

## ECONOMIC LIBERALIZATION AND INTERNATIONAL ORDER

*John A. Tures*

In a recent study, I examined the connection between economic freedom and internal conflict (Tures 2003). This article expands upon the earlier study by examining the link between economic liberty and *external* conflict. The question I now address is, does economic liberalization promote international order by reducing conflict among nations?

### Research Design

In analyzing the relationship between economic freedom and external conflict, I rely on the KOSIMO data set from the Heidelberg Institute for International Conflict Research (HIIK 1998, 1999) and on the Fraser Institute's economic freedom of the world (EFW) index (Gwartney and Lawson 2000). The HIIK provides data on cases of external conflict, ranging from latent conflicts to less violent crises, to mostly violent crises, to international war. For the purposes of this study, I divide these conflicts into two groups: (1) less severe conflicts, which include latent conflicts and less violent crises, and (2) more severe conflicts, which include mostly violent crises and international wars. I look at all cases of external conflict that involve multiple parties, and each country involved is treated as a unique case. For example, Bolivia, Chile, and Peru have feuded over a narrow strip of land between Tacna and Arica in the Antofagasta region. That conflict is treated as three separate cases: one for Bolivia, one for Chile, and one for Peru.

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John A. Tures is Assistant Professor of Political Science at LaGrange College. He thanks Sara Gilreath, Brandon Holcomb, Christopher J. Stanford, Temisha Miles, Kelly Wren, and Matthew Dobson for their help collecting the data used in this study and for other research assistance.

In measuring economic freedom, I rely on the EFW index that ranks countries on a scale of 0 to 10, with higher scores representing greater economic freedom. Countries with EFW scores ranging from 7 through 10 are categorized as Free, those with scores from 5 to 6.999 as Partly Free, and those below 5 as Not Free. The EFW index scores are only reported every five years for each country, beginning in 1970. This study examines seven cross-sections: 1970, 1975, 1980, 1985, 1990, 1995, and 1997. The EFW index scores are paired with the KOSIMO data. The unit of analysis is the country and year for each cross-section (a “country case”). In other words, I check to see if the EFW report provides scores for Saudi Arabia in 1970, 1975, 1980, and so on. If it does, I then examine KOSIMO data to see if Saudi Arabia experienced an external conflict (or war) in 1970, 1975, 1980, and so forth. This methodology generated 712 country cases or units of analysis.

### Preliminary Findings

Table 1 shows that 25.4 percent of all *cases* of external conflict involved economically Free countries, 38.7 percent involved Partly Free countries, and 35.8 percent involved nations that were Not Free. Free countries were also *less likely* to experience an external conflict (Table 1). The likelihood that a Free country would experience an external conflict was only 41.9 percent vs. 50.6 percent for a Not Free country.

TABLE 1  
ECONOMIC FREEDOM AND EXTERNAL CONFLICT REDUCTION

Economic Freedom Levels	% of External Conflict Cases	% of External Conflicts	% Chance of Experiencing an External Conflict
Free	25.4	27.2	41.9
Partly free	38.7	38.4	44.5
Not free	35.8	34.3	50.6

Evidence also shows that Free countries experienced a lower percentage of *less severe* external conflict cases (27.2 percent) than countries with less economic freedom (Table 2). Finally, Table 3 shows that the chance that an economically Free country will experience a *more severe* external conflict is much lower (5 percent) than for a Not Free country (12.1 percent).

TABLE 2  
ECONOMIC FREEDOM AND LESS SEVERE EXTERNAL  
CONFLICT REDUCTION

Economic Freedom Levels	% of Less Severe External Conflict Cases	% of Less Severe External Conflicts	% Chance of Experiencing a Less Severe External Conflict
Free	27.2	29.1	36.9
Partly free	39.6	38.2	37.5
Not free	33.2	32.6	38.5

TABLE 3  
ECONOMIC FREEDOM AND MORE SEVERE EXTERNAL  
CONFLICT REDUCTION

Economic Freedom Levels	% of More Severe External Conflict Cases	% of More Severe External Conflicts	% Chance of Experiencing a More Severe External Conflict
Free	17.2	16.0	5.0
Partly free	34.5	39.5	7.1
Not free	48.3	44.4	12.1

### Detecting Differences between Observations and Expectations

In the preceding section, we learn two lessons. First, economically Free states do fight other countries. Second, these liberal states engage in fewer external conflicts than their Partly Free and Not Free counterparts. Does this evidence indicate that there is a relationship between economic freedom and international conflict? If one uses a strict criterion of falsification, then even if one country case shows no relationship between economic freedom and external conflict, we must reject the hypothesis that economic liberalization is conducive to international order. However, if we adopt a less restrictive probabilistic assessment and simply test to see whether a certain type of behavior is more or less likely or less likely to occur, then our preliminary findings lend support for the theory that economic freedom fosters peaceful external relations (i.e., reduces external conflicts). Nevertheless, we need to conduct some additional tests before we can conclude that such a relationship exists.

