



**The Texas-Mexico Economy  
and its Uncertain Future**

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The William J. O’Neil Center for Global Markets and Freedom was founded in 2008 with an initial grant from William J. O’Neil, a 1955 SMU business school graduate, and his wife Fay C. O’Neil. Its broad mission is the study of why some economies prosper and others do poorly. The center’s programs promote understanding of how capitalism works among the general public, policy makers, business managers and the next generation of business leaders. To these ends, the O’Neil Center teaches SMU Cox students, conducts economic research, publishes economic reports, sponsors conferences and educates the public through the media and speeches.

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*Myers moderating a Texas/Mexico Center program at SMU*

## A Message from the Dean

My first year as SMU Cox dean took me far beyond the SMU campus, the DFW area and even the state of Texas. The school's students, alumni and supporters are spread around the world, and I've gotten to know some of them in South America, Asia, Europe and cities all across the United States.

I traveled to Mexico more than any other place—a total of three times. In April, I was in Mexico City as a moderator for a symposium hosted by SMU's 2-year-old Mission Foods Texas-Mexico Center, one of the business school's on-campus partners. I serve on the center's board, and we met a group of business leaders and presented new research relevant to the shared economy of Texas and Mexico.

A few months later, I went to El

Paso with the Texas-Mexico Center for a summit on the critical importance of cross-border economic integration.

The growing economic connection between Texas and Mexico is the topic of this year's O'Neil Center Annual Report essay. "Texico: The Texas-Mexico Economy, and its Uncertain Future," written by O'Neil Center founding director W. Michael Cox and co-author Richard Alm, discusses why integration took so long to really get started, how it's paid off over the past two decades and what has prevented Texico from reaching its full potential.

For years now, Cox and Alm have teamed up to spearhead the O'Neil Center's research project on the Texas economy, so they already know full well how much Mexican trade and migration contribute to

the state's prosperity. They spent the past six months on a deep dive into the Mexican economy—looking not only at statistics and recent events but also at the history of Mexico's economic policies.

In the essay, Cox and Alm acknowledge concerns about Texico's future. In so many parts of the world, North America included, a resurgent economic nationalism challenges the consensus on the advantages of opening borders for business. Companies in Texas and Mexico, the prime movers in seizing the Texico opportunity, can long longer count on their nations' commitment to the policies that make Texico possible—thus the title's uncertain future for this dynamic and diverse cross-border economy.

Matthew B. Myers  
Dean, Cox School of Business



## The Texas-Mexico Economy and its Uncertain Future

By W. Michael Cox and Richard Alm

The Rio Grande takes a sharp eastward turn in the barren Chihuahuan desert west of El Paso, then meanders more than 1,254 miles before emptying into the Gulf of Mexico just east of Brownsville. The river forms the border between Texas and Mexico, neighbors with a long and complicated history.

For most of this shared history, the river acted as an economic boundary as well as a physical one. About three decades ago, that began to change. Many of the impediments to cross-border business were swept away over the span of just 10 years, giving Texas and Mexico companies more freedom to do business.

As the Rio Grande receded as an economic barrier, trade and investment surged to record levels, helping create the sprawling and diverse economic space we denote by

the portmanteau word Texico. The name captures today's reality—that the Texas and Mexico economies are now by most measures highly integrated and becoming more in sync with each passing year.

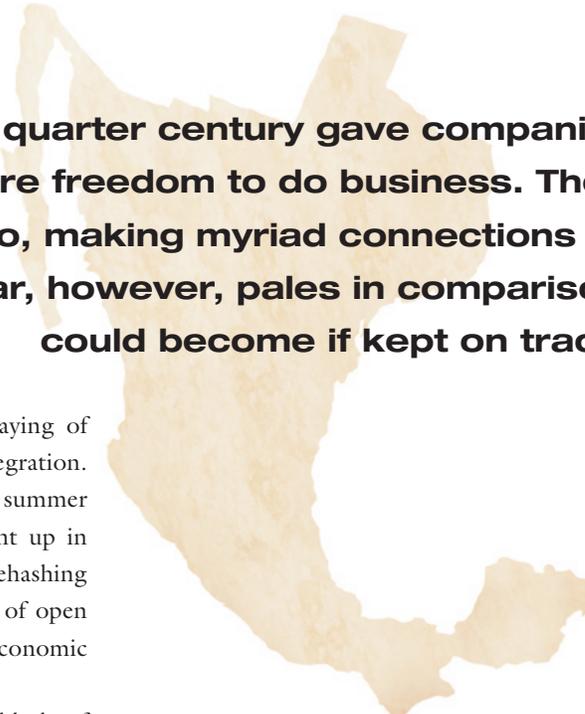
Envisioning Texico as its own economic space highlights key issues in the process of cross-border integration—the interplay of economics and policy in shaping its pace and depth and the trap-laden path to fully realizing its promise. The journey of these two neighbors also shows the potential and perils of integrating a rich economy and a poorer one.

