



THE 2008 LEGATUM PROSPERITY INDEX™

An Inquiry into Global Wealth and Wellbeing

PREFACE



Dear Reader,

Welcome to the 2008 Legatum Prosperity Index. This second edition builds on last year's inaugural publication, with expanded coverage and refined analysis.

The Prosperity Index is an inquiry into the nature of prosperity and how it is created. This year, scholars and researchers affiliated with the Legatum Institute have significantly expanded the scope of the Index, investigating prosperity drivers and outcomes in more than 100 countries worldwide, increased from only 50 last year. Africa, particularly, is better represented with 19 countries featured, although collecting data for every single country remains a challenge.

We define prosperity holistically to include both material wealth and quality of life. Rather than replicating other measurements that rank countries by their actual levels of material wealth or life satisfaction, the Index produces a ranking based on the conditions that foster prosperity – that is, the factors that promote economic competitiveness and improved liveability in a given country. We refer to these factors as *drivers* of prosperity and to those that impede prosperity, as *restrainers*. The Index endeavours to rank countries according to the strength of these drivers and restrainers, not according to simple measures of income and life satisfaction. In this way we hope to contribute to a richer analysis of what promotes prosperity globally.

The full details of the Index and its construction are included in the *2008 Prosperity Index Report*, together with

a comprehensive fold-out table of country rankings inserted at the end of this book.

The Report, which also includes original research papers on key topics in prosperity from leading scholars and country profiles for each of the 104 countries in the Index, is available in printed form and on the Legatum Institute website at www.prosperity.com.

This Summary and Commentary introduces the findings from the 2008 Index, and provides our interpretation of the results. It describes the personal and policy choices that can increase the prosperity of individuals and nations around the globe.

The conclusions we draw in this commentary are based on data research as well as theory, experience, and the lessons of history. While we draw on statistical analysis to support these findings and views, quantitative analysis is limited in its ability to separate the drivers of prosperity from their outcomes, and to disentangle the interactions between related drivers. Simply put, there are limits to what science can tell us about the causes of the prosperity of nations (for a discussion of some of these issues, see the full *Prosperity Index Report*, available on request).

Yet while there are limits to our knowledge, there is still much that we have learned and can learn. While governments by themselves cannot create or mandate prosperity, they can help create an environment that is conducive to entrepreneurship and productive endeavour. Ultimately, it is citizens and their leaders who must choose to take

ownership of the solutions that will drive their nation's long-term prosperity, and their personal happiness.

We very much hope that you find the 2008 Legatum Prosperity Index of interest, and this commentary engaging and thought-provoking. For Legatum, the quest to understand prosperity is a long-term investigation that we will seek to improve with every edition. We would welcome any comments or feedback that may help improve our understanding.

Yours sincerely,



Dr. William Inboden
Senior Vice-President
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MISSION STATEMENT

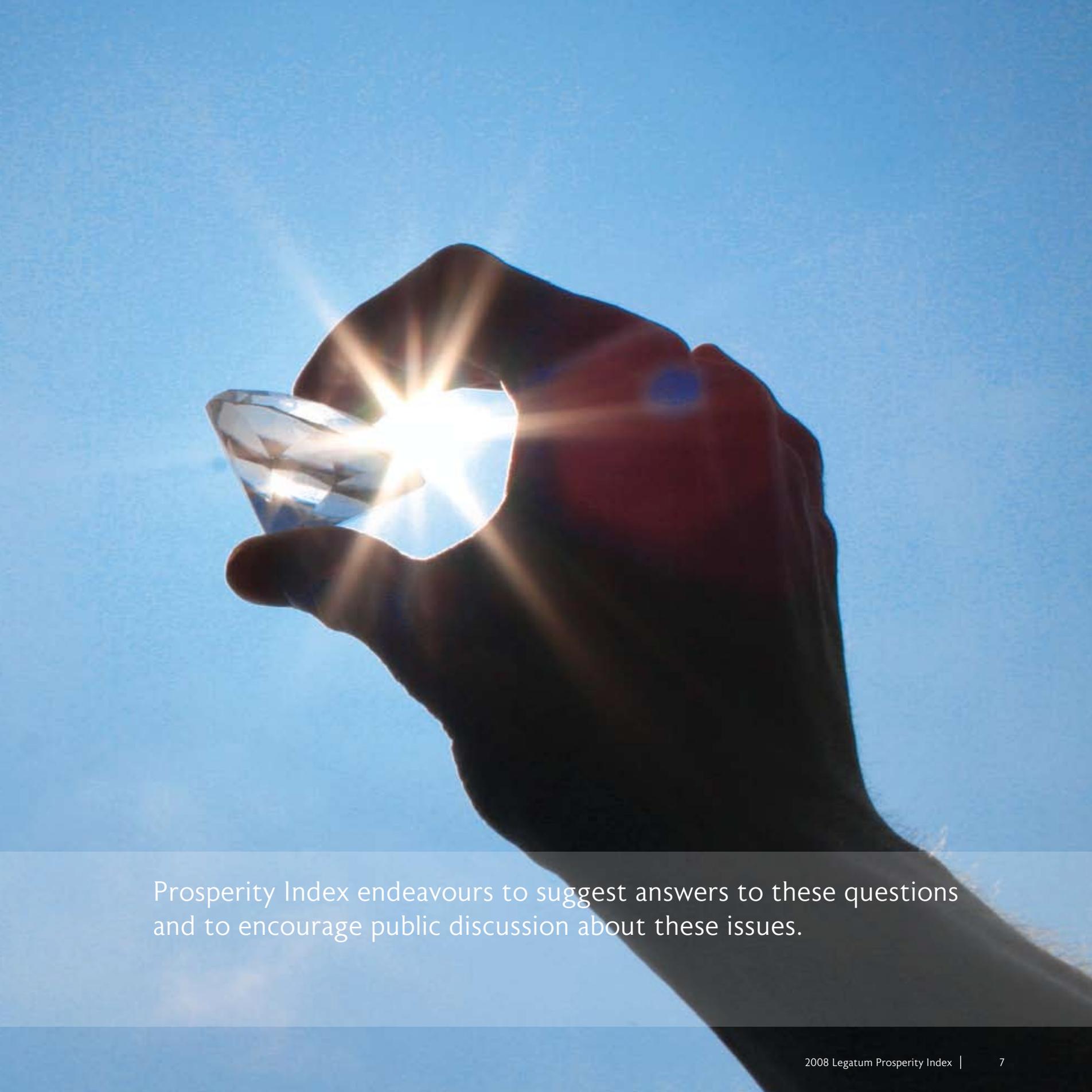
The purpose of the Prosperity Index is to encourage policymakers, scholars, the media, and the interested public to take a holistic view of prosperity and understand how it is created. Holistic prosperity extends beyond just material wealth, and includes factors such as social capital, health, equality of opportunity, the environment, effective governance, human rights and liberties, and overall quality of life.

“...Gross National Product counts air pollution and cigarette advertising, and ambulances to clear our highways of carnage...It counts the destruction of the redwood and the loss of our natural wonder in chaotic sprawl...Yet the Gross National Product does not allow for the health of our children, the quality of their education or the joy of their play. It does not include the beauty of our poetry or the strength of our marriages, the intelligence of our public debate or the integrity of our public officials...*it measures everything, in short, except that which makes life worthwhile.*”

Senator Robert Kennedy

EXECUTIVE SUMMARY

In a world in which many people are becoming richer, are we also getting happier, healthier, and more fulfilled? What does it mean to become more prosperous, and how does it happen? The Legatum

A hand holding a large, faceted diamond against a clear blue sky. The diamond is held in a way that it catches the light, creating a bright, multi-pointed starburst effect. The hand is silhouetted against the sky, and the diamond's facets are clearly visible, reflecting light in various directions. The overall mood is one of aspiration and value.

Prosperity Index endeavours to suggest answers to these questions and to encourage public discussion about these issues.

EXECUTIVE SUMMARY

The Prosperity Index is unique in three ways.

First, it takes a holistic view of prosperity, encompassing both material wealth and life satisfaction. Second, it assesses the drivers and causes of prosperity, rather than measuring outcomes. Third, it includes factors that relate to government policy and to individual citizens.

Constructing the Index

- The 2008 Legatum Prosperity Index is the result of an investigation into the various factors that promote prosperity in nations. Recent research advances have made it possible to compare not only the material wealth but also the life satisfaction of people in countries worldwide. Accordingly, we have defined national prosperity as the holistic combination of both of these factors.
- The overall Index scores and rankings are based on a weighted combination of indicators that reflect *Economic Competitiveness* and *Comparative Liveability*. That is to say, the Index does not rank countries according to which have the most material wealth or the highest levels of happiness at a given time. Rather, it is an index of drivers, which means that countries are ranked by how well they are doing at fostering economic growth and improved quality of life. In other words, how well are nations promoting the practices, habits, policies, and institutions that create enduring prosperity?
- The indicators that comprise the Index were identified and weighted based on statistical analysis, using 40 years of historical data on economic growth in more than 50 countries, and life satisfaction survey data for more than 100 countries.
- The Index combines 22 key indicators and 44 sub-indicators in order to rank more than 100

countries, based on the degree to which the actions of their people and governments drive or restrain the creation of holistic national prosperity, relative to the prosperity of other countries.

- The Index is presented in a set of publications. This book summarises the Index results and provides our interpretation of the meaning of the findings. Separately, the *Prosperity Index Report* describes the methodology and indicators in detail, profiles each of the countries covered in the Index, and presents research and policy papers on key topics in prosperity. For readers interested in more background or in conducting their own investigations, the Technical Appendix in the Report describes the research methodology in detail. All these publications, together with an extensive set of interactive data analysis tools, are available at www.prosperity.com.



Key Findings

The key drivers of economic competitiveness vary according to a country's level of development. For poorer countries (those with average incomes of less than \$10,000 per capita), where increasing material wealth is a particular priority, the most important components of economic competitiveness include:

- Government Effectiveness
- Levels of Education
- Growth in Invested Capital
- Low Costs of Starting a Business
- Commercialisation of Innovation
- Low Dependence on Foreign Aid
- Low Dependence on Commodity Exports
- Economic Openness

For richer countries (those with incomes greater than \$20,000 per capita) that wish to experience continued economic growth, the most important components of competitiveness include:

- Invested Capital
- Education
- Entrepreneurship
- Commercialisation of Innovation

The key factors for promoting life satisfaction also vary according to a country's level of development. In richer countries, where moving beyond material wealth to broader wellbeing is an important goal, the most important components of liveability include:

- Continued High Levels of Income
- Good Health
- Political Rights and Civil Liberties
- Freedom of Choice
- Charitable Giving
- Family Life
- Equality of Opportunity
- Pleasant Natural Environment
- Community Life
- Religious Freedom

Many poor countries have surprisingly high levels of wellbeing, because traditional social strengths can compensate, at least somewhat, for low average standards of living. In poor countries, the most important components of comparative liveability include:

- Family Life
- A Warm Climate
- Religious Faith

PROSPERITY PERFORMANCE: HOW DO DRIVERS COMPARE WITH OUTCOMES?

The Prosperity Index is an index of drivers. That is, it assesses which countries' leaders and citizens are doing the most to actively foster or promote holistic national prosperity.

But what about outcomes? Which countries actually achieve the greatest prosperity performance – that is, the highest incomes and highest levels of life satisfaction? And to what extent do high Prosperity Index scores correlate with these actual prosperity outcomes?

As one might expect, because the factors in the Index are based on analysis of historical data, the link between drivers and outcomes is strong. In statistical terms, the correlation is higher than 0.85 both between countries' ranks on the Competitiveness Index and their actual per capita incomes, and between their ranks on the Liveability Index and actual average national life satisfaction survey results in the Gallup World Poll.

There are a few countries in which performance differs notably from what the Prosperity Index predicts. Singapore, Germany, Hong Kong, Norway and Ireland are the countries in the top ranks of the Prosperity Index where significant differences appear. Most of these differences are on the material wealth side.

Based on their Prosperity Index scores, we would expect Germany, Singapore and Ireland to be even wealthier than they are. In Germany's case this may reflect the long slowdown that followed reunification, while in Singapore and Ireland it may reflect a late start in growth.

Norway, by contrast, is predicted by the Index to be less wealthy than it actually is. In the Index, Norway scores poorly on entrepreneurship and some innovation indicators. Yet these areas of apparent weakness do not appear to have reduced the country's economic performance, which is among the world's best. This owes in part to Norway's proven ability to mitigate natural resource dependence by responsibly investing its oil revenues in ways that foster growth and impressive levels of wellbeing.

But perhaps the most surprising case is Hong Kong. Despite extremely high levels of development, and generally good quality of life indicators, Hong Kong registers very low life satisfaction results that are difficult to explain.

The top 30 countries, ranked by holistic prosperity performance (taking the average of the ranking on income and life satisfaction) are shown below. The full details of countries' performance are available at www.prosperity.com.