Although the distribution of cases does support the argument that Free nations are less likely to engage in external conflicts, one cannot ignore the evidence that there is a 5 percent chance that an economically Free country will engage in a severe crisis or war with another nation, compared with a 12 percent chance that an illiberal state will do the same. Is that difference enough to matter; is it statistically significant?

To answer that question, we need to compare the observed results with results expected under a normal distribution of cases—that is, we need to determine how many conflicts Free countries can be expected to be engaged on average. For example, the *expected* number of cases with one *more severe conflict* among economically Free states is 11.1. This value is generated by multiplying the number of single conflict cases (40) by the number of economically Free countries (198) and dividing by the total number of cases (712). We can then compare this number (11.1) with the *observed* number of cases in which an economically Free state fought one more severe conflict (8).

In addition to comparing observations with expectations, we also have a standard by which we can ascertain whether the differences between the two are statistically significant—namely, the chi-square statistic, which represents the entire sum of differences between observations and expectations. If the difference between the observed and expected values is statistically significant, then the null hypothesis of no difference can be rejected, increasing our confidence in the connection between economic freedom and international order.

#### *Less Severe External Conflict*

Table 4 shows that a connection exists between countries that practice economic freedom and nations that are less likely to engage in a less severe external conflict. Economically Free nations generally have fewer cases of conflict than expected while Partly Free and Not Free countries are more likely to engage in a low-level conflict than expected.

The differences between the observed and expected cases may not seem very large. However, the chi-square value of 23.997 is statistically significant at the 10 percent level. This means that there is less than a 10 percent chance that the results are attributable to something other than the statistical relationship between the variables. In other words, we can be 90 percent confident in rejecting the null hypothesis that claims an absence of a connection between the variables.

TABLE 4  
ECONOMIC FREEDOM AND LOW-LEVEL EXTERNAL CONFLICTS: A CHI-SQUARE TEST

Economic Freedom Levels	No. of Less Severe External Conflicts in a Given Year (1970, 1975, 1980, 1985, 1990, 1995, 1997)								Total	
	0	1	2	3	4	5	6	7		8
Free	O = 125 E = 123.5	O = 46 E = 44.8	O = 14 E = 18.4	O = 2 E = 3.3	O = 3 E = 1.1	O = 3 E = 1.9	O = 2 E = 0.8	O = 2 E = 0.8	O = 1 E = 0.8	198
Partly free	O = 177 E = 176.5	O = 61 E = 64	O = 27 E = 26.2	O = 9 E = 4.8	O = 7 E = 4.8	O = 0 E = 1.6	O = 0 E = 2.8	O = 1 E = 1.2	O = 1 E = 1.2	283
Not free	O = 142 E = 144.1	O = 54 E = 52.2	O = 25 E = 21.4	O = 1 E = 3.9	O = 2 E = 3.9	O = 1 E = 1.3	O = 5 E = 2.3	O = 0 E = 1	O = 1 E = 1	231
Totals	444	161	66	12	12	4	7	3	3	712
Chi-square statistic: 23.997; Df = 16; X2 < .10.										

NOTES: O = observed, E = expected, Df = degrees of freedom (parameters), X2 = level of statistical significance.

*More Severe External Conflict*

The preceding section dealt with cases of low intensity warfare, such as less violent crises and latent conflict. This section deals with more severe cases, ranging from mostly violent crises and outright war. As with the less severe cases, countries that adopt policies resulting in economic freedom are less likely to engage in high-level hostility (Table 5). Results for Partly Free countries are mixed, but these countries are somewhat less likely to fight a foreign power. Not Free countries, on the other hand, have not only produced more conflict cases than expected, but fewer peace cases as well. These differences are statistically significant. The chi-square statistic is 14.182, which allows us to reject the null hypothesis with 90 percent confidence that the more economically free a country is, the less likely it will engage in conflict: severe or not.

*Controlling for Level of Development*

Our results thus far reveal a relationship between economic freedom and international order (i.e., less external conflict). Do these results apply to rich and poor countries alike? To determine this, we can divide our sample into two types of cases. One group includes members of the Organization of Economic Cooperation and Development, a group of countries that represent the most developed nations. The other sample includes countries that do not belong to the OECD.

As expected, most of the cases (536 of 712) are underdeveloped countries or non-OECD states. These less developed countries do not display statistically significant results for lower-level conflicts—that is, we cannot reject the null hypothesis of no relationship between economic freedom and lower-level external conflicts. Among more severe cases of conflict, the results just miss displaying statistical significance. Economically Free countries appear to engage in fewer cases of violent conflicts and wars, but the results are mixed. It should be noted that while the Pearson chi-square statistic likelihood ratio just misses displaying statistical significance at the 10 percent level (the result is .106), the likelihood ratio (another measure) is statistically significant at the 5 percent level.

