

CHAPTER I: INTRODUCTION

“Nobody is at liberty to attack several property and to say at the same time that he values civilization. The history of the two cannot be disentangled.” — *Sir Henry Maine*

Economic development is both fairly simple and impossibly difficult. We know it's fairly simple because 235 years ago Adam Smith was able to boil it down to three words: division of labor. While visiting a pin factory Smith observed that instead of making each pin from start to finish the workers would instead specialize in one or a few steps of the process and then pass their product on to another laborer. This focus allowed the employees to hone their skills and increase their productivity, albeit in only a few steps of pin making. But Smith found when the slightly more productive employees work together the result is a fantastic increase in output. The same basic principle is in play for people who specialize in one industry and trade their surplus output with people who specialize in other industries. More output means more consumption which is essentially economic development. Simple as that.

And yet something is missing. The wealthy industrialized countries are certainly characterized by specialization and division of labor. But large portions of the world's population still engage in economic activity best described as self-sufficient. In fact, wealthy industrialized countries are a relatively new phenomenon. For most of human history life could be best described as poor, nasty, brutish, and short. So while the mechanism for achieving economic development is fairly simple, the process of getting that mechanism going in the first place appears to be quite difficult. Otherwise all these poor and stagnant societies would (presumably) just specialize and trade and become wealthy. What do the wealthy industrialized countries have that other societies lack?

The answer is a system of secure property rights. Property rights internalize costs and benefits and provide the proper incentives for good stewardship of resources. A farmer will treat a parcel of land or a tractor or a hat differently if she is the one reaping the benefits. A baker is more likely to bake breads and pastries for sale if he knows that someone else will not confiscate the profits of his activity. Property rights give the baker the incentive to bake.

Property rights also play a vital role in directing resources to those uses most valued by society. This was first pointed out by the economist Ludwig von Mises in the academic debates about the efficiency of socialism in the 1920s. When privately owned goods are sold they are transferred between owners at some price. These market prices contain in them important information about the resources' relative scarcity. As a good becomes more scarce either through a decrease in supply or an increase in demand, its price will rise indicating to society that it is more valuable and should only be used for higher valued purposes. Mises pointed out that without private property there are no exchange markets, and with no markets there are no prices. This makes it impossible to allocate resources efficiently. Should cars be built with steel or some alloy? Should a restaurant use plastic silverware and plates or more durable ones? Without prices to act as a guide people can only guess at the answers to questions like these. The result is resources being used less efficiently than would otherwise be the case and society is poorer as a result.

The International Property Rights Index helps illustrate the vital role property rights play in generating material well being. By ranking countries' respect for property rights we are able to make comparisons and see the consequences of having a weak or strong property rights regime. As with any study, there are limitations to our approach. Data limitations prevent us from ranking every country for example. But we remain confident that this study clearly demonstrates the positive relationship between property rights and economic development.