

## **Freedom and growth: Do constitutions matter?\***

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In England, everything that is not prohibited is permitted; in Germany, everything that is not permitted is prohibited; in France, everything that is prohibited is permitted; in the USSR everything that is permitted is prohibited.<sup>1</sup>

Democracy is good, but sausages are better.<sup>2</sup>

**Abstract.** This paper uses an augmented Solow model, with cross section data, to measure the effect on per-capita income of a) the entrenchment of various rights in a country's constitution and b) the level of economic freedom in a country, broadly construed. The results suggest that entrenchment, *per se*, of any single right seldom has a significant general economic effect, while the effect of economic freedom is significant and substantial. The paper then considers whether such evidence could support the proposition that "constitutions do not matter." While it concludes otherwise, it does caution against incurring excessive negotiation costs to obtain entrenchment of a comprehensive "wish list" of rights.

### **1. Introduction**

Do constitutions matter? Judging from the current frenzy of constitution-making and remaking, a substantial number of people in vastly diverse countries throughout the world must be of the opinion that they do. Otherwise, how could such real resource exhaustion be justified for these endeavors?

Of course, we have just witnessed the apparent conclusion of one of the longest and broadest social experiments in modern history; an experiment which, at least in the case of the Germanies, came about as close as possible in "aggre-

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gate" social science to being "controlled". But the lessons to be drawn from that experiment apply mainly to broad categories of social systems;<sup>3</sup> namely, to those that "lost" (in the sense that the system "collapsed") versus those that "won" (in the sense that system has not yet "collapsed"). These lessons do not necessarily apply to determining the successful or best elements of the internal structure of the winning systems.

In fact, many of those same "winning" systems are also undertaking or contemplating dramatic changes in their constitutions and other institutional structures. Canada is again in the midst of a "constitutional crisis" which hinges in part on the phrasing and placement of a constitutional insertion designating one of the provinces as "a distinct society" (or an equivalent designation). The European Community is currently negotiating a "social charter" as a part of its constitutional structure which may have dire consequences for the economic competitiveness of some current or potential members which are thought to lag behind other European countries in guaranteeing social amenities.

What are the root causes of this veritable "constitutional revolution" (in Buchanan's, 1980, words) in modern, successful economies? While other academic disciplines may focus elsewhere, say on the physiological, social, legal and/or political determinants, it is natural for economists to consider the economic forces at play, their effects on the creation and evolution of constitutions as sort of a super-contract, and, in turn, the constraints on economic forces provided by "effective constitutions."<sup>4</sup>

Constitutional political economists (Hayek, 1979; Gwartney and Wagner, 1988) suggest that constitutions have an economic value for at least two reasons: first, constitutions can aid in establishing the basic conditions for human liberty and freedom which have utilitarian value in their own right; second, liberty and freedom so established are essential to individuals' fulfilment of other wants through economic activity. Public choice economists (Buchanan, 1980; Olson, 1982) also emphasize the role of constitutional and other institutional constraints in the limitation of rent-seeking activity which might otherwise dissipate surplus<sup>5</sup> and lead to the "decline of nations". Further, property-rights economists (Allen, 1991; Barzel, 1989; North, 1990) expand on the latter theme to emphasize the evolving role of constitutions as institutions which define systems of property rights and which shape, and in turn are shaped by, transaction costs in order to promote efficiency in specific and in general.<sup>6</sup> Finally, legal theorists (Epstein, 1988; Pilon, 1988) emphasize the role of constitutional constraints in controlling arbitrary takings by the state which, in anticipation, would lower the value of private wealth and income.

While the welfare derived directly from constitutions may be difficult to measure, the relationship between constitutions, or, more generally, constitutionally-mandated institutions of freedom and liberty, and economic