Holistic Prosperity Performance			Material Wealth Performance		Life Satisfaction Performance	
Country	Performance Rank	Legatum Prosperity Index Rank	Rank	Income per Person	Rank	Survey Average (1-10)
Denmark	1	9	6	\$31,422	1	7.9
Switzerland	2	7	5	\$32,775	3	7.5
Norway	3	14	2	\$37,667	8	7.4
United States	3	4	1	\$38,165	9	7.4
Netherlands	5	11	7	\$31,306	4	7.4
Finland	6	2	10	\$30,420	2	7.7
Ireland	7	20	3	\$36,238	13	7.2
Sweden	8	12	11	\$30,392	6	7.4
Australia	9	1	9	\$30,678	10	7.3
Canada	9	14	12	\$30,278	7	7.4
Austria	11	2	8	\$30,736	16	7.1
Belgium	12	14	14	\$30,004	12	7.3
New Zealand	13	9	23	\$23,109	5	7.4
United Kingdom	14	14	13	\$30,237	18	6.9
France	15	14	15	\$28,877	20	6.8
Spain	16	22	21	\$24,681	15	7.1
Singapore	17	4	16	\$28,305	23	6.6
Israel	18	19	25	\$22,662	17	7.0
Italy	18	25	20	\$26,496	22	6.7
Germany	20	4	18	\$27,438	25	6.5
United Arab Emirates	21	28	24	\$22,698	21	6.7
Japan	22	13	17	\$27,992	30	6.4
Saudi Arabia	23	45	34	\$14,769	14	7.2
Taiwan	24	21	19	\$26,826	34	6.2
Czech Republic	25	23	29	\$19,700	28	6.5
Greece	25	34	26	\$21,675	31	6.3
Hong Kong	25	8	4	\$32,901	53	5.5
Costa Rica	28	38	47	\$9,646	11	7.3
Kuwait	29	30	22	\$23,416	37	6.0
Argentina	30	31	37	\$13,652	32	6.2
Mexico	30	43	45	\$9,967	24	6.5



Many Asian countries score very well on the wealth indicators, but have weaknesses in wellbeing, including limited equality of opportunity for women, a degraded natural environment, and long working hours.

The Rankings

- The top spot in the Index is claimed by Australia, followed by Austria and Finland in a tie for second place. These are followed closely by Germany, Singapore, and the United States, also in a tie. While there are limits to what statistical analysis can tell us about the relative importance of indicators that are often highly interrelated, each of these countries registers high scores on nearly every indicator and outstanding scores on a few indicators.
- Australia makes a particular virtue of entrepreneurship as a source of material wealth, as well as pursuing broader societal wellbeing through high levels of volunteering and charitable giving. Austria turns in top scores in education, a key to long-term income growth, and also in health, a key to quality of life. Finland boasts superb governance, helping to drive both wealth and wellbeing in that country.
- This group of countries tops the Index because of imbalanced results from other regions. Many Asian countries score very well on the economic competitiveness indicators, but have comparative weaknesses in liveability, including limited equality of opportunity for women, a degraded natural environment, and long working hours. In contrast, most Nordic countries score very well on liveability indicators, but poorly on some wealth drivers, most notably entrepreneurship.
- While no country has poor scores in every category, Yemen comes closest. While its people maintain a strong religious faith, they also suffer from extreme levels of poverty and poor governance. For most of the countries in the bottom ranks of the Index, extreme poverty appears to be the main cause. This usually has further wellbeing impacts by contributing to ill health and unemployment. A number of countries, such as Zimbabwe and Sudan, are both impoverished and politically repressive.

PRINCIPLES OF PROSPERITY

The results of the 2008 Prosperity Index research highlight a number of general principles relevant to the promotion of national prosperity. These include:

1. **Freedom of choice is crucial.** Whether people have freedom of choice and control over how they direct their lives and spend their time and resources is a strong determinant of life satisfaction and productivity.
2. **Government should be effective, honest and limited.** Governments that exercise power responsibly and are accountable to their citizens dominate the top quartile of the rankings for both competitiveness and liveability.
3. **For poorer countries, raising incomes is a top priority.** For countries with an income per person of less than US \$10,000 on average, income levels are the single strongest predictor of how happy that country's people will be.
4. **For richer countries, wellbeing means more than just money.** For most people in rich countries, non-material drivers tend to have a bigger impact on their life satisfaction than increases in income.



5. **Entrepreneurship is a promising path to material wealth.** Entrepreneurship indicators show a significant statistical relationship with long-term economic growth in both rich and poor countries.
6. **Growth in invested capital is crucial to long-term economic growth.** Investment by the private sector (e.g. in factories, offices and production machinery) is one of the most important drivers of material wealth, for both rich and poor countries.
7. **Economic openness can help poorer countries catch up faster.** Open economies in which foreign direct investment and international trade play larger roles have higher long-term growth rates. Economic openness enables countries to absorb foreign capital, technologies, skills and business techniques. However, poor countries that depend heavily on commodity exports, such as oil and gas, often have lower long-term growth rates.
8. **Climate and the environment impact our happiness.** Several indicators of climate and the environment, including temperature extremes, land area devoted to nature, and perceived air quality, show a significant relationship with average national life satisfaction.
9. **Develop your gift and then give it away.** Countries where charitable giving and volunteering are common report higher average levels of wellbeing.
10. **Geography is not destiny.** Advances in medical science and productive technology are now available worldwide. The top 30 countries in the Prosperity Index include not only countries from Western Europe and North America but also Asia, Eastern Europe, and the Middle East.
11. **Governments and citizens each have a role in building the prosperity of nations.** The 2008 Prosperity Index includes factors driven by individual choice (such as volunteering and charitable giving), factors driven by the choices of policymakers (such as economic openness and good governance), and factors influenced by both, such as health.

Economic openness enables countries to absorb foreign capital, technologies, skills and business techniques.

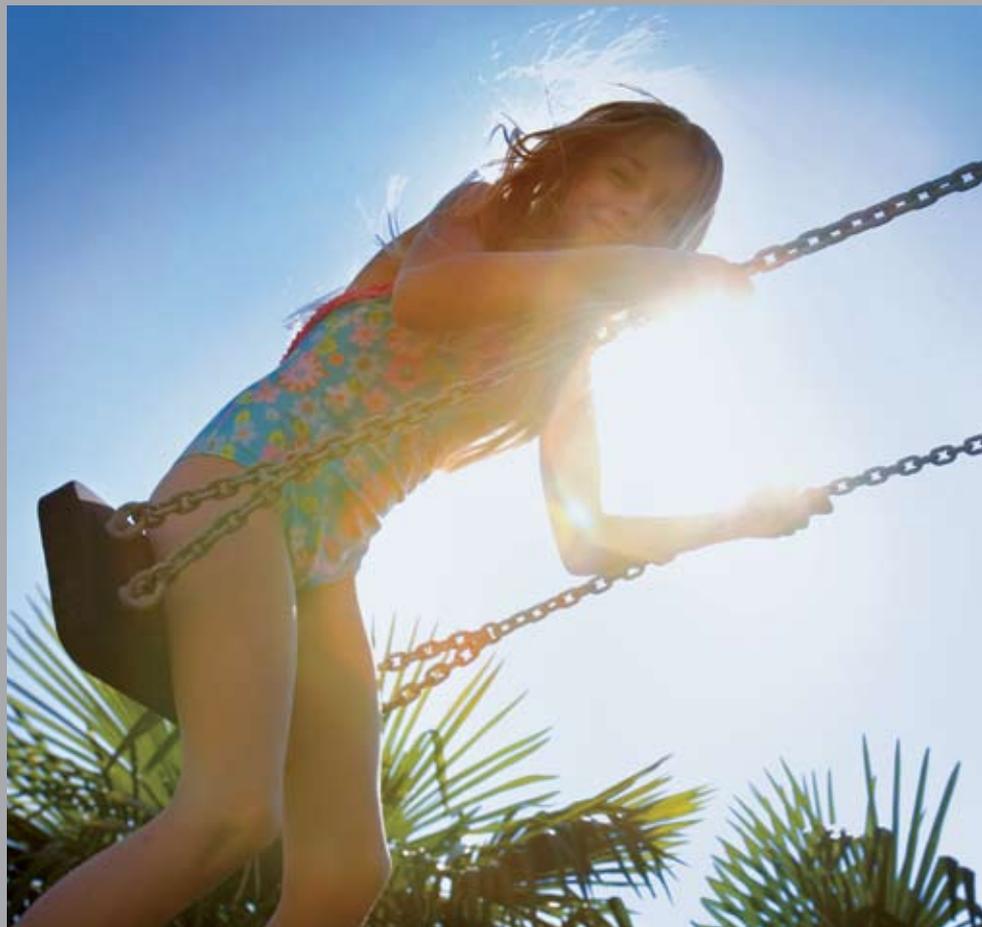
A FASCINATION WITH HAPPINESS

While the pursuit of happiness has long been of interest to individuals, in recent years it has become a priority for many political leaders worldwide. The UK government appointed Lord Richard Layard, an academic at the London School of Economics, as “happiness tsar”, with responsibility for advising on policies to improve wellbeing in Britain. The President of India, Pratibha Patil, announced the creation of a Prosperity Index specifically for her country, measuring quality of life. And French President Nicolas Sarkozy announced that a panel of eminent scholars, led by Nobel Laureates Joseph Stiglitz and Amartya Sen, would develop new economic indicators that would assess wellbeing in France.

Why this sudden interest in happiness from some very serious-minded people? Happiness itself has been an aspiration from the advent of humanity and it has been studied for some time. What is new is the “science of happiness” – new methodologies taking advantage of brain scans and large-scale survey research to assess human wellbeing with quantitative methods. As a result, the study of happiness is now not only of interest to philosophers and psychologists but also to economists and political scientists. The field now attracts attention from well-known scholars including Robert Putnam of Harvard and Nobel Laureate Daniel Kahneman of Princeton.

And thus, in the past few years, wellbeing research has entered the mainstream. *The New York Times* reported on new data linking income and happiness, and *The Independent* on the unhappiness of

Great Britain. *The Wall Street Journal* carried stories on Bhutan’s happiness policies, the *Canberra Times* on wellbeing in Australia, and the *Los Angeles Times* on declining quality of life in the US. Newspapers in countries from Singapore and India to the UK and Canada covered the release of the 2007 Legatum Prosperity Index. In short, it appears our fascination with happiness will not abate any time soon.



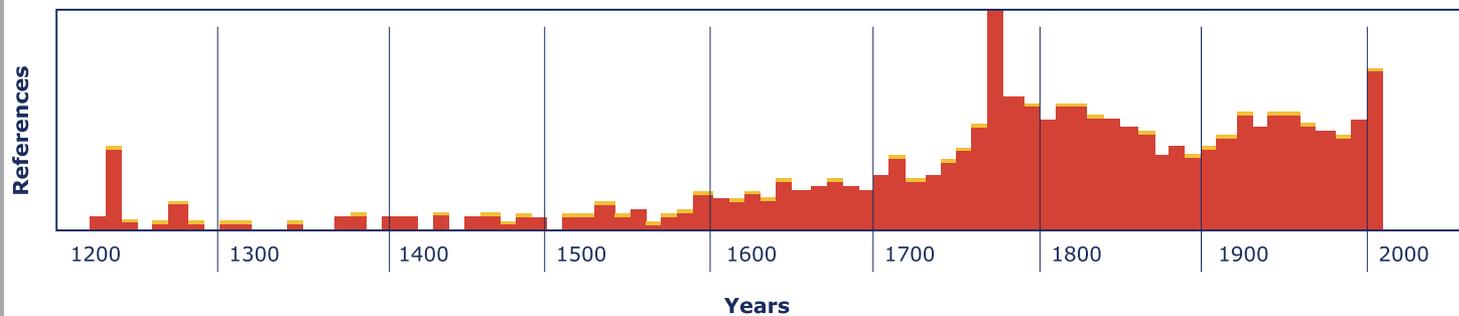
Volume of searches for "Happiness" on Google

