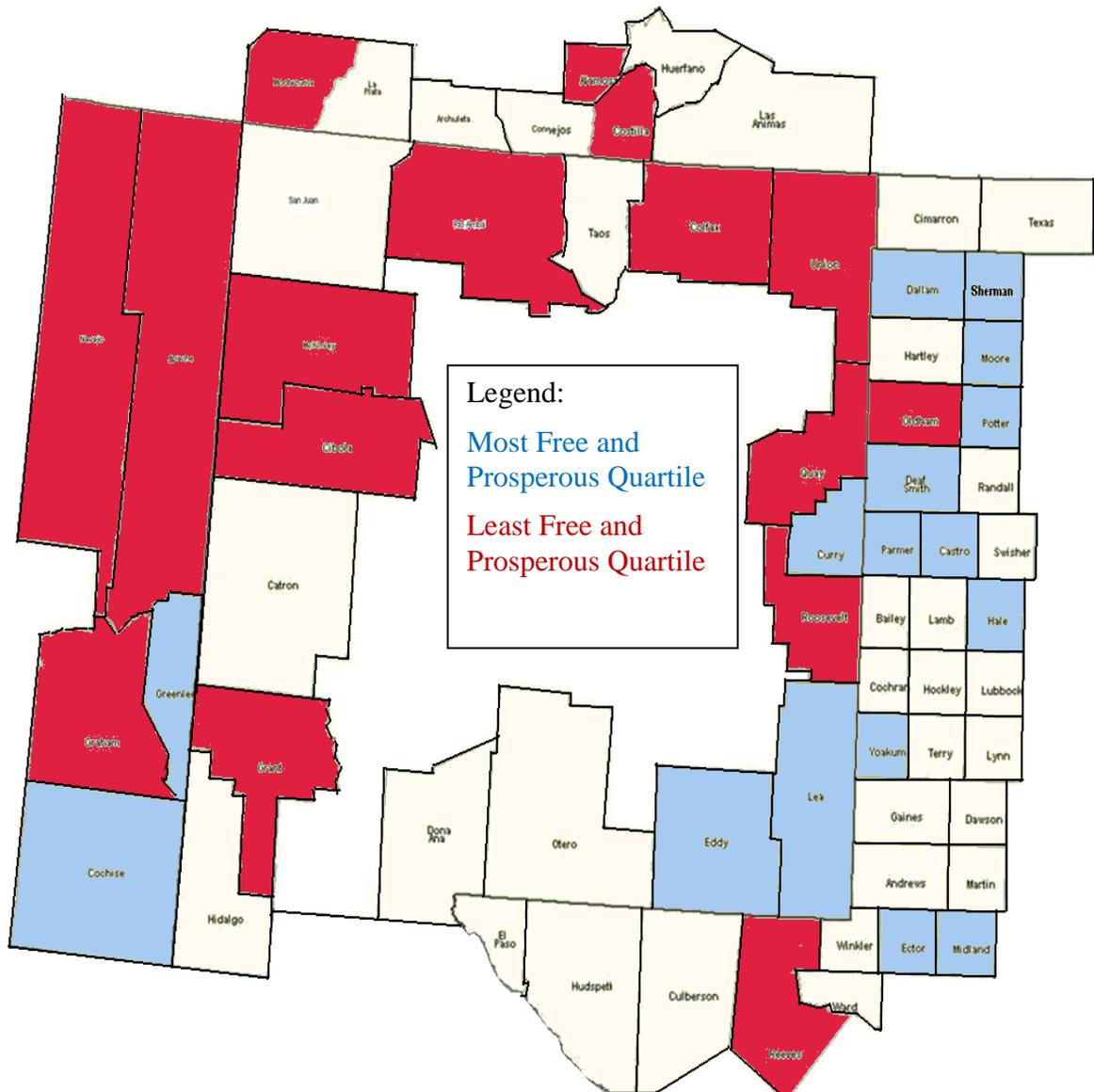


# Liberty, Opportunity, Prosperity along New Mexico's Border

Summary by Harry Messenheimer, Ph.D., April 2013



Neighboring Counties along New Mexico's Border

## Summary

A large body of scholarship over the past few decades has given us compelling evidence that prosperity emerges in the presence of economic freedom. Whether it is among countries throughout the world or among states and provinces throughout North America, the greater is economic freedom the greater is prosperity. That evidence, coupled with well-known prosperity-reducing incentives within government, strongly suggests that we should also find compelling evidence at more decentralized levels. If greater economic freedom begets greater prosperity internationally and at state and provincial levels, then shouldn't it do so at the county level, too?

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The purpose of this study is to examine that question empirically. We do so by examining 66 neighboring pairs of counties on each side of New Mexico's border. New Mexico borders Texas, Oklahoma, Colorado and Arizona; and confining the data set to neighboring border communities with similar culture, climate, geography and natural resources is a distinct advantage of this approach. Statistical errors associated with such characteristics should be reduced relative to prior studies.

What is prosperity and why does government tend to overreach? Prosperity emerges from *voluntary exchange* among countless individuals in their roles as buyers and sellers. Voluntary exchange makes both parties to each exchange better off, creating value and thereby prosperity in the process (otherwise those exchanges would not take place). Unfortunately governments at all levels tend to grow too coercive, impeding voluntary exchange and undermining the discipline of competition. Reducing that excessive coercion (increasing economic freedom) would increase voluntary exchange and prosperity.