As for developed countries, we find that OECD members are less likely to engage in less severe cases of conflict. These results do not show a clear connection between economic liberalism and lower forms of violence between nations. Nevertheless, there is a strong association between the two variables when it comes to the *more severe cases* of external conflict (violent crises and wars). These

TABLE 5  
ECONOMIC FREEDOM AND HIGH-LEVEL EXTERNAL CONFLICTS: A CHI-SQUARE TEST

Economic Freedom Levels	No. of More Severe External Conflicts in a Given Year (1970, 1975, 1980, 1985, 1990, 1995, 1997)				Totals	
	0	1	2	3		4
Free	O = 188 E = 181.9	O = 8 E = 11.1	O = 1 E = 3.9	O = 1 E = 0.8	O = 0 E = 0.3	198
Partly Free	O = 263 E = 259.9	O = 12 E = 15.9	O = 5 E = 5.6	O = 2 E = 1.2	O = 1 E = 0.4	283
Not Free	O = 203 E = 212.2	O = 20 E = 13	O = 8 E = 4.5	O = 0 E = 1	O = 0 E = 0.3	231
Totals	654	40	14	3	1	712
Chi-square statistic: 14.182; Df = 8; X2 < .10.						

NOTES: O = observed, E = expected, Df = degrees of freedom (parameters), X2 = level of statistical significance.

results are statistically significant at the 10 percent level. Among the wealthier countries, the freer a nation is, the less likely it will use significant amounts of military force against another nation.

One might wonder why the results (among higher levels of conflict) apply to the wealthier countries, but the record on less developed countries is mixed. One plausible explanation revolves around the countries excluded from the underdeveloped nation sample. The Fraser Institute's *Economic Freedom of the World* data set provides no data for countries such as Iraq, Cuba, Libya, Afghanistan, Vietnam, Sudan, Lebanon, and Laos. It is likely that these repressive regimes, had they been included, would have received low EFW index scores. Furthermore, these countries have engaged in many external conflicts, as noted in the HIIK's KOSIMO dataset.

Another possible explanation focuses on membership in other economic organizations such as the World Trade Organization, the European Union, the North American Free Trade Agreement, and the Asian Pacific Economic Cooperation forum. The more developed nations are likely to join these associations. By joining such organizations, countries do not relinquish their decisions to disagree with fellow members. But these organizations often have dispute resolution mechanisms that enable countries to resolve their external conflicts before they become major crises or wars.

### Comparing Results: Internal vs. External Conflict

Comparing the results of my 2003 study with the present one reveals that the relationship between economic freedom and *internal* conflict is stronger than the link between liberalism and *external* conflict, even though both associations are statistically significant. The question remains why internal conflicts, rather than international conflicts, are less likely to occur under conditions of economic freedom.

The answer may lie in the benefits economic freedom provides, as well as the motives market-liberal nations might occasionally have for external conflict. Those who attempt to reduce government intervention in economic transactions hope to strengthen property rights and create new wealth for individuals and the nation. Conditions of conflict at home are likely to jeopardize those gains, mitigating motives for war with one's countrymen.

The relations between economically Free countries and other countries are much different. Economically Free countries may fight other countries but not necessarily endanger the private sector on the home front. Scholars such as Doyle (1986) note that liberal countries are likely to expand their number by waging war against illiberal



nations. Such cases of “liberal imperialism” may generate economic benefits by creating a new client state dedicated to the principles of capitalism. Economically Free states may also witness a call to arms for additional reasons. Countries like the United States and Great Britain may feel that a defensive or preventive war may be necessary to defend free markets and free people from illiberal foreign powers.

Additional research needs to be conducted to further explore these relations. Politicians and academics alike have frequently cited the robust findings from the “Democratic Peace,” which contends that democracies are far less likely to fight each other than any other pair of nations in the international system. Results showing similar findings for economic freedom would reinforce the importance of private property rights and the rule of law for international, as well as domestic, order.

## Conclusion

Clearly, commercial freedom has been instrumental in reducing conflict in recent years. Our analysis shows that the greater respect a country has for the private sector, the less likely it is to engage in external conflict. This finding generally holds true for both the developed and developing world with respect to more severe cases of conflict. These findings are not as strong as the connection between liberalism and internal order (i.e., a lack of internal conflict), owing to the exclusion of rogue states from the sample as well as the decision of capitalist powers to promote or protect free markets in the international system. Nevertheless, there is no denying the importance of economic freedom for creating wealth and reducing the level of conflict in the world.

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