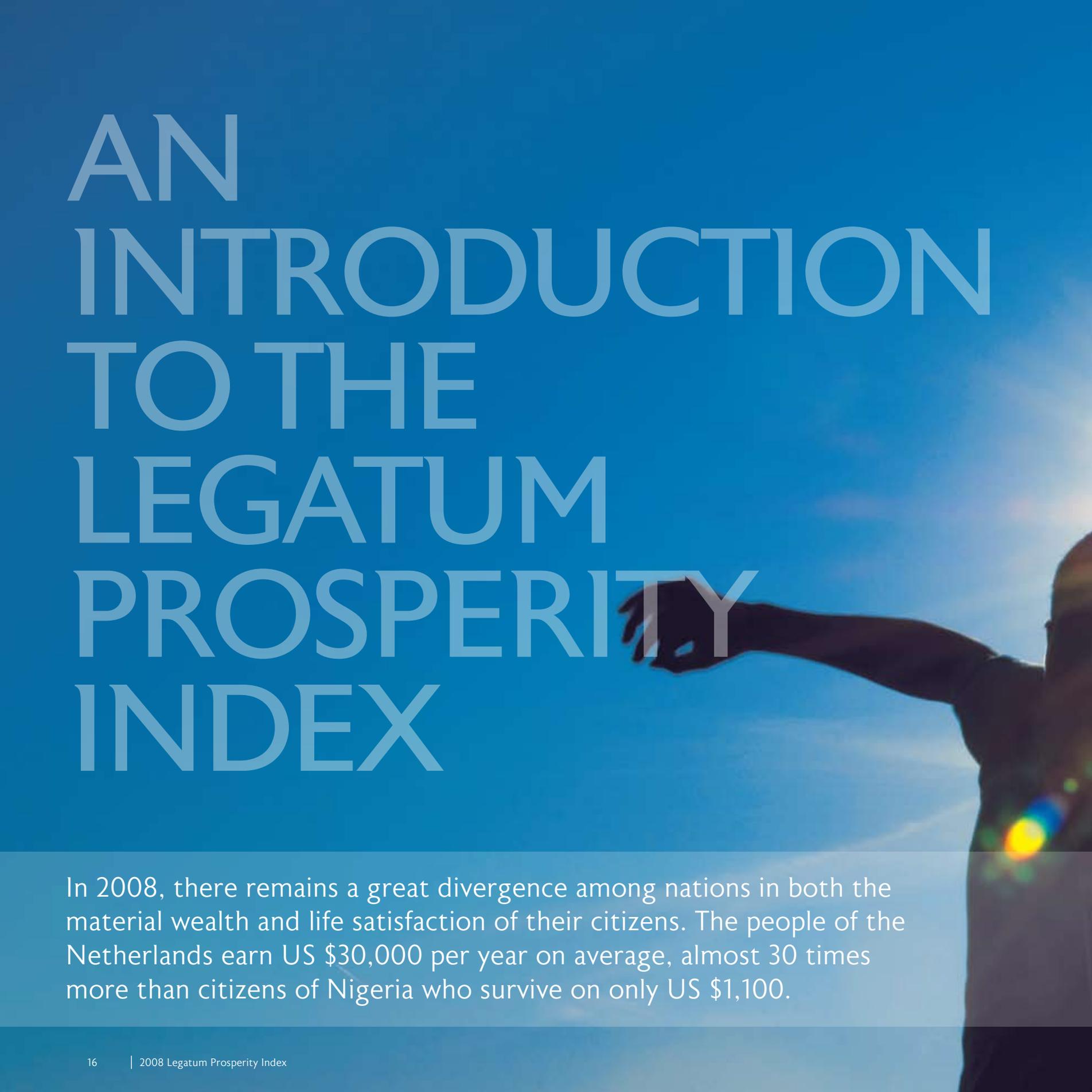
The graph below, produced by Google Trends, shows the near-doubling in search volume for the term "happiness" over the past four years. The temporary spike in late 2006 anticipates the January 2007 release of the movie, "The Pursuit of Happiness", starring Will Smith.



References to "Happiness" over the years

The graph below, also produced by Google Trends, shows the volume of book and news references to specific years in conjunction with the term "happiness". Aside from the current boom, spikes occur in 1776, when the US Declaration of Independence asserted the "pursuit of happiness" as an inalienable right, and in 1238, the date of the founding of the Sukhothai ("Dawn of Happiness") kingdom in Thailand.





AN INTRODUCTION TO THE LEGATUM PROSPERITY INDEX

In 2008, there remains a great divergence among nations in both the material wealth and life satisfaction of their citizens. The people of the Netherlands earn US \$30,000 per year on average, almost 30 times more than citizens of Nigeria who survive on only US \$1,100.



The citizens of Costa Rica report themselves very satisfied with their lives, while those of Zimbabwe, on average, report themselves very dissatisfied.

NEW FACTORS IN THE 2008 PROSPERITY INDEX

In 2008, new research resulted in the addition of several new indicators to the Index. A few of these are highlighted below. Each of these indicators, as with all those in the Index, shows a statistical link with either long-term economic growth or average levels of life satisfaction. For the full list, visit www.prosperity.com.

The Number of Regional Trade Agreements Signed shows a strong link

with economic growth, particularly in poor countries. While some observers dispute the impact of these agreements on global trade flows, for individual countries, this indicator may reflect a government's level of interest and effectiveness in pursuing outward-oriented economic development.

The Business Ownership Rate shows a strong link to income growth, particularly

in rich countries, and is an indicator of entrepreneurship (see Principle of Prosperity 4, page 37).

Researchers in R&D per Capita assesses a country's capacity to innovate in a business context, as well as reflecting the general quality of higher education and human capital in the workforce.

"Can people who work hard get ahead in this country?" is a question on the Gallup World Poll. While answers to this question doubtless reflect individual beliefs, on a national-average basis this indicator seems to reflect the degree to which opportunities for advancement are widely available in society according to individual merit and initiative, rather than being confined to a privileged elite.

Net Migration measures the degree to which people leave a country, fleeing poor conditions or in search of opportunity elsewhere. Data suggest that individuals tend to emigrate from countries where incomes, levels of life satisfaction, or life expectancies are low, and to countries where incomes are high.

Ecosystem Services per Capita is an innovative measure of the value of nature in a country, such as lakes, rivers, wetlands, forests and grasslands. Based on satellite photographs, scientists are able to measure the proportion of a country's land area remaining in a natural state (see Principle of Prosperity 8, page 47).

Charitable Giving and Volunteering are both assessed by the Gallup World Poll, and show a strong statistical relationship with life satisfaction (see Principle of Prosperity 9, page 49).



What are the reasons for disparities between countries? How can these disparities be remedied? And how can countries that have achieved high levels of material wealth today broaden their success to include a good quality of life?

In 2007, the Legatum Institute published the first results of an investigation into the drivers and restrainers of prosperity in nations, in a report and website accompanying the 2007 Prosperity Index. This year, the Institute has sponsored further research, leading to new lines of inquiry and new findings.

The guiding principles of the 2008 Prosperity Index remain unchanged from the previous edition:

- The Index takes a holistic view of prosperity. This means a view that extends beyond just material wealth, and includes other factors such as social capital, health, the environment, political liberty, and overall quality of life.
- Operationally, holistic prosperity is defined as the combination of two widely-available statistical measures: material wealth, measured by long-term growth in average income per person, and life satisfaction, measured by average levels of life satisfaction as reported on national surveys (see the callout, *A Fascination with Happiness* on page 14).
- The Index is an index of drivers, not results. The top countries in the Index are not necessarily those that achieve the highest outcomes in material wealth and life satisfaction. Rather, the top countries are those that have, relative to their peers, the most *factors that promote* wealth and wellbeing. This is why countries are ranked based on a weighted average of indicators of *Economic Competitiveness* (drivers of differences between countries' relative levels of material wealth) and *Comparative Liveability* (drivers of differences between countries' relative levels of life satisfaction). Citizens of the top countries in the Index pursue wealth, the yardstick by which prosperity has been

traditionally measured. At the same time, they pursue broader wellbeing, in areas such as health, leisure time, family life, the environment and social capital (for a comparison of drivers and performance, see the callout, *Prosperity Performance* on page 10).

- The Index is produced using a quantitative approach. The Index includes only factors for which a statistical link with material wealth or life satisfaction can be shown.

Citizens of the top countries pursue broader wellbeing, in areas such as health, leisure time, family life, the environment and social capital.

- The Index is produced in the spirit of “progress not perfection”. Our understanding of the drivers of prosperity increases each year, as new data and techniques become available. This Index reflects this progress, and in years to come it will continue to change to reflect advances in knowledge.

The 2008 Index also improves on last year's Index in a number of ways. Hence, readers of this Summary and Commentary will find there is much that is new.

SUPPORTING NEW RESEARCH: EXPANDING OUR UNDERSTANDING OF PROSPERITY

The Legatum Institute was active in promoting new research into prosperity in 2008. The Institute sponsored research by Harvard University's Robert Putnam on religion and wellbeing, research by Ruut Veenhoven of Erasmus University in the Netherlands on freedom and wellbeing, and an interdisciplinary academic symposium on topics in prosperity in which more than 20 leading scholars participated.

The Institute also commissioned three research and policy papers on key issues in prosperity, the full text of which is available in the *2008 Prosperity Index Report*, as well as online at www.prosperity.com.

"Entrepreneurship and Economic Growth", by David Audretsch

Audretsch, the Director of the Max Planck Institute of Economics in Jena, Germany, and the Ameritech Chair of Economic Development at Indiana University, offers new thinking on the link between entrepreneurship and economic growth. He explains why policymakers lost interest in entrepreneurship during the postwar period and argues that entrepreneurship is now central to economic progress. "Entrepreneurship provides an important mechanism that actually transforms investments in knowledge, ideas and creativity, into innovative activity", he writes.

"Happiness and Charity", by Arthur Brooks

Arthur Brooks is the Louis A. Bantle Professor of Business and Government Policy at Syracuse University and the author of a new book, *Gross National*



Happiness: Why Happiness Matters for America – and How We Can Get More of It. He offers an engaging survey of new research – including his own – that links charitable giving and life satisfaction. He contends that "the evidence is clear that gifts of money – as well as gifts of time – to charitable organisations, houses of worship, and other worthy causes, bring authentic happiness to givers".

"The Role of Freedom and Control in Explaining Happiness", by Paolo Verme

Paolo Verme is a professional development economist and is a contract Professor of Economics at the University of Turin and at Bocconi University in Milan. He analyses

the World Values Survey data in detail, finding a surprisingly robust link between freedom of choice and wellbeing in more than 80 countries worldwide. He suggests a theoretical explanation for this link and speculates on possible policy implications. "Public policies which focus on other institutional aspects such as marriage, religion or political orientation may not be so powerful in delivering happiness as they may have negative effects on freedom and control and, through this variable, reduce the positive effect that these factors have on happiness", he suggests.

We encourage readers with an interest in this area to review the research for themselves in the full *Prosperity Index Report* available for download at www.prosperity.com.

- In addition to this commentary, the Legatum Institute has published a full report on the research that produced the Index, covering methodology, related academic literature, results and data sources, and full country profiles for the 104 countries in the Index. The full report also includes three research papers by leading scholars on key topics in prosperity: on entrepreneurship by David Audretsch, on charitable giving by Arthur Brooks, and on freedom of choice by Paolo Verme (see the callout, *Supporting New Research* on page 20).
- Drawing on the Gallup World Poll and other new data, the country coverage of the Index has been expanded from 50 countries in 2007 to 104 in 2008.
- Based on new statistical research, the Index uses a much wider range of indicators. This year the Index employs 16 drivers that show a strong statistical relationship with differences in countries' relative levels of material wealth (indicators of *Competitiveness*), and 28 drivers that show a strong statistical relationship with differences in countries' relative levels of life satisfaction (indicators of *Liveability*). For a description of some of the new indicators in the Index, see the callout, *New Factors* on page 18.
- The Index includes a new weighting methodology, which assesses how the drivers of prosperity change as countries become wealthier (see the callout, *What Explains Differences in National Prosperity?* on page 22).

We encourage readers with an interest in this area to review the research for themselves, in the full *Index Report* available to download at www.prosperity.com, and to take advantage of the extensive online tools for analysis available on the website.

In what follows, we provide our own interpretation of the Index research and results. In the study of prosperity, many findings remain contested and imprecise. But in the lives of people and the policies of nations, decisions must be made on imperfect information. This book presents our views on the 2008 Prosperity Index results and the individual and policy choices that can best promote global prosperity.



WHAT EXPLAINS DIFFERENCES IN NATIONAL PROSPERITY?



We assigned weights to the various components of the Index based on the degree to which each component explains why some countries are more prosperous than others. To produce this analysis, we used 40 years of data on economic growth, and data on average life satisfaction for more than 100 countries.

We also assessed the ways in which the strength of the relationship between each Index component and national prosperity varies as countries become wealthier. For instance, in poorer countries, basic factors such as governance and foreign aid dependence appear to have a large impact on income growth, whereas in richer countries, high-tech innovation and

entrepreneurship unsurprisingly play a much larger role.

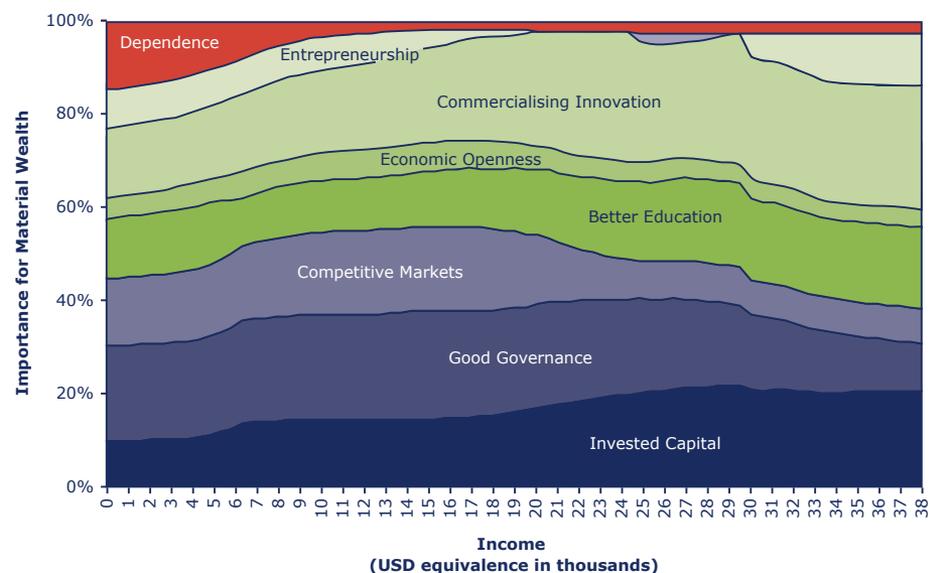
There are limitations to what statistical analysis can tell us about the drivers of prosperity. In particular, this type of statistical analysis can identify relationships, but cannot determine whether these relationships are causal. The Prosperity Index presents the results of an investigation into the drivers of

prosperity, not a precise measurement of these drivers (for more details, see the full *Prosperity Index Report*).