The explanation for excessive coercion has become standard doctrine in economics. It's not that the politicians and bureaucrats from whom collective decisions emerge are not generally well-intentioned. It's that they tend to be overly influenced by the differential power of well-organized interest groups. Their *incentives* are misplaced when contrasted with the incentives of buyers and sellers engaging in *voluntary exchange* in the marketplace.

As a result special privileges are legislated directly by providing interest groups a monopoly privilege, special tax advantage or direct subsidy. Licensing, health care mandates, minimum wage laws, construction permitting and inspections and "certificates of public convenience or necessity" are prime examples. Or they are provided indirectly by special privilege to government's resource providers, making provision of core functions more costly than they otherwise would be. The *coerced* costs of each of these privileges are widely spread among the citizens. Because the costs of each special privilege are widely spread, the cost to each citizen is so small as to be invisible; and the individual citizen has no incentive to become informed or do anything about the problem.

What affect do the special-privilege impediments to voluntary exchange have on prosperity? The primary goal of this study is to statistically test our expectation that fewer impediments to voluntary exchange lead to greater prosperity. We do so by estimating how *differences in prosperity* in neighboring counties on each side of New Mexico's border are affected by *differences in their impediments to economic freedom*.

Since prosperity may also be affected by differences in federal presence in each locale, the test also includes the difference in federal presence between paired counties. We often hear assertions from "economic development" specialists about how an increased federal presence will benefit the local economy by a multiple of the increase (the so-called multiplier effect). In essence, though, they are really stating the trivially obvious proposition that increased number of local federal workers and spending will increase the demand for goods and services in their locale. But how does the influx of workers, federal spending and/or subsidies affect the prospects for individuals to prosper in any particular locale? Does it improve or worsen conditions that allow each individual the opportunity to flourish?

This is a particularly interesting question. Historically, New Mexico's federal legislators have been particularly adept at "bringing home the bacon." Nonetheless the state is still relatively poor, and that should make one skeptical of equating multipliers with prosperity. We test the effect of federal presence by estimating how *differences in prosperity* in neighboring counties are affected by *differences in their federal presence*.

How do we measure prosperity? We cannot measure it directly. But the voluntary nature of the exchange process suggests a measurement that should be highly correlated with prosperity, namely the earnings of those involved in private transactions.

Also, we cannot measure economic freedom directly; but we have reasonable metrics for impediments to economic freedom, namely the relative size of each county's state/local government. The size of state/local government should be proportional to those impediments at the margin. Why is this so? Impeding voluntary exchange requires resources, as does subsidizing involuntary exchange. Governments that are more susceptible to privilege seeking should therefore be relatively larger than those that are less susceptible.

Similarly, we should be able to detect the effect of federal presence on prosperity, if any, by comparing its relative size between counties.

Using data available from the Bureau of Economic Analysis for 66 pairs of counties along New Mexico's border, we tested the hypothesis that economic freedom promotes prosperity. Two sets of empirical tests were conducted, one each for calendar years 2001 and 2010. Each of those tests supported the proposition that economic freedom advances prosperity. Moreover, each test found that those counties having a larger federal presence suffered from reduced prosperity.

Statistically speaking, the results for each test are significant at any of the usual predetermined levels of significance (0.05, 0.025, and 0.01). Simply put, it is highly unlikely the results could have been obtained by chance alone. Moreover, the estimated effects are consistent with observed increases in prosperity from 2001 to 2010, lending even more support to the proposition that economic freedom matters at the county level.

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How much does it matter? We can estimate “what might have been” for a poor county. The typically poorer county (Rio Arriba, NM; Grant, NM; Roosevelt, NM; Quay, NM; Costilla, CO; Apache, AZ) with low economic freedom on average devotes a profligate 35 percent of its resources to state/local government, while the typical county with high economic freedom (Curry, NM; Lea, NM; Midland, TX; Dallam, TX; Greenlee, AZ) devotes a much more parsimonious 10 percent of its resources. Using earnings per private worker in 2010 as our indicator of prosperity, we estimate that, had it emulated the freer county, the poorer county would have been 75 percent more prosperous (earnings per private worker estimated to average \$52.5 thousand rather than observed \$30 thousand per year).

Similarly, we can estimate how much federal presence matters for prosperity. Take a county like Curry County in New Mexico, for example. 40 percent of its resources are devoted to federal presence in the county, mostly due to Cannon Air Force Base (which has managed to avoid being closed several times in recent years). Say that Curry County had had a more modest federal presence of five percent without Cannon. In that case Curry County’s estimated prosperity would have been 40 percent higher (earnings per private worker estimated to be \$61.5 thousand rather than the observed \$44 thousand per year).

We don’t want to overstate the precision of our estimates. They are estimates only, and the study discusses some possible sources of error in the estimates. Nonetheless, the study provides compelling evidence of the direction and approximate magnitude of state/local government’s affect on prosperity. Assuming that laying the ground work for maximum prosperity should be the aim of government, policy makers should give emphasis to making their counties more resistant to privilege-seeking.

The full study may be found online at [http://www.riograndefoundation.org/downloads/rgf\\_border\\_project.pdf](http://www.riograndefoundation.org/downloads/rgf_border_project.pdf).