Economics tends to look favorably on breaking down barriers that impede the exchange of goods, services, money and ideas. The widely touted benefits of opening up economies include gains from specialization and trade, a more efficient

allocation of scarce resources, greater global competitiveness, higher consumer welfare and transfers of knowledge and technology relevant to business.

Integration delivers its progress by unleashing powerful and disruptive market forces that toss producers, workers, suppliers and customers into a crucible of international competition. Most successfully adapt and prosper; some find the new environment too much, leaving them worse off.

As winners and losers shake out, the existing economic order takes a beating—so it's not surprising that Texico has critics as well as champions. The naysayers made little headway while a succession of governments in both the United States and Mexico supported policies to keep their economies open.



**“The past quarter century gave companies in Texas and Mexico more freedom to do business. They’ve responded with gusto, making myriad connections ... What’s been gained so far, however, pales in comparison to what Texico could become if kept on track.”**

The past decade has seen a fraying of the consensus favoring greater integration. As we write this essay in the late summer of 2018, Texico’s future is caught up in the greater drama of a world rehashing the old battle between adherents of open economies on one side and economic nationalism on the other.

Voters fed up with all the hubbub of economic change are casting ballots for new leaders who campaign on turning back the clock and restoring old ideas that favor protection over production, isolation over integration. With the ground shifting, Texas and Mexico find their economic partnership at risk.

The challenge to the integration orthodoxy comes at a critical time. The past quarter century gave companies in Texas and Mexico more freedom to do business. They’ve responded with gusto, making myriad connections, most good for their companies and good for their customers. What’s been gained so far, however, pales in comparison to what Texico could become if kept on track. Untapped opportunities abound.

Just over two decades in, Texico remains very much a work in progress—its future brighter than its past. Both sides of the Rio Grande would suffer if the revival of economic nationalism smothered the full realization of the economic partnership between Texas and Mexico.

### **The Right Time—at Last**

Economic integration is an organic process, driven by the private sector. It

unfolds through countless individual decisions on what to buy, sell and produce, where to invest, how to exploit available technology and use labor and other resources and when business risk-taking is manageable.

The process benefits from geographical proximity, transport and information infrastructure and other ties that facilitate connections across borders. Geography and technology impose some constraints on how deeply economies come together, but most impediments to integration are imposed by governments, usually for the benefit of entrenched domestic interests.

True integration requires economic freedom and market forces. Governments can try to forge cross-border economic ties, but integration led by the state instead of the private sector ends as colonialism.

Economies don’t start integrating in earnest unless the economics and policy are both right. On the economic side, each partner must offer something the other values—labor, capital, raw materials, technology, potential customers, or any of these in combination. On the policy side, economies must be open enough to allow the private sector to capitalize on available

business opportunities.

It took a long time for Texas and Mexico to get it right. When Texas was part of Mexico’s northernmost state in the early 1800s, economic collaboration between Texico’s north and south was minimal because 900 miles of rough terrain and bad roads separated San Antonio and other Texas settlements from the heavily populated and relatively rich region of central Mexico.

Integration only became less likely after Texas declared its independence in 1836 and joined the United States in 1845. The acrimony of war lingered south of the border, and Texas’ drive to integrate focused in other directions, shipping cotton, beef and eventually oil to the rapidly industrializing U.S. and European economies.

Throughout the 1800s and well into the 1930s, tariff walls protected the U.S. market—although Texas and the rest of the South, as exporters of farm products and importers of manufactured goods, generally opposed them. U.S. protectionism hardly mattered to Mexico, a largely agricultural economy with undeveloped ports or railroads that couldn’t supply much beyond metals to the emerging American juggernaut.