It is important to note that foundational social capital factors such as family, friends, faith, and health, all of which are strong determinants of human happiness, are generated and experienced by individuals, not entire countries. In other words, it is individual people who are

Economic Competitiveness Weights

The graph below shows the relative weights of the factors in the Economic Competitiveness Index and how these weights change as countries become wealthier. The width of each bar indicates the factor's weight, as a percentage of a total Index score. Generally, the weights do not change significantly. That is to say, the fundamental drivers of differences in long-term economic growth rates amongst rich countries are similar to those of poor countries. Two notable exceptions are governance and dependence on commodity exports, which are problems for poor countries but not rich countries. By contrast, the importance of innovation rises markedly as countries become wealthier.



2008 COUNTRY STANDINGS

Rather than replicating other measurements that rank countries by their actual levels of material wealth or life satisfaction, the Index produces a ranking based on the conditions that foster prosperity.



THE 2008 COUNTRY STANDINGS

The Leaders in Promoting Prosperity

The top spot in the 2008 Index is claimed by Australia, followed by Austria and Finland in a tie for second place. These countries are followed closely by Germany, Singapore, and the United States, also in a tie. While there are limits to what a purely quantitative analysis can tell us, as of 2008, these countries appear to have the strongest attributes that promote the holistic prosperity of their citizens.

What do the successes of Australia, Austria and Finland suggest? Each nation has a well-rounded set of attributes, scoring well in a very broad range of drivers of prosperity, and outstandingly in a few. Australia makes a particular virtue of entrepreneurship as an engine of economic competitiveness, as well as pursuing broader societal wellbeing as an effective democracy with high levels of citizen volunteering and charitable giving. Austria turns in top scores in education, a key to long-term income growth, and also in health, a key to a country's liveability. Finland boasts excellent governance, helping to drive both wealth and wellbeing in that country. In addition, the Finns report the greatest satisfaction with their freedom to choose the course of their own lives of any country in the Index.

Interestingly, a diverse group of countries – three in Europe, two in Asia, and one in North America – take up the top six spots in the Index, in part because of imbalanced performances by the leading countries in other regions. Several Nordic countries do very well in liveability, but less well in competitiveness. Several Asian countries, on the other hand, have achieved tremendous leaps in income, but do less well in promoting the wellbeing of their citizens.

Unbalanced Performers

In general, the Nordic countries (Denmark, Sweden and Norway) achieve top scores in the drivers of life satisfaction (and indeed, Denmark currently rates as the “world's happiest country” – see the callout, *Prosperity Performance* on page 10). These Nordic countries are rich, highly democratic, scrupulously incorrupt, extremely healthy, enjoy vibrant community life, and their citizens have great personal and political freedom to make choices in determining the course of their own lives. No other region can match the Nordic performance in all of these indicators of liveability.

However, at the same time, the Nordic countries lack economic vibrancy. They therefore score relatively poorly on our Index of Economic Competitiveness. The Nordics are capital-rich – particularly Norway, enjoying a boom in oil wealth – and have excellent standards of education. But the Nordic countries score relatively poorly on indicators of innovation, competition in domestic markets, and particularly, on entrepreneurship. Relatively few citizens in these countries choose to go into business for themselves. This lack of entrepreneurial flair suggests the Nordic countries may not be taking full advantage of their citizens' individual potential, and may also warn of potential constraints on future growth (see the callout, *Supporting New Research* on page 20).

Some Asian countries fall into the opposite category. The Asian leaders (Singapore, Hong Kong, Taiwan, and Japan) take top positions in our Index of Economic Competitiveness. These countries and territories have achieved the fastest income growth of perhaps any on earth, surging from poverty to material prosperity in a single generation. They boast excellent mass education, highly effective and market-oriented regulation, a focus on income growth rather than a

dependence on foreign aid, and an ability to engage effectively with the global economy. They particularly excel at taking advantage of the market demand and advanced technologies on offer from the world's consumers and businesses (although the Asian economies have been most successful at commercialising foreign technologies, and show some weaknesses in generating their own technological innovation).

At the same time, while few countries can equal Asia's long-term economic growth rates, most Asian countries show weaknesses in liveability. Most notable is equality of opportunity. The Gallup World Poll finds that relatively few people

in Hong Kong, Singapore, or South Korea report that they agree with the statement that "in this country, people who work hard can get ahead". This is all the more remarkable considering the high economic growth rates in these countries. Perhaps, however, it is not so remarkable when one considers the level of exclusion of women from leading positions in the economy and politics in Asia. Other weaknesses in liveability common to many countries in Asia include a degraded natural environment and extremely long working hours. Having achieved rapid advances in material wealth, citizens of the leading Asian economies may wish to focus on the drivers of wellbeing.



DOWN UNDER IS ON TOP

Australia earns the top position in the 2008 Legatum Prosperity Index. The 'Lucky Country' has reinvented itself as a wealthy service-oriented economy, and earns its top spot by combining economic competitiveness with good scores on liveability indicators, including health, charitable giving, and effective governance.

High levels of capital investment and innovation are key to Australia's success in terms of material wealth. No doubt this can be partially attributed to policies pursued from the 1970s to the 1990s that deregulated labour and financial markets, controlled public spending and privatised state industries. Australia's extremely high score on regulatory quality, a component of the World Bank Governance Indicators that measures market-oriented policymaking, reflects this history.

Perhaps as a partial consequence of Australia's wealth, levels of charitable giving in the country are extremely high, according to the Gallup World Poll. This boosts Australia's liveability score considerably. Although Australia's indigenous population lives with the adverse effects of socio-economic disparities, the country enjoys good community life scores overall, bolstered by strong norms of civic participation. Australians have one of the highest sport participation rates in the world, and leisure time of over seven hours a day on average, according to Gallup.

But leisure time, environmental satisfaction, land area devoted to nature, and air quality – Australia scores well on all of these – are just the icing on the

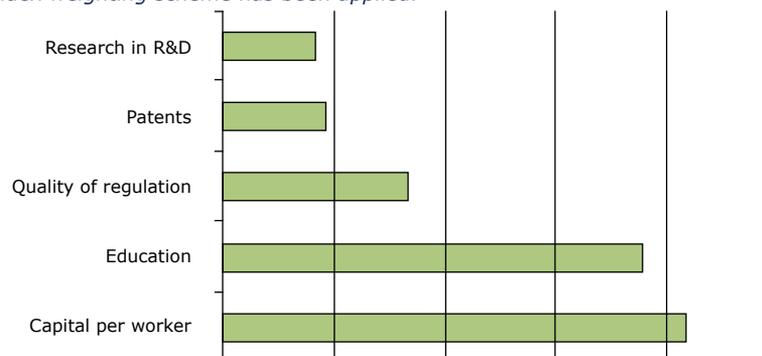
cake. Australia earns its high Index score by getting the fundamentals right. Australians enjoy robust good health, with an average health-adjusted life expectancy of 72.6 years, and the Australian government earns high

scores on corruption control and overall effectiveness, supporting the country's quality of life in many areas.

Country profiles are available for all 104 countries in the Prosperity Index at www.prosperity.com.

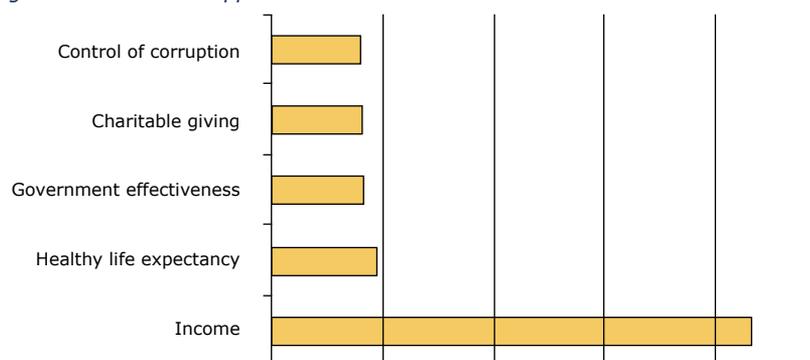
Indicator Score in the Prosperity Index

Key score drivers for economic competitiveness. The graph below shows the competitiveness factors with the greatest influence on Australia's score, after the Prosperity Index weighting scheme has been applied.



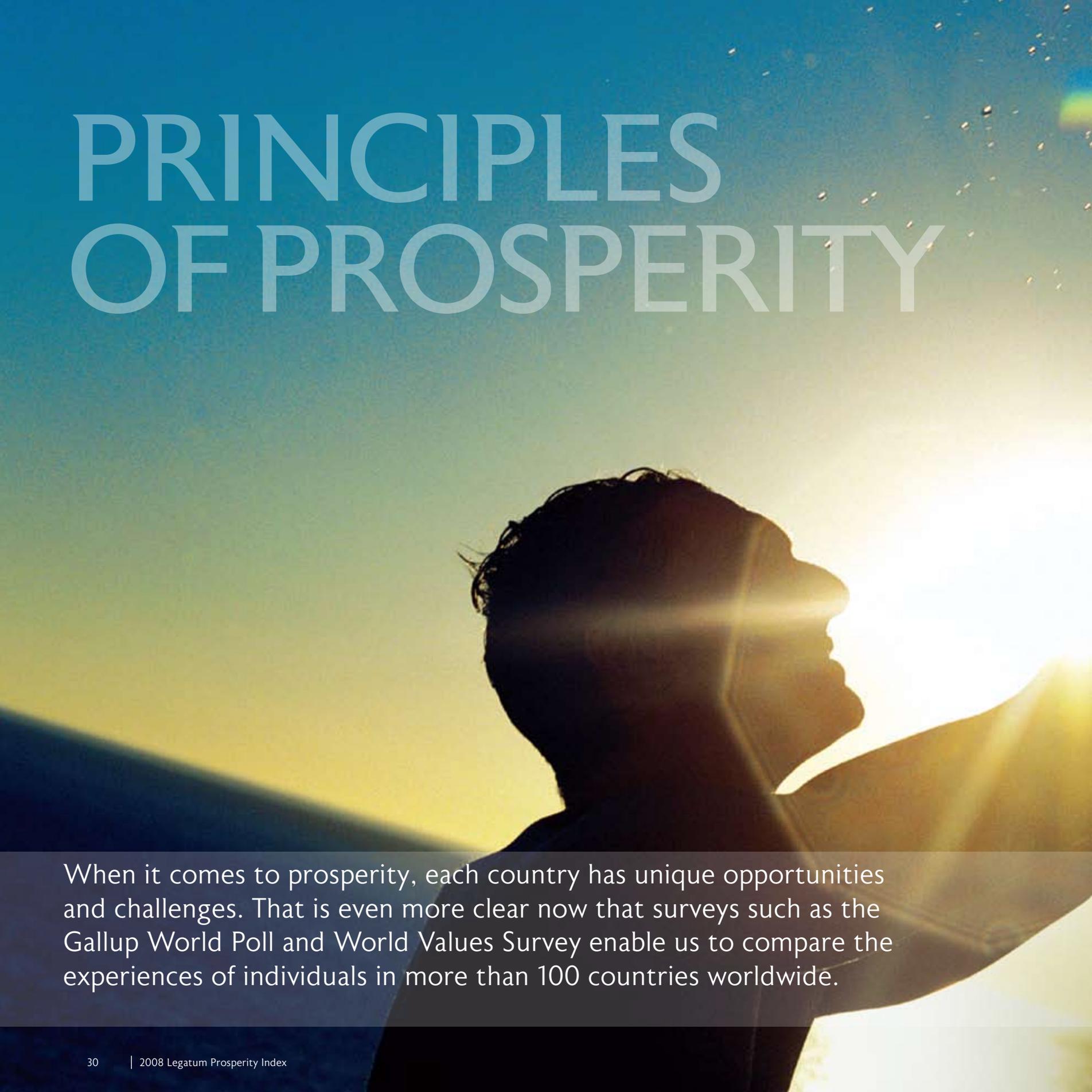
Indicator Score in the Prosperity Index

Key score drivers for comparative liveability. The graph below shows the liveability factors with the greatest influence on Australia's score, after the Prosperity Index weighting scheme has been applied.





PRINCIPLES OF PROSPERITY

A silhouette of a person's head and shoulders is shown in profile, looking upwards towards a bright sun. The background is a clear blue sky with numerous small water droplets or raindrops scattered throughout. The sun is positioned on the right side of the frame, creating a strong lens flare and illuminating the scene. The overall mood is one of hope and aspiration.

When it comes to prosperity, each country has unique opportunities and challenges. That is even more clear now that surveys such as the Gallup World Poll and World Values Survey enable us to compare the experiences of individuals in more than 100 countries worldwide.

A close-up photograph of a hand reaching upwards against a bright blue sky. The hand is silhouetted against the light, and numerous water droplets are suspended in the air around it, creating a sense of motion and freshness. The background is a clear, vibrant blue sky with a bright light source on the left, causing a lens flare effect.

Nonetheless, the statistical research presented in the *2008 Prosperity Index Report* identifies some clear patterns in the data on global wealth and wellbeing. In what follows, we highlight eleven Principles of Prosperity based on these patterns and suggest some potential implications for individual and policy choices.

1. FREEDOM OF CHOICE IS CRUCIAL

FINDING: There is a robust correlation between perceived freedom of choice and self-reported life satisfaction in nearly every country studied, across regions and income levels.



