116809\\_1199898101894.htm](http://www.g8italia2009.it/G8/Home/News/G8-G8_Layout_locale-1199882116809_1199898101894.htm) (June 30, 2009).
2. *Ibid.*
3. Andrea Thomas, "Merkel Pledges Tax Cuts Despite Rising Deficit," *The Wall Street Journal*, June 30, 2009, at <http://online.wsj.com/article/SB124631002610270209.html> (June 30, 2009).
4. Gary Becker and Kevin Murphy, "Do Not Let the 'Cure' Destroy Capitalism," *The Financial Times*, May 12, 2009, at [http://www.ft.com/cms/s/0/009e1e8c-14ef-11de-8cd1-0000779fd2ac.html?nclick\\_check=1](http://www.ft.com/cms/s/0/009e1e8c-14ef-11de-8cd1-0000779fd2ac.html?nclick_check=1) (June 30, 2009).
5. For more information on charting the advance of economic freedom, see Terry Miller and Kim R. Holmes, *2009 Index of Economic Freedom* (Washington, D.C.: The Heritage Foundation and Dow Jones and Company, Inc., 2009), pp. 135–136, at [http://www.heritage.org/index/PDF/Index09\\_Chapter2.pdf](http://www.heritage.org/index/PDF/Index09_Chapter2.pdf).

crisis triggered extensive economic and political unrest in emerging Asian markets, sending many into recession. At the time, one commonly employed shortsighted interpretation was that the crisis debunked the “Asian Miracle.” Capitalism and globalization were repudiated and blamed for the bursting of currency and property bubbles and the resultant difficulties.

The years since the 1997 crisis, however, have shown that this interpretation was exaggerated. Asia has become once again the most dynamic region in the global economy. As painful as the crisis was, the aftermath of the market turmoil helped crisis-hit Asian economies such as South Korea, Thailand, and Malaysia embrace more economic freedom as part of exit strategies out of the crisis. That is, the crisis offered an opportunity to embrace more market principles. To their credit, most crisis-affected Asian governments took steps to address their problems by reforming financial sectors, improving transparency of regulations, strengthening corporate governance, and opening their markets to more competition. In addition, they have continued to promote their economic advantages by embracing foreign trade and seizing opportunities to integrate themselves into the global trading system. In hindsight, the 1997 Asian financial crisis was nothing more than a transitory setback that spurred more openness and transparency for the Asian economy.

Today’s world economy could also emerge stronger if the right policy choices are decisively made at this critical juncture of the financial crisis. Abruptly

halting the long-standing commitment to economic freedom will only prolong the current economic downturn and weaken the foundation for solid economic growth.

**Preserving Economic Freedom.** The challenge is to preserve the progress in economic freedom that has been made and to revamp the reform agenda to focus on generating greater economic freedom, not less. Meeting this challenge will require strong commitment and political leadership. This is where the G-8 should come in.

Leaders of the G-8 should be reminded that economic freedom is an indispensable link between economic opportunity and prosperity. The principles of economic freedom and rules for a free market that enhance rather than suppress competition are proven to work only if governments will respect them. Nothing the G-8 could do would be more powerful in promoting an economic turnaround than a reaffirmation of these principles, with a pledge by each leader to rededicate themselves to openness, liberalization, and freedom.

With such a commitment, the global economy would emerge quickly with better-equipped institutions and a more vigorous and vibrant economy that can more effectively deal with not only today’s challenges but also those of the future.

—Anthony B. Kim is Policy Analyst in the Center for International Trade and Economics at The Heritage Foundation.

---

6. For more discussion, see Khor Hoe Ee and Kee Rui Xiong, “Asia: A Perspective on the Subprime Crisis,” International Monetary Fund, June 2008, at <http://www.imf.org/external/pubs/ft/fandd/2008/06/pdf/khor.pdf> (June 30, 2009).