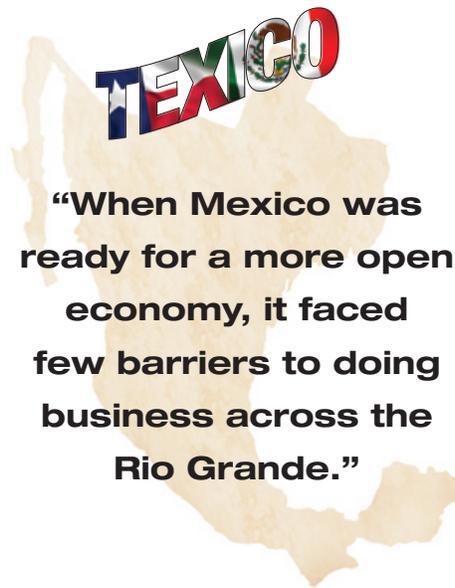
In the closing decades of the 1800s, Mexico sought to industrialize under President Jose Porfirio Diaz, a polarizing figure who served seven terms in the decades after 1876. He welcomed foreign investment, with some success in mining, railroads and manufacturing. Even with the advantage of proximity, Texans didn’t lead the charge. Mexico needed capital, and the places to find it were the financial centers of the

Northeast and Europe, not commodity-producing Texas.

After revolution deposed Diaz in 1911, Mexico entered a long period of economic nationalism. The country adopted an import-substitution strategy that curtailed imports to nurture home-grown industries. In 1938, President Lazaro Cardenas struck economic nationalism's most decisive blow by seizing foreign-owned oil operations.

While Mexico hunkered down behind its import substitution orthodoxy, the United States jettisoned its protective tariffs in the wake of the Depression and World War II. The country led a 60-year global march toward freer trade, taking Texas along with it. When Mexico was ready for a more open economy, it faced few barriers to doing business across the Rio Grande.

In Mexico, import substitution spurred industry and growth, particularly during the Mexican Miracle in the decades after World



War II. GDP per capita more than doubled from less than \$4,000 a year in 1950 to more than \$10,000 in the early 1970s.

The miracle didn't last. A closed economy isolated from foreign competition left Mexico with bloated government,

crushing public debt, capital flight, triple-digit inflation, a corrupt cronyism riddled with monopoly and a withered private sector. For a while, the petrodollars of the 1970s oil boom kept Mexico afloat, but the good times came crashing down when oil prices plunged in the early 1980s.

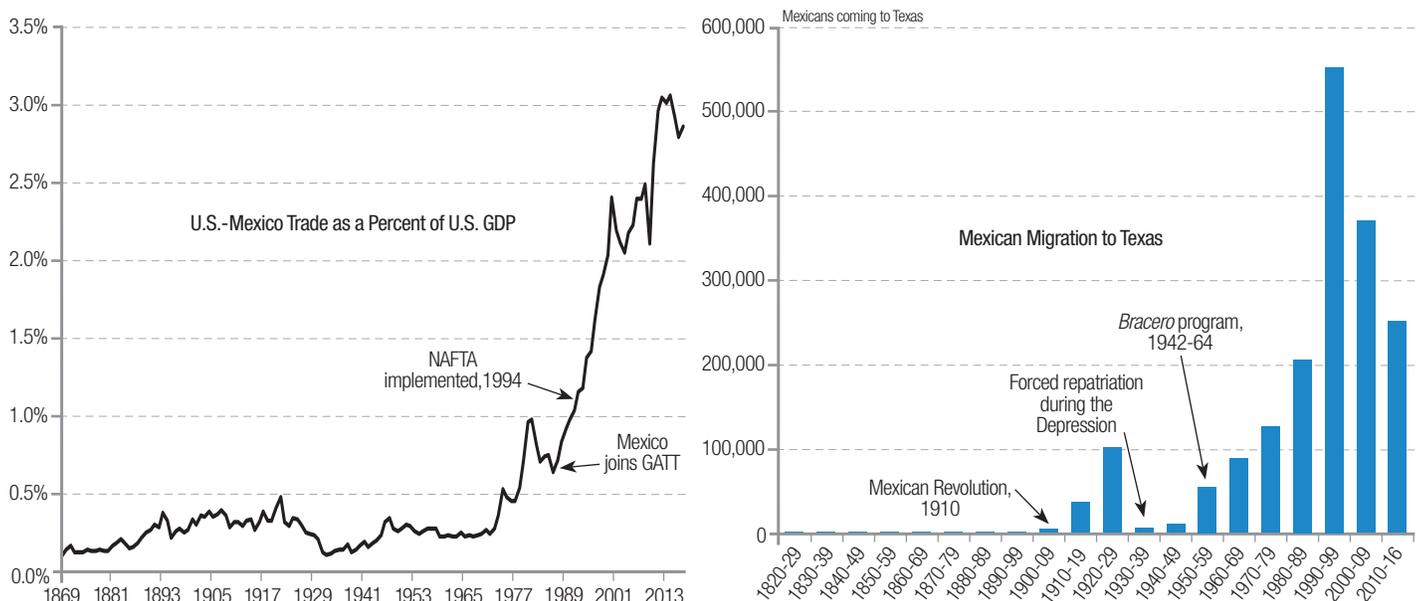
The decade's falling oil prices roiled Texas' economy, too. The state had what it took to bounce back from deep recession—an entrepreneurial business culture with the freedom to find new paths to success. What emerged in the 1990s was a big, highly diversified and outward-looking Texas economy, with oil no longer so dominant.