OUR VIEW: Wellbeing in European and North American countries has been studied for decades. In the past few years, however, new surveys such as the Gallup World Poll and World Values Survey have produced high-quality datasets for Africa, the Middle East and Southeast Asia.

While some findings vary, there is one factor that appears to have a large impact on wellbeing in nearly every country studied: whether or not individuals perceive that they have freedom of choice and the ability to control the way their lives turn out. In nearly every country, people who report high levels of freedom of choice and control over how their life turns out are happier than those who do not. This is as true in Nigeria as it is in the Netherlands. Furthermore, the countries where people report the highest levels of freedom of choice, notably the United States and New Zealand, followed by Canada, Australia, and Austria, tend to enjoy higher levels of life satisfaction than other countries.

Why is this? Freedom of choice implies the existence of opportunity, and the absence of restraint by arbitrary authority. For people of all nations, cultures, income levels, and backgrounds, being free to choose entails having the chance to create better lives for themselves and their families. Freedom of choice in turn is anchored in human dignity and human liberty. Dignity describes the inherent value and sanctity that defines every person; liberty means the capacity to think, speak, and work freely and the creativity to produce, build, and grow freely. Nations that affirm human dignity and liberty equip their citizens with the freedom to choose the best course for their lives and realise their individual potential.

Freedom of choice does not mean license to harm. The strong connection between freedom of choice and wellbeing holds only for people making choices to better their own lives, not to

Freedom of choice implies the existence of opportunity, being free to choose entails having the chance to create better lives for themselves and their families.

The strong connection between freedom of choice and wellbeing holds only for people making choices to better their own lives, not to harm the lives of others.



harm the lives of others. Nor does freedom of choice mean that people always choose wisely. Rather, the research shows that people are happiest when they are free to realise the benefits of their good choices – and to learn from the consequences of their bad choices. It has been said that good judgment comes from experience, and experience comes from bad judgment. If government policy, however well-intended, denies people the freedom to learn from their choices, they arguably are also denied the opportunity to gain the experience and wisdom needed for their own personal development.

There are many potential impediments to freedom of choice. Poverty, corruption, illness, illiteracy, oppression, excessive regulation, cultural restrictions, and many other factors can all constrain people's ability to chart their own course. Looking through the country rankings, citizens report the least freedom to choose in places ranging from Algeria to Macedonia to Nepal to Zimbabwe. The reasons vary. Algeria has been afflicted by decades of civil war and terrorist violence; Macedonia suffers from persistent corruption and economic stagnation; Nepal has endemic poverty and political instability; Zimbabwe's many torments include tyranny and hyperinflation. As different as these nations are, in each of them the people have little chance to choose a better life for themselves.

There is almost as much diversity among countries where people are happy with their freedom to choose. Some are wealthy (Norway and Finland), while others are poor yet growing (Vietnam and Ghana). Some are secular (Denmark and Sweden), others are predominantly Christian (Costa Rica and the Philippines), Buddhist (Thailand), or Islamic (Malaysia and the United Arab Emirates). In all of these places, people's happiness with their freedom to choose bodes well for their futures.

COMPARING PROSPERITY IN CHINA, TAIWAN AND HONG KONG



Any attempt to compare the rankings of China, Taiwan and Hong Kong is complicated by disparities in geography, population, and history. Nevertheless, some interesting findings emerge. Despite its recent rapid economic growth, mainland China ranks far down the economic competitiveness scale, compared to Taiwan and Hong Kong, because the mainland's levels of productive capital investment, education, and income remain very low when measured on a per capita basis.

On the liveability side, the divergence is also substantial. Taiwan and Hong Kong have political systems that are significantly more free and functional than that of China, with Taiwan leading the group on political rights and Hong Kong leading on control of corruption. On environmental indicators, citizens of the People's

Republic of China – perhaps with lower expectations – report good air quality while Hong Kong has one of the worst air pollution scores in the world (ironically enough, mostly because of pollution emanating from China's Guangdong Province). On other social indicators, including charitable giving and religious freedom, Hong Kong and Taiwan far exceed the performance of the People's Republic.

All three countries and territories, however, have one thing in common: excellent levels of innovation, or, more accurately, commercialisation of innovation. Many a foreign technology, as anyone who has done business in the region can attest, has been adopted and then improved by local companies.

Country	Overall Rank	Economic Competitiveness Rank	Comparative Liveability Rank	Income	Capital Per Worker	Secondary Education	High Tech Exports	Patents	Control of Corruption	Political Rights and Civil Liberties	Clean Air	Volunteering	Charitable Giving	Religious Freedom
Hong Kong	8	2	19	19	17	3	33	9	15	4	-42	-4	13	7
Taiwan	20	5	36	4	16	6		18	4	7	-20	-4	2	10
China	53	50	58	-5	-6	-5	16	21	-7	-19	9	-17	-13	-21

2. GOVERNMENT SHOULD BE EFFECTIVE, HONEST AND LIMITED

FINDING: Governments that exercise power responsibly and are accountable to their citizens dominate the top quartile of the rankings for both material wealth and life satisfaction.

OUR VIEW: While government does not create prosperity, it does create an environment which will encourage productive endeavour to either flourish or fail. Citizens are most empowered to pursue wealth creation and happiness when their governments maintain basic order, apply impartial justice, respect human rights, and function with transparency and integrity. In contrast, citizens living under oppression, ineptitude, and corruption face severe obstacles to achieving economic growth and life satisfaction.

Democratic governance can take many forms and the top ranked countries display a wide diversity of systems. But they have in common a few basic and indispensable characteristics. These include the rule of law, an independent judiciary, respect for human rights and civil liberties, multiple political parties, media freedom, transparency, institutional checks and balances, and rulers who are accountable to their citizens through regular competitive elections.

Besides the structure of a government, two other areas are vital for good governance: what a government does – and what it does not do. First, a government should be *effective*, meaning it provides basic services for its citizens honestly and efficiently. This includes areas such as national security, law enforcement, judicial services, regulations, revenue collection, and border control. Second, a government should be *limited*, meaning that its power is restrained by its citizens and by law, and that it respects the proper roles of the private sector. Ways that governments exceed their limits include everything from

excessive taxation, onerous regulation, and violation of property rights, to abuse of human rights, stifling of civil society, and encroachment on commercial enterprise. In short, governments cannot create prosperity, but do their job best when they respond to the demands of their citizens and foster the conditions for them to create prosperity.

Every one of the top 29 countries in the overall Prosperity Index scores half a standard deviation or more above the global mean on good governance. The weightings are equally telling (see the callout, *What Explains Differences in National Prosperity?* on page 22). At a broad range of income levels, governance is one of the strongest factors – and in some cases the strongest factor – behind economic growth and happiness.

Singapore and Hong Kong are the exceptions that prove the rule. These unique city-states are the only two governments in the top quartile that are not fully democratic and accountable to their citizens. Yet they rank very well in other governance areas such as efficiency, effectiveness, rule of law, lack of corruption, and respect for economic liberty.

Although good governance does not create prosperity, it does create an environment in which economic competitiveness and comparative liveability flourish.

3. FOR POOR COUNTRIES, RAISING INCOMES IS THE FIRST PRIORITY

FINDING: In countries with an average income per person of roughly US \$10,000 or less, income levels are the single strongest predictor of how satisfied, on average, people will be with their lives.

OUR VIEW: While “money can’t buy happiness”, it is equally true that a lack of money can cause great misery. In rich countries, without exception, people on average report themselves satisfied with their lives. By contrast, in many poor countries, such as Zimbabwe and Pakistan, the stresses of hunger, poor housing, and physical insecurity appear to be so overwhelming that large numbers of people report themselves dissatisfied with the lives they lead. This suggests that for countries at the lower end of the income scale, raising incomes via long-term economic growth should be among the top priorities.

To be sure, poor countries have strengths in many other areas. The highest scores on many of the liveability indicators in the 2008 Prosperity Index are to be found in the developing world. Countries including Peru, Bolivia and Kenya have the most favourable climates (measured via a temperature average that has been weighted according to where their populations reside). Wealthy New Zealand leads on the environmental indicators in the Index, but developing Botswana is close behind. Panama and Colombia are ranked highest on family life, with divorce and widowhood relatively rare and most people reporting they have someone to rely on in times of need, and the Dominican Republic and Venezuela lead in indicators of religious life.

Nonetheless, it stands to reason that for the destitute, even the most pleasing natural environment will not produce happiness. This simple observation is borne out by the data. At low levels of income, the pernicious impact

of poverty tends to outweigh the positive impacts of the other factors described above. For the poorest countries, raising incomes through economic growth will achieve the greatest wellbeing dividends. And today’s poor countries could well become tomorrow’s prosperity leaders, if they can meet the challenge of preserving their traditional strengths as they climb the prosperity ladder.



4. FOR RICH COUNTRIES, PROSPERITY MEANS MORE THAN JUST MONEY



FINDING: Each step increase on the life satisfaction scale is associated with a doubling of per capita national income.

OUR VIEW: The “Easterlin Paradox” is one of the earliest and most established findings of academic research on human wellbeing. Identified in 1974 by Richard Easterlin, the “paradox” is that even though more income may appear to produce higher levels of life satisfaction, survey data indicate that rich countries that have become even richer have not become any happier.

New data, particularly from the Gallup World Poll, have cast some doubt on this “paradox”. These new data suggest that the relationship between income and life satisfaction continues to hold all the way up the income scale. These new findings have led to an avalanche of recent newspaper headlines to the effect that “money is what matters, after all”.

These headlines are overstating the case. The new data show a significant relationship between life satisfaction and income, but nonetheless indicate diminishing returns to additional income. That is to say, the first \$10,000 in annual income makes a big difference, providing essentials like food and shelter. The next \$10,000 in income matters a bit less. The \$10,000 after that matters less still. Because the relationship between income and life satisfaction is logarithmic, each step increase on the life satisfaction scale requires a doubling of income: a person earning \$10,000 who earns an additional \$10,000 experiences the same boost in life satisfaction as a person earning \$100,000 who earns an additional \$100,000. Hence at high levels of income, vast sums must be added to make any noticeable difference.

For most people in rich countries, non-material factors such as family, community, and faith will have a bigger impact on their wellbeing than further increases in income.

The main lessons drawn from Easterlin’s research remain valid: for most people in rich countries, non-material drivers will have a bigger impact on their wellbeing than changes in income (this is just as true when looking at differences between average life satisfaction levels among nations – see the callout, *What Explains Differences in National Prosperity?* on page 22). Citizens of rich countries may wish to consider the liveability drivers carefully as they evaluate their personal choices. It has long been said that wealth poses a more difficult test of a person’s character than poverty, as wealth offers more choices, for good and for ill, and needs to be managed responsibly.

PROSPERITY IN SUB-SAHARAN AFRICA



Out of the 15 Sub-Saharan African countries featured in this year's Index, only three are not ranked in the bottom quartile of prosperity: South Africa (38th), Botswana (45th) and Namibia (55th).

These rankings reflect the fundamental and often well-publicised problems of the region. One of these is poverty and capital flight: aside from the three countries mentioned above, a lack of capital investment hampers accumulation of material wealth and low incomes restrain wellbeing. Poor governance, low levels of education, high dependence on foreign aid, chronic unemployment and low average life expectancies are further

well-known obstacles to national prosperity in Africa.

While governments in Sub-Saharan Africa need to alleviate sources of misery for their citizens, the region maintains comparatively high levels of social support via community and religious life. There are also signs of optimism: notably high proportions of the population believe that working hard will enable them to get ahead. Exceptions are Mali and Zimbabwe, where a lack of equal opportunities goes along with perceptions of restricted individual choice. Dissatisfaction with personal freedom also persists in Sudan, Nigeria and Cameroon, and – perhaps a

legacy of the apartheid regime – in South Africa as well.

But there are many bright spots. Well-governed Botswana has, over a period of 30 years, achieved one of the fastest rates of income growth in the world (although HIV/AIDS infection rates are extremely high). Namibia is unique in the region in having no severe weaknesses (and one notable strength, equality of opportunity). And South Africa has enjoyed success in enabling individual entrepreneurship by lowering the costs of formalising a business.

Economic Competitiveness								
Overall Rank	Country	Rank	Growth in invested capital	Good governance	Better education	Economic openness	Entrepreneurship	Foreign aid
38	South Africa	41	-6	5	1	-6	10	4
45	Botswana	54	1	4	-10	-6	7	2
55	Namibia	61	-4	-1	-6	-1	0	-7
86	Ghana	79	-10	-2	-10	-7	-6	-20
94	Nigeria	89	-11	-13	-7	-8	-9	-5
92	Senegal	90	-10	-5	-15	-7	-15	-20
96	Mozambique	91	-11	-6	-19	-5	0	-30
96	Kenya	92	-11	-9	-16	-7	-7	-12
100	Tanzania	93	-11	-6	-17	-6	-7	-26
93	Cameroon	94	-10	-12	-9	-11	-17	-5
99	Zimbabwe	98	-10	-21	-10	-7	0	-15
102	Mali	100	-11	-7	-18	-8	-17	-24
102	Zambia	101	-11	-10	-12	-6	-3	-19
94	Sudan	102	-9	-15	-15	-8	-9	-16
101	Central African Republic	104	-11	-17	-16	-14	-21	-20

Comparative Liveability											
Overall Rank	Country	Rank	Freedom of choice	Equality of opportunity	Good governance	Pleasant environment	High incomes	Good health	Low unemployment	Community life	Religious belief
45	Botswana	38	6	1	5	17	-1	-18	-7	-10	
38	South Africa	43	-8	15	5	-4	-2	-13	-16	-4	9
55	Namibia	50	3	11	0	8	-5	-3	6	-7	
86	Ghana	85	10	6	1	4	-9	-6	0	8	
94	Sudan	86	-13	2	-20	2	-10	2	-8	-3	
93	Cameroon	89	-8	-4	-13	6	-10	-21	-20	-3	
92	Senegal	92	-2	-6	-2	-10	-10	-6	-40	-2	
101	Central African Republic	95	-5	11	-13	10	-10	-9	3	10	
99	Zimbabwe	96	-24	-10	-19	0	-10	-18	5	-6	12
96	Kenya	97	-5	3	-4	8	-10	-5	-31	-4	
96	Mozambique	98	-6	5	-2	1	-10	-2	-11	-5	
94	Nigeria	99	-8	1	-10	-7	-11	-4	5	9	12
102	Zambia	101	-4	8	-6	3	-11	-11	-42	-4	
102	Mali	102	-15	-20	2	0	-11	-16	-20	-10	
100	Tanzania	104	-1	10	-5	3	-11	-20	6	-7	12

FAITH AND HAPPINESS

In the past decade, strong religious faith has come to be associated by some people with terrorism and violence, as extremist groups have claimed religious justifications for their actions. In the Prosperity Index, however, religious engagement is a positive indicator. Why?

A repeated finding of research on the science of happiness is that there is a positive link between religious engagement and wellbeing. For instance, people who report that God is very important in their lives are on average more satisfied with their lives, after

accounting for their income, age and other individual characteristics. Research also suggests that religious people's happiness is less vulnerable to fluctuations in economic and political uncertainty, personal unemployment and income changes.

The Prosperity Index identifies similar effects at the country level. A number of highly religious countries are happier, on average, than one might expect based on their standard of living alone. This effect is perhaps most pronounced in Mexico, El Salvador, the Dominican Republic,

Indonesia, Venezuela and Nigeria. As this diverse list suggests, this effect can be found in many regions and for many faiths.

That said, one must also account for the negative impacts of religious intolerance or extremism. The Prosperity Index does so with another indicator, religious freedom, which also correlates with average national life satisfaction. Countries with high levels of religious faith score well on the Religious Life indicator in the Index, but they achieve top marks only if they have religious freedom as well.



5. ENTREPRENEURSHIP IS A PROMISING PATH TO MATERIAL WEALTH

FINDING: Entrepreneurship indicators show a significant statistical relationship with long-term economic growth in both rich and poor countries.

OUR VIEW: In almost any given economy, small businesses are the largest employers. In emerging markets, small businesses often offer the best hope for economic growth and social stability through the creation of worthwhile, sustainable employment.

The statistical analysis detailed in the *2008 Prosperity Index Report* suggests that entrepreneurship plays multiple roles in growth. In poor countries, it is the cost of starting a



business that shows the strongest relationship with income growth. In these countries, a few uncompetitive businesses often dominate economic production. With capital hard to come by and the cost of starting a new business prohibitive, it is extremely difficult to dislodge poorly-performing businesses that have strong political connections. The countries that can overcome this challenge are often those with low barriers to starting businesses. This allows capital to come into the formal sector, where it can be invested productively and pose a serious competitive challenge to more established but under-performing enterprises.

In rich countries, by contrast, the entrepreneurship indicator that shows a significant relationship with long-term economic growth is the rate of business ownership. In these countries, the vast majority of the population has entered the formal economy, and attracting capital is less of a problem – provided that regulations are sound and tax rates are low. However, there are reserves of creativity and innovation that are untapped (see the callout, *Supporting New Research* on page 20). For instance, a university professor may stumble upon a research breakthrough with great commercial implications. However, her university is not the place to commercialise it, and if the idea is sufficiently complex, she will have a hard time convincing a large company to invest in it. In countries that encourage entrepreneurship, however, she can use her idea to start a business that may one day grow to be the next Google.

WHO'S GOING PLACES?

The Economic Competitiveness section of the Index measures achievement: which countries have done the most to increase the wealth of their citizens? But there is also the question of progress: which countries are doing the most to achieve the highest growth rates today, to top the competitiveness rankings tomorrow? To answer this question, we have recalibrated the Economic Competitiveness Index to assess performance over the past five years, and present the results in the table below.

Last year the top five were Ireland, Croatia, Portugal, Greece and China. This year the same phenomenon dominates the top ranks: catch-up growth by the newer European Union members, with Slovakia and Bulgaria leading at 1st and 2nd, and Romania close behind at 7th (not shown on the chart). Joining the

European Union seems to make the income convergence predicted by economic theory a reality. Like Ireland and Portugal before them, today's new EU members appear on their way to joining the ranks of the world's richest countries.

By contrast, the phenomenon dominating the bottom five places is insecurity (see the callout, *Security and Prosperity* on page 48). Several countries, most notably Zimbabwe, have registered actual net destruction of their stocks of physical and human capital. Sierra Leone has also experienced the shock of political instability and war in recent years.

More positively, another phenomenon highlighted by these rankings is that of convergence in global incomes. Though predicted by economic theory, historically, this has not occurred: while economic growth has continued in the

rich world, in many of the poorest regions, blighted by insecurity or poor governance, the pace of growth has been much slower. The result has been actual divergence of global incomes, and a growing material wealth gap between the richest and poorest nations.

While severe problems persist in many countries, the global wealth gap is starting to narrow. China ranks 6th on our "who's going places" ranking, and India ranks 10th. Recent economic growth rates in these countries tell the same story. Both economies have recently grown faster than almost any country in the rich world. Because these two giant nations are home to more than two billion people, these improvements in competitiveness are bringing about a dramatic lessening of the global wealth gap, and are very good news for global prosperity.

Rank	Country	Invests productively			Commercialises new ideas				Avoids dependence	
		...via growth in invested capital	...via good governance	...via competitive markets	...via better education	...via economic openness	...by commercialising innovation	...via entrepreneurship	...on commodity exports	...on foreign aid
1	Slovakia	41	8	0	1	20	4	15	-16	8
2	Bulgaria	39	0	-3	-8	17	0	9	5	8
3	Singapore	-10	19	6	-4	47	25	4	-3	7
4	Taiwan	-4	8	32	-1	10	19	2	1	8
5	Chile	-3	11	9	1	5	0	9	-1	7
100	Ecuador	-1	-15	-19	2	-6	-14	-3	-21	-16
101	Central African Republic	-6	-18	7	-7	-14	-10	-21	-16	-3
102	Lebanon	-12	-7	-12	-8	-5	-7	-14	6	-26
103	Cambodia	-11	-13	4	-14	-7	-8	-21		-20
104	Zimbabwe	-15	-21	3	-7	-7	-9	0	3	-18

6. GROWTH IN INVESTED CAPITAL IS CRUCIAL TO LONG-TERM ECONOMIC GROWTH

FINDING: The factor with the strongest statistical relationship to economic growth is the growth in the value of fixed capital investment (such as factories and machinery) per worker.

OUR VIEW: Every country has financial capital, but all too often it is dormant and unproductive. Sometimes it is hidden under the mattresses of the poor, or in their informal homes, because the absence of secure property rights makes it impossible for the poor to put these assets to use (for instance, a squatter without legal title to his or her home cannot mortgage this home to start a small business). Sometimes a country's financial capital becomes flight capital, which seeks a more stable and welcoming environment in foreign banks or real estate.

It is difficult to lure this capital out of its hiding places and back into a country's economy because productive assets such as factories are high-profile and immobile – easy targets for thieves or unscrupulous government officials. Turning hidden capital into invested capital thus requires a great leap of trust by investors, and this usually only happens in stable business environments offering sound property rights, the impartial application of just laws, and good economic policy.



THE PERSONAL PROSPERISCOPE:TM MEASURING YOUR HAPPINESS

The 2008 Prosperity Index analyses aggregate wellbeing in nations. But surely the research on the science of happiness has something to say about the choices we make as individuals – about where to live, whether or when to marry, or how to spend our time?

In fact, surveys such as the Gallup World Poll, World Values Survey, US General Social Survey, the European Quality of Life Survey, and the German Socio-economic Panel Survey, have addressed these questions in detail. Some of the relationships identified by scholars analysing these survey results are fascinating. For instance:

- People living close to a coastline tend to be happier.
- Long commuting times may have a large negative impact on one's life satisfaction.
- Long commuting times of one's partner also have a negative impact.
- Parental divorce during childhood appears to have a negative impact on wellbeing, lasting into adulthood.
- Women tend to be happier than men.

This research on survey data from hundreds of thousands of people in more than 100 countries worldwide has created a new body of knowledge, often called the "science of happiness".

What can this new science tell you? Use our Personal Prosperiscope to find out. Answer the same survey questions that were used in major research studies on human wellbeing, and the Prosperiscope will tell you what factors may be having the biggest impact on your satisfaction with life.

The Personal Prosperiscope is available online at www.myprosperity.com.



7. ECONOMIC OPENNESS CAN HELP POORER COUNTRIES CATCH UP FASTER

FINDING: Economies in which foreign investment and trade play a greater role grow more rapidly than closed economies.

OUR VIEW: Many of the factors in the Prosperity Index have a simple relationship with economic growth. Increases in capital and education contribute directly to the value of physical and human capital and thus directly increase economic output. Poor governance and excessive bureaucracy impose costs on business and thus restrain growth.

Foreign investment and trade are different. These factors are measured as a percentage of economic output – that is, based on their relative weight in an economy, not their direct contribution to output. Analysis of these data reveals a strong relationship between the weight of foreign trade and investment and long-term growth.

In part, this is because openness helps poorer countries catch up. Exposure to foreign trade and investment enables poor countries to adopt, in a matter of a few years, certain technologies, skills, and business methods that required generations to develop in Western Europe and North America. Foreign direct investment in particular is doubly beneficial: not only does it provide much-needed invested capital (see Principle 6 on page 43), it also facilitates the transfer of advanced skills and technology.

Increases in capital and education contribute directly to the value of physical and human capital and thus directly increase economic output.

MAKING TIME FOR LEISURE

Studies of wellbeing survey data have repeatedly found evidence of the importance of “taking it easy”, as the saying goes. For instance, people who say they frequently spend time socialising tend to be happier. One survey, the World Values Survey, covering more than 90,000 people in 84 countries, found that people who considered leisure to be more important than work were significantly more satisfied with their lives than people who thought the opposite.

The Prosperity Index considers this issue as well, at the national level. Using data from the Gallup World Poll, the Index indicates that countries where people report they have more hours for leisure

each day tend to have higher levels of wellbeing. The Index also tracks average working hours, as reported by national statistical authorities. This shows a more complex relationship with wellbeing; in rich countries, where people can choose between jobs with longer or shorter working hours, shorter workdays are correlated with higher life satisfaction. In poorer countries, however, this relationship is absent or even reversed, presumably because many people are underemployed, and would wish to work more hours if they could.

Looking at the countries in the Index, some clear patterns are evident. Working hours are extremely long in even the

wealthiest Asian countries, suggesting that one avenue for individuals to improve their wellbeing might be more vacation time, given the lower liveability scores in Asian countries. And citizens in each of the bottom 20 countries in the Comparative Liveability Index report very few leisure hours, which further emphasises the importance of leisure to wellbeing. It seems evident that competitive economies offering their citizens a range of opportunities provide a fruitful environment in which workers can balance work and free time.



8. CLIMATE AND THE ENVIRONMENT IMPACT OUR HAPPINESS

FINDING: Several indicators of climate and the environment, including temperature extremes, land area devoted to nature, and air quality, show a significant relationship with average national life satisfaction.



OUR VIEW: As will be immediately evident to anyone who has moved in search of warmer winters or a stretch of coastline, the environment matters to human happiness. As far as temperature is concerned, research suggests that moderate temperatures are best: a winter that is not too cool, and a summer that is not too hot. As mentioned above, countries like Peru, Bolivia and Kenya have the most favourable climates in this regard. The harshest climates in the Prosperity Index are found in extremely cold Mongolia and extremely hot Kuwait.

At first glance, it may appear that these climate statistics are of great interest to individuals, but of little interest to policymakers. However, the results reported in the Prosperity Index suggest that cold climates have a strong negative impact in poor countries but not in rich countries. This makes intuitive sense: in rich countries,

people are more able to afford the well-built homes and heating that can take the sting out of a cold winter. This finding suggests that poor, cold countries will receive a “double benefit” from economic progress: not only will rising incomes directly benefit Mongolians, but the negative wellbeing impact of spending harsh winters on the steppe will be reduced. Scholars have suggested that hot climates can hinder economic development, for instance by increasing the prevalence of tropical disease. The Index identifies a negative impact of extreme heat on wellbeing that persists across the income scale.

The *2008 Prosperity Index Report* also finds a strong impact on life satisfaction of environmental quality indicators including land area devoted to nature and air quality. At the extremes, environmental degradation almost certainly has a severe impact on human wellbeing. The countries in the Index with the worst perceived air quality are Hong Kong, Ukraine, and Russia. Those countries with the smallest land area devoted to nature (on a per-person basis) are Belgium, Singapore, and Taiwan. Those with the greatest dissatisfaction with environmental preservation efforts are Ukraine, Russia, and Macedonia. In these countries, personal choices that prioritise the environment may go a long way towards improving wellbeing.