To the south, President Miguel de la Madrid, facing a severe economic crisis when taking office in 1982, made the momentous decision to abandon the inward-looking dogma in favor of a stunning opening to the rest of the world. He swept away

**EXHIBIT  
1**

## Slow to Gain Traction

Bilateral trade—the sum of merchandise exports and imports—was below 0.5 percent of U.S. gross domestic product until 1974 and below 1 percent until 1991. It exceeded 3 percent from 2013-15 (*left panel*). Even with a surge after Mexico's revolution and the influx of *Bracero* farm workers, migration to Texas remained below 200,000 in every decade until 1980. In an era of tighter immigration enforcement, it surged in the 1990s and then receded (*right panel*).



the country's barriers to foreign trade and investment and joined the General Agreement on Tariffs and Trade (GATT), the multinational pact that certifies the rules for cross-border commerce. (Since then, GATT morphed into the World Trade Organization.)

Mexico jettisoned fixed exchange rates. To thwart politically driven monetary policy, it enshrined the independence of *Banco de Mexico*, its central bank, in the constitution. State-owned enterprises were sold to the

private sector. Carlos Salinas de Gortari, the next president, negotiated the North American Free Trade Agreement (NAFTA) with the United States and Canada to cement the open-market reforms. With Texas' economy already open, conditions were right for Texico—at last.

Texas and Mexico lived as neighbors for decades—so why did it take so long for cross-border business to start booming? Throughout the 1800s and most of the 1900s, neither economics nor policy were

right, owing mostly to U.S. protectionism and Texas' commodity-based economy. In the second half of the 20<sup>th</sup> Century, U.S. policy improved, but Texas didn't rapidly diversify until after the 1980s oil bust. The same disruption sent Mexico's policy veering in a radically new direction. It's not too much to say that the genesis of Texico was the wreckage of the 1980s.

A quick look at trade and immigration will confirm the timing of Texico's origin. Data on state-level trade go back only a

## Box 1 Texas and Mexico, By the Numbers

### Bordering on a Great Divide

Texas was once part of Mexico's northernmost province, relatively poor and isolated, separated by an arduous journey from the population centers and wealth far to the south. After going their separate ways in 1836, the economies of the state and its former country took different paths.

Texas eventually cast its lot with the United States, becoming part of a rich and dynamic economy. For Mexico, economic progress took place in fits and starts, and the World Bank ranks the country among the second tier of upper middle-income countries.

Mexico is more than three times larger than Texas, with

nearly five times the population (*see table below*). More people are working with longer hours, producing a bigger GDP.

Yet, on most measures of economic well-being, Texico's north is much better off than its south. Texas surpasses Mexico by being far better educated, working fewer hours to produce a higher per capita GDP and average wage. Texas has moved farther along in the development path, with fewer workers in farming and manufacturing and more in services. Texans have 10 times the average net wealth of Mexicans, and Texas households are more likely to own many everyday consumer products—from cars to smartphones.

	Mexico	Texas		Mexico	Texas
Landmass (square miles)	758,400	268,597	Workers in agriculture (2016)	12.9%	2.0%
Miles of coastline	5,797	367	Workers in industry (2016)	25.7%	15.3%
Population (2017)	129,163,276	28,304,596	Workers in services (2016)	61.4%	82.7%
Median age (years)	28.8	34.2	Mean net wealth per adult (\$2017)	22,346	204,533
Employment (2017)	56,086,808	16,982,868	Living space per person (square feet)	354	787
Average years of schooling (2015)	8.6	13.3	Households with one or more passenger cars (2016)	46%	95%
Population 25+ with graduate or professional degree (2015)	2.1%	9.7%	Households with complete plumbing facilities (2016)	68%	100%
Population 25+ with bachelors degree or higher (2015)	14.8%	28.4%	Households with a refrigerator (2016)	86%	99%
Population 25+ with high school degree or higher (2015)	33.3%	82.4%	Households with a washing machine (2013)	64%	79%
Average annual hours worked	2,255	1,866	Households with a clothes dryer (2013)	6%	78%
Average workweek (hours)	43.2	35.8	Households with a microwave oven (2013)	44%	97%
GDP (\$2017 millions)	2,344,197	1,696,206	Households with a dishwasher (2013)	12%	80%
GDP per capita (\$2017)	18,149	59,927	Households with air conditioning (2013)	13%	98%
GDP per hour worked (\$2017)	18.53	53.52	Households with central heat and air (2013)	13%	91%
Average hourly wage (\$US)	6.79	25.39	Households with a computer (2016)	46%	90%
Growth in GDP per employed person 1990-2017	5.4%	73.6%	Households with access to broadband internet (2016)	39%	80%
Growth in industrial output 1990-2017	131%	188%	Households with a smartphone (2016)	46%	81%
Growth in manufacturing output 1990-2017	81%	196%	Texas merchandise exports to Mexico (\$2017 millions)	—	97,701
Crude oil production (millions of barrels in 2017)	723	1,283	Mexico merchandise exports to Texas (\$2017 millions)	89,833	—

## EXHIBIT 2

# Trade Among Neighbors

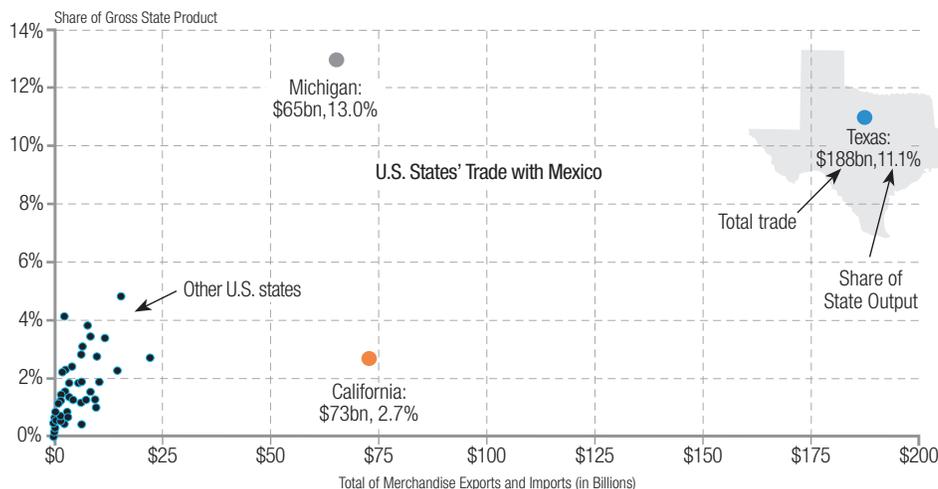
Among states and countries, Mexico ranks as Texas' leading market for both imports and exports, and Texas ranks first for Mexico (*top tables*). Texas stands apart from other states in trade with Mexico, leading in value by far and ranking second in trade as a share of state GDP (*bottom chart*).

2016		
State or Country	Mexico's Exports	Percent
1. Texas	80,958,010	21.6
2. Michigan	49,038,080	13.1
3. California	46,345,060	12.4
4. Illinois	11,706,950	3.1
5. Ohio	7,947,960	2.1
6. Arizona	7,447,940	2.0
7. Tennessee	7,324,040	2.0
8. Georgia	6,469,970	1.7
9. Florida	5,780,630	1.5
10. China	5,411,244	1.4
Other	145,516,810	38.9
Total	373,946,694	100.0

2016		
State or Country	Texas' Exports	Percent
1. Mexico	92,039,140	12.2
2. Louisiana	84,081,297	11.1
3. Oklahoma	51,168,077	6.8
4. California	31,174,385	4.1
5. Illinois	30,694,743	4.1
6. Ohio	23,891,409	3.2
7. Canada	19,965,660	2.6
8. Florida	17,349,696	2.3
9. Pennsylvania	16,170,992	2.1
10. Arkansas	16,050,815	2.1
Other	374,560,552	49.5
Total	757,146,766	100.0

2016		
State or Country	Mexico's Imports	Percent
1. Texas	92,039,140	24.6
2. China	69,520,671	18.6
3. California	25,260,270	6.8
4. Japan	17,751,109	4.7
5. Germany	13,877,975	3.7
6. South Korea	13,612,211	3.6
7. Michigan	12,044,650	3.2
8. Canada	9,631,526	2.6
9. Illinois	9,488,860	2.5
10. Arizona	8,285,200	2.2
Other	115,552,887	30.9
Total	387,064,499	103.5

2016		
State or Country	Texas' Imports	Percent
1. Mexico	80,958,010	10.7
2. California	57,357,706	7.6
3. Oklahoma	42,151,650	5.6
4. Louisiana	39,035,922	5.2
5. China	36,637,860	4.8
6. Illinois	29,051,056	3.8
7. Kansas	22,439,756	3.0
8. Tennessee	17,702,090	2.3
9. Ohio	17,269,865	2.3
10. Indiana	17,113,176	2.3
Other	375,674,436	49.6
Total	735,391,526	97.1



few decades, so we use national statistics to provide the historical sweep. They show that bilateral trade was relatively insignificant from 1869 to the late 1970s (*see Exhibit 1, left panel, Page 4*). Trade rose in the 1980s but didn't take off until the early 1990s—after Mexico opened its market, joined GATT and signed NAFTA.

The migration surge was recent, too. Few Mexicans came to Texas until the decades after the Mexican revolution (*see Exhibit 1, right panel*). The United States forcibly repatriated Mexicans during the Great Depression, and migration resumed with the *Bracero* program to admit agricultural workers.

The pace of migration built slowly over the next few decades, then took its Texico jump in the 1990s before ebbing as U.S. border controls tightened or Mexican workers stayed home to take advantage of job opportunities in Texico's south.

### Ties that Bind

Texico churns out an annual GDP of more than \$4 trillion, good enough to rank as the world's sixth largest economy, just behind Germany and ahead of Russia.

Beyond sheer size, the region's defining characteristic is the gap between north and south. Texans are more educated, better paid and wealthier, and they're more likely to own the signature products of successful economies—from cars to smartphones (*see Box 1, Page 5*). By comparison, Mexicans work harder for lower pay, and they've struggled to build wealth and afford the modern world's household goods.

Two centuries ago, Central Mexico was the richer place, envied by the *Tejanos* living in a sparsely populated and relatively poor part of northern Mexico. The relative merits of open vs. closed economies had a lot to do with the reversal of fortunes—as did policies

shaping economic freedom, the integrity of institutions and investment in human capital.

Forging a stable, dynamic economy that could close the development gap motivated Mexico's opening in the mid-1980s. The country saw its salvation in foreign trade, investment and know-how. Since then, these flows arrived from many places—with big contributions coming from Texas.

Exhibit 1 showed that merchandise trade between the United States and Mexico grew 4.5 times faster after Mexico joined GATT. Domestic and foreign trade differ, but mixing U.S. states with countries shows how Mexico's trade skews on a north-south axis. Mexico trades more with Texas than any *country*, including China. Texas trades more with Mexico than with any