SECURITY AND PROSPERITY

The 2008 Prosperity Index does not include a specific security component, but implicitly, security plays a major role. This is evident from the overall Index rankings. The top twenty countries and territories in the Index are at domestic peace and are politically stable. Some are involved in conflicts overseas (such as the United States and United Kingdom), and some have difficult regional relations (such as Taiwan or Israel). But all are generally able to provide physical security for their citizens. Moreover, consistent with the Prosperity Index's emphasis on accountable governance, numerous studies have identified the "democratic peace theory" that democratic governments rarely, if ever, go to war with each other.

In contrast, many of the bottom twenty countries in the Index face significant security challenges. Zimbabwe and Kenya have recently been gripped by internal violence, Nigeria by ongoing conflict in the Delta, Pakistan by terrorism and instability, and Sudan by ongoing violence in the Darfur region and elsewhere. Paul Collier of Oxford University identifies the "conflict trap" as one of the most pernicious and persistent barriers to economic growth. Insecurity can destroy stocks of physical and especially human capital, both directly and because the most talented and well-educated workers will tend to flee the country, as well as reduce incentives to invest in these fundamental drivers of economic progress. In conflict and even early post-conflict environments, businesses cannot flourish, investors are not welcome, basic services are not provided, and trade shuts down. Men and women are hindered from work,



students cannot attend schools, and families and communities cannot thrive where the streets are not safe. Insecurity also appears, unsurprisingly, to undermine people's feelings that they are able to make free choices and control their lives: on this indicator, Zimbabwe and Pakistan report two of the lowest scores in the Index.

Because of its severe negative impact on almost every dimension of wealth and wellbeing, insecurity often is the most urgent challenge to address before progress can be made on other drivers of prosperity. Conversely, security is an

indispensable factor in sustaining the virtuous cycle of economic growth, effective governance, social capital, and quality of life. Moreover, prosperous nations that provide security for their own citizens often are able to strengthen the security environment in their region and the world, including through deterrence of potential threats, support for peacekeeping missions, and military partnerships with developing nations. Given the important links between security and prosperity, we hope to explore these issues further in future editions of the Prosperity Index and encourage others to do the same.

9. DEVELOP YOUR GIFT AND THEN GIVE IT AWAY

FINDING: There are significant statistical relationships between life satisfaction, charitable giving, and volunteering.

OUR VIEW: The timeless wisdom that “it is better to give than to receive” is backed up by the latest research. A series of studies have found that volunteering and charitable giving raise the wellbeing of not just the recipients of charity, but also of the givers (see the callout, *Supporting New Research* on page 20). While in wealthy countries additional income produces little measurable gain in life satisfaction, those who choose to give away part of their income tend to report higher levels of personal wellbeing.

The *2008 Prosperity Index Report* finds similar patterns, but at the societal level. Countries in which people report extremely high levels of volunteering (led by the Central African Republic, New Zealand, the United States, and Ireland), and countries in which a high percentage of people are engaged in charitable giving (led by the Netherlands, the United Kingdom and Switzerland), tend, on average, to report higher levels of life satisfaction than might otherwise be expected.

These impacts may come about through the creation of “social capital” (in the *2008 Prosperity Index*, indicators of social capital are grouped under the Community Life heading). Volunteering in particular may promote the growth of community organisations that bring citizens into contact with each other and enhance levels of social trust. Of course, the higher average levels of wellbeing in these countries may come about because the people who give or volunteer are themselves happier.

Volunteering especially may promote the growth of community organisations that bring citizens into contact with each other and enhance levels of social trust.

Either way, the relationship between giving and wellbeing provides another example of the importance of freedom of choice: choices freely made by individuals to donate their time and income, as opposed to coercive policies of wealth redistribution, have empowered individuals to strengthen their communities and enhance liveability in their home nations.

PROSPERITY IN THE MIDDLE EAST

Given the Middle East's dominance of international news and its strategic importance, conditions in the region will continue to attract global attention. The Prosperity Index finds that the region is far from monolithic. Middle Eastern countries cover a range of rankings, from Israel, the UAE and Kuwait within the top 30, to Jordan, Tunisia and Saudi Arabia in the top 50, to Egypt lower down and Yemen at the bottom of the Index.

To be sure, many Middle Eastern countries do have some things in common. No Arabian Gulf or North African country scores well on political life, chiefly because of a lack of political rights and civil liberties. This indicator of democracy

shows an increasingly strong relationship to life satisfaction as countries become wealthier, and is an area needing considerable improvement in the region.

However, most Middle Eastern countries score very highly on satisfaction with health, on family life, and on religious faith. Survey data suggest that, together with highly-religious Latin America, the region is home to a disproportionately large number of the world's faithful. Yet all Middle Eastern countries in the Index, except Israel, score poorly on religious freedom.

Predictably, some of the richer Middle Eastern countries report high levels of charitable giving, but also, on the

economic side, many countries exhibit dependence on commodity exports (notably oil and gas). A dearth of trade agreements is in part an artefact of severe political tensions in the region.

The UAE, one of the highest-ranked Middle Eastern countries, warrants a special mention. One of the emirates, Dubai, has, in particular, moved past dependence on oil exports towards a more diversified economy based on attracting international capital and talent. As a result, the UAE has an extraordinarily high migration and therefore opportunity score, as a global workforce has flocked to the opportunities created by Dubai and its fellow emirates.

Overall Rank	Country	Economic Competitiveness					
		Rank	Invested Capital	Good Governance	Education	Commercialising Innovation	Commodity Exports
19	Israel	8	12	8	11	13	7
28	United Arab Emirates	39	6	6	-2	6	-23
30	Kuwait	35	2	2	18	4	-38
45	Saudi Arabia	62	11	-5	-9	-1	-38
49	Tunisia	52	-4	2	-6	-1	
50	Jordan	42	-6	0	12	-6	4
66	Algeria	65	6	-7	-5	-6	-32
67	Egypt	56	-8	-7	-2	-5	1
73	Iran	87	-3	-13	-6	2	-12
74	Morocco	77	-7	-3	-11	-7	6
79	Lebanon	82	-5	-6	1	-7	
104	Yemen	103	-10	-12	-11	-10	-16

Rank	Comparative Liveability					
	Freedom of Choice	Good Governance	Health	Community Life	Religious Freedom	Religious Belief
21	0	7	7	6	3	2
20	12	1	9	-2	-8	
27	2	-1	12	-9	-17	
30	-10	-9	8	3	-24	12
52	-2	-4	3	-12	-11	
63	-1	-5	8	-12	-17	13
67	-19	-9	4	-8	-14	12
79	-3	-11	5	-11	-17	12
55	-12	-12	3	2	-17	11
66	-3	-6	4	-4	-6	13
70	-4	-8	1	4	-6	
103	-6	-13	-7	-9	-11	



BHUTAN'S GROSS NATIONAL HAPPINESS



The mountainous Kingdom of Bhutan, which famously forbade its citizens access to television until 1999, was the first country on earth to declare the pursuit of Gross National Happiness (GNH) as a policy goal. Other countries, including France, have recently announced plans to develop and prioritise broader wellbeing indicators (see the callout, *A Fascination with Happiness* on page 14). But Bhutan's GNH policy is not part of some trendy attempt to capitalise on new wellbeing research. The GNH policy was announced in 1998, although some scholars claim it was established by the Fourth King of Bhutan when he assumed the throne in 1972.

Perhaps unsurprisingly, the Bhutanese government has seized on the new science of happiness, and initiated research on GNH indicators. But detailed and reliable data on Bhutan is not available, which prevents its inclusion in the 2008 Prosperity Index. If it did, how might Bhutan fare, and how does the Legatum Prosperity Index compare with the Bhutanese concept of GNH, with its roots in Himalayan Buddhism?

Firstly, the CIA World Factbook estimates Bhutanese income per capita at \$5,300, which would likely place the country near the bottom of the Prosperity Index. At low levels of income per person,

the negative impacts of poverty tend to overwhelm other influences on wellbeing. At least, that is the story told by the global statistical averages on which the Prosperity Index is based – perhaps in the unusual case of Bhutan, wise policy could create good health and housing at low levels of income? It is possible, although infant mortality rates of 52 deaths per 1,000 live births (on par with Cambodia and Zimbabwe, if the numbers are accurate) do cast some doubt on this.

Bhutan's operationalisation of GNH is based on four pillars: equitable and sustainable socio-economic development, preservation and promotion of culture, conservation of the environment, and good governance. Most of these ideas do find strong corollaries in the Prosperity Index. Governance and the environment are included in the Index, and show strong links with wellbeing. Health, also in the Index, is part of Bhutan's socio-economic development pillar. Finally, preservation of culture, in the Bhutanese context, includes elements of voluntarism and family life, both of which feature strongly in the Index weightings.

Is GNH missing anything? That is hard to say. But freedom of choice is an obvious candidate, and the Bhutanese state, despite recent democratisation, seems to take a strong interest in regulating personal activity. And in terms of building income and alleviating poverty, Bhutan seems to be moving slowly – according to the CIA World Factbook, three-fifths of Bhutanese government expenditures are funded by Indian development aid.

10. GEOGRAPHY IS NOT DESTINY

FINDING: The top 30 countries in the Prosperity Index include not only countries from Western Europe and North America but also Asia, Eastern Europe, and the Middle East.

OUR VIEW: It has sometimes been claimed that geography shapes the destiny of nations, and that the modern prosperity of many countries is linked to their locations and natural endowments in the distant past. While such arguments may explain much of human history, in the 21st century, these inheritances can be overcome through smart choices.

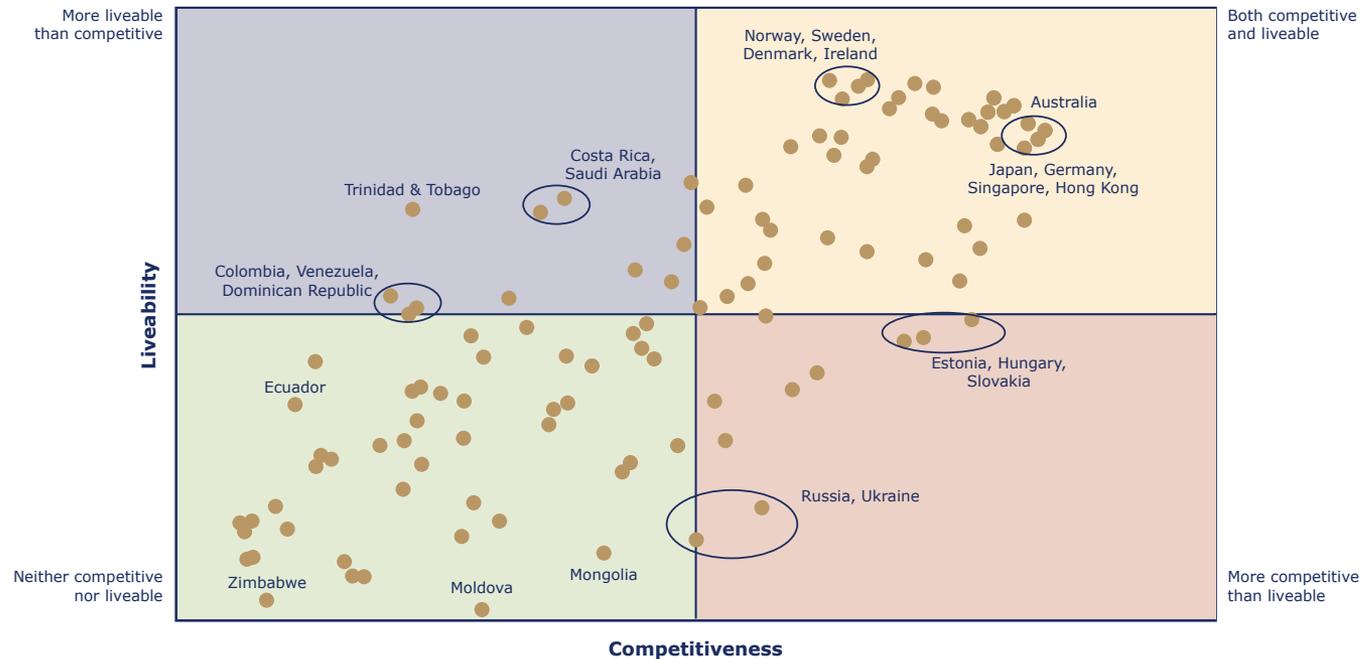
For example, South Korea and North Korea share a similar geography (not to mention cultures and languages) and yet vastly different destinies. Over a 35-year period, Botswana, a landlocked country in Sub-Saharan Africa, was the fastest-growing economy on earth, on a per capita basis, while neighbouring Zimbabwe has recently suffered one of the world's worst economic disasters. Modern technology and medicine can break the curse of the tropics: Singapore, which was once plagued by tropical disease and corruption, now tops our Economic Competitiveness Index, and has a stable and effective government.

With top countries in the Prosperity Index including the aforementioned Singapore (a tropical country), the United Arab Emirates (an Arab country), the Czech Republic (a former communist country), and Malaysia (a majority-Muslim country), it is fair to say that while geography and history can pose ongoing challenges, they are not destiny. This offers hope to countries in regions blighted by poverty and instability, as well as a lesson to those governments that seek to attribute their countries' present misfortunes solely to a poor inheritance.



HAPPINESS – MORE THAN JUST MONEY?

Plot of Competitiveness and Liveability



Many of the factors that produce high levels of life satisfaction in countries are the by-products of economic success: richer countries have more money to spend on medical care, faster-growing economies will tend to suffer lower rates of unemployment, and of course, long-term growth produces higher incomes and reduces poverty.

There are, however, several factors that are not highly correlated with income but nonetheless strongly impact life satisfaction – most notably Religious Life, Climate, Equality of Opportunity, and Family Life. Hence a few countries that do very well on our Economic Competitiveness Index do relatively badly on our Comparative Liveability Index, and vice versa.

There are interesting patterns in the relationship between competitiveness and liveability, as assessed by the Prosperity Index. The top-performing countries (in the upper right quadrant) show some level of balanced pursuit of both wealth and wellbeing. Russia, Mongolia, and several Eastern European countries, by contrast, tend to be comparatively weak on liveability (relative to their levels of competitiveness), with poor scores in social capital, climate, and the environment.

Conversely, many Latin American countries tend to be comparatively strong on liveability, with high scores on religious faith and, usually, health. The outlier, Trinidad & Tobago,

does not earn its position only by virtue of being an island paradise (although its climate scores are not bad). Rather, it has an extreme negative score on one competitiveness indicator, as 40 percent of its economic output is generated by reliance on oil and gas exports.

In the lower left quadrant, some countries have a low rank owing especially to poor liveability scores (e.g., Moldova), others especially to poor competitiveness scores (e.g., Ecuador), while Zimbabwe has an obvious low rank owing to poor scores on both.

11. GOVERNMENTS AND CITIZENS EACH HAVE A ROLE IN BUILDING THE PROSPERITY OF NATIONS

FINDING: The 2008 Prosperity Index includes both factors driven by individual choice and factors driven by the choices of policymakers.



OUR VIEW: In seeking to explain the holistic prosperity of nations, it quickly became apparent that an Index confined to policy indicators, such as political and civil liberties, the unemployment rate, or economic openness, would omit many crucial drivers. It also became apparent that for a number of goals, the choices of citizens might be just as, and perhaps more, effective than government policy in producing favourable outcomes. Is the health problem of obesity best tackled through healthcare policy or citizens choosing to eat better? Is air pollution best tackled by new regulations or public pressure on polluting companies? Is better education best pursued and paid for by parents or government-funded schools?

The statistical analysis in the 2008 Prosperity Index avoids judgement on these issues. It simply reports the statistical links between health, pollution, education, and prosperity. Where possible, the Index includes policy indicators as well as indicators of results. The best solutions for tackling each of these issues – especially as regards life satisfaction, a relatively new area of concern - will be tested in years to come.

The 2008 Prosperity Index results clearly indicate that both individuals and governments have a role to play.

What the 2008 Prosperity Index results do clearly indicate is that both individuals and governments have a role to play. No poorly governed country has achieved high levels of holistic prosperity (see Principle 2 on page 35) since such countries have failed to create the conditions necessary not only for economic progress but also for personal flourishing. And in the countries topping the Index, individual choices on issues such as marriage, charitable giving, and leisure time, have clearly played a major role.



THE INVESTIGATION CONTINUES

Our understanding of the determinants of both material wealth and life satisfaction has increased by leaps and bounds but much remains unknown.



THE INVESTIGATION CONTINUES



While our understanding of the determinants of both material wealth and life satisfaction has increased by leaps and bounds, much remains unknown. And no wonder, since inquiries into the sources of prosperity trace back to the most fundamental questions about the nature of wealth and happiness. We intend to continue the research that produced the 2008 Legatum Prosperity Index, contributing to an evolving understanding of the drivers and restrainers of prosperity.

The analysis in the Index, especially the rankings of countries, should not be read as a precise measurement of countries' relative success or failure, but rather as an effort to offer insights into the elements which contribute to creating fulfilled lives and prosperous societies. Although the analytical techniques that produced the Index are rooted in statistical research on historical and current data, any analysis stretching across so many countries and years and containing so many interrelated factors is not undertaken for the purposes of measurement precision so much as to elucidate trends and principles.

We hope that the 2008 Prosperity Index provides some useful insight as to where, in principle, we can choose to do better in enhancing the material wealth and life satisfaction which define our prosperity, and that this commentary offers a thought-provoking interpretation of the Index results.

Researchers, policymakers, and the generally curious are welcome to examine the results for their countries and others on our website, www.prosperity.com. At this address, a full set of data and interactive analysis tools are available for all 104 countries in the Index.

The raw research results reported in the full report are intended as a stimulus to research and as a diagnostic tool, to identify areas where focused effort may reap significant rewards, and to encourage debate on crucial social issues. However, knowing that a country has a relatively low level of invested capital is not the same as knowing the cause of the deficiency or how to remedy this deficiency, and the solutions will vary from country to country depending on context. We expect that there will be substantial debate on these issues.

It is important to note that while the Index results may suggest that increasing one factor should, on average across countries, produce a jump in life satisfaction, the exact effect in each country will depend on its cultural, legal, political, religious, historical, and economic context.

Notably, no country currently scores well in every category. While rich countries enjoy higher levels of economic prosperity, many also face increased levels of social poverty characterised by the loosening of community bonds, familial ties and overall social trust. Likewise, poorer countries face the challenge of improving clear economic deficiencies while maintaining the social capital that so many of them enjoy.

We hope that our analysis of the historical data, the basic prosperity principles identified in this commentary, and the detailed results in the full report will prove useful to those who are concerned about their own prosperity, that of their country, and of other countries around the world. Our hope is to stimulate further debate not only on the causes of economic growth but also on the overall factors that make life worthwhile. In so doing we hope to enrich each other's lives towards a more prosperous world.



GLOSSARY OF KEY TERMS

Better Education

The average number of years of secondary education completed per worker, where “workers” are defined as the population between 16 and 65 years of age. More education corresponds to faster long-term economic growth.

Commercialising Innovation

(1) Researchers employed in research and development per million population; (2) patent applications filed as recorded by the World Intellectual Property Organisation; and (3) exports of innovative high-technology goods as a percentage of GDP. More researchers, patents and high-technology exports correspond to faster economic growth.

Community Life

(1) Survey on whether people have given money to a charity in the past month, from the Gallup World Poll; (2) survey on whether people have volunteered their time to an organisation or worthy cause in the past month, also from the Gallup World Poll; (3) survey on whether people are members of community organisations such as sports clubs, social clubs, and church groups, from the World Values Survey; and (4) survey on whether people believe that most other people can be trusted, also from the World Values Survey. These indicators measure different aspects of the strength of community, social, political and religious organisations – so-called “social capital”. More social capital corresponds to higher levels of life satisfaction.

Comparative Liveability

The Comparative Liveability Index of the Prosperity Index rates how liveable countries are; that is to say, how well countries are doing at fostering the practices, habits, policies, and institutions that lead to high levels of life satisfaction. It does not measure a country’s current level of average life satisfaction. Rather, this Index assesses countries’ relative performance on the factors that appear to increase or decrease average levels of life satisfaction.

Competitive Markets

(1) The ratio of movements in prices that consumers pay for goods and services compared to prices that producers pay for goods and services; and (2) the ratio of movements in prices for domestically-traded goods and services to prices for internationally-traded goods and services. If these price indices tend to move together, it suggests that markets are competitive. More competition in markets corresponds to faster economic growth.

Dependence on Commodity Exports

Exports of natural resources and other primary commodities as a percentage of GDP. Greater dependence on primary commodity exports corresponds to slower economic growth.

Dependence on Foreign Aid

Foreign aid as a percentage of GDP. Greater dependence on foreign aid corresponds to slower economic growth.

Economic Competitiveness

The Economic Competitiveness Index of the Prosperity Index rates how competitive national economies are; that is to say, how well countries are doing at fostering the practices, habits, policies, and institutions that lead to increases in material wealth. It does not measure a country’s current level of wealth; rather, this Index assesses countries’ relative performance on the factors that drive or restrain sustained increases in wealth over the long term.

Economic Openness

(1) The average of foreign direct investment and foreign trade as a proportion of GDP; (2) an assessment of policies promoting trade freedom as measured by the Heritage Foundation’s Trade Freedom Index; and (3) the number of regional trade agreements (RTAs) to which a country is a party, as notified to the World Trade Organisation. More foreign trade and investment, greater trade freedom, and more memberships of regional trade agreements correspond to faster growth.

Entrepreneurship

(1) The cost of starting a business as a percentage of Gross National Income (GNI) per capita, as measured by the World Bank Doing Business Indicators; and (2) business owners (that is, entrepreneurs) as a percentage of the labour force. Lower costs of starting a business and a higher business ownership rate correspond to faster growth.

Equality of Opportunity

(1) Survey on the perception that anyone who works hard can get ahead, from the Gallup World Poll; (2) percentage of parliamentary seats held by women, adjusted to remove the impact of quotas; (3) the ratio of the female to male share of national income; and (4) the net migration rate. Each indicator reflects an aspect of how opportunities are distributed in society. Migration rates, for instance, reflect the degree to which people leave a country, fleeing poor conditions or in search of opportunities elsewhere. More widely distributed opportunities correspond to higher levels of life satisfaction.

Family Life

(1) Share of the population that is divorced, measured by the Gallup World Poll; (2) share of the population that is widowed, measured by the Gallup World Poll; (3) survey on whether people have relatives or friends they can count on in times of trouble, from the Gallup World Poll. Strong and unbroken family ties correspond to higher levels of life satisfaction.

Freedom of Choice

Survey on the satisfaction people feel with their freedom to choose what to do with their lives, from the Gallup World Poll. Greater average satisfaction with personal freedom of choice corresponds to higher levels of life satisfaction.

Gallup World Poll

A survey collecting data on beliefs, opinions, and behaviours of citizens in more than 140 countries. The results are gathered using interviews with at least 1,000 people in each country, selected to be representative of the country's population as a whole.

Good Health

(1) Average life expectancy adjusted for the presence of debilitating disease; and (2) survey on satisfaction with personal health, from the Gallup World Poll. Better health corresponds to higher levels of life satisfaction.

Good Governance (as it Pertains to Economic Competitiveness)

(1) The effectiveness of a government, including the quality of public services, the capacity of the civil service and its independence from political pressures, and the quality of policy formulation, as assessed by the World Bank Governance Indicators; and (2) the quality of regulation, meaning the ability of a government to provide sound policies and regulations that enable and promote private sector development, also as assessed by the World Bank Governance Indicators. Better governance corresponds to faster economic growth.

Good Governance (as it Pertains to Comparative Liveability)

(1) The effectiveness of a government, including the quality of public services, the capacity of the civil service and its independence from political pressures, and the quality of policy formulation, as assessed by the World Bank Governance Indicators; (2) control of corruption, reflecting the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as "capture" of the state by elites and private interests, as assessed by the World Bank Governance Indicators; and (3) voice and accountability, reflecting the degree to which citizens enjoy political rights and civil liberties, also as assessed by the World Bank Governance Indicators. Better governance corresponds to higher levels of life satisfaction.

High Incomes

Average income per person measured at purchasing power parity. Greater income per person corresponds to higher levels of life satisfaction.

Invested Capital

The value of fixed capital (e.g. factories, machine tools) per worker, where "workers" are defined as the population between 25 and 65 years of age. More invested capital corresponds to faster growth.

Life Satisfaction

The degree to which people report they are satisfied with the lives they lead, as measured in surveys such as the World Values Survey and Gallup World Poll.

Low Unemployment

The unemployment rate. Low unemployment rates correspond to higher levels of life satisfaction.

Material Wealth

Average annual income per person, approximated using output per capita (GDP) at purchasing power parity. These data are regularly compiled by the International Monetary Fund.

Moderate Climate

(1) Maximum average monthly temperature in a country, with regional variations weighted by each region's

population; and (2) minimum average monthly temperature in a country, with regional variations weighted by each region's population. Moderate temperatures (not too hot, and not too cold) correspond to higher levels of life satisfaction.

Pleasant Environment

(1) Land area devoted to nature, measured by the Ecosystem Services Product per capita, an assessment of the value of nature such as lakes, rivers, wetlands, forests and grasslands; (2) survey on people's satisfaction with air quality, from the Gallup World Poll, and (3) survey on people's satisfaction with the government's efforts to protect the environment, also from the Gallup World Poll. A more pleasant natural environment corresponds to higher levels of life satisfaction.

Prosperity

Recent research advances have made it possible to compare not only the material wealth but also the life satisfaction of people in countries worldwide. Accordingly, we have defined national prosperity as the holistic combination of both of these factors.

Religious Life

(1) Survey on the "importance of God in one's life", from the World Values Survey; and (2) an index of government regulation of religion, measuring the degree to which government policy permits the exercise of religious freedom. Higher average levels of religious belief and greater religious freedom correspond to higher levels of life satisfaction.

Time for Leisure

(1) Average working hours per week in non-agricultural jobs; and (2) survey on average hours of free time when "you can do what you want to do" (during the previous day), from the Gallup World Poll. More hours of leisure correspond to higher levels of life satisfaction.

World Values Survey

A periodic survey consisting of more than 200 questions regarding cultural issues, including life satisfaction and religious faith, conducted in more than 50 countries worldwide. The results are gathered using interviews with at least 1,000 people in each country, selected to be representative of the country's population as a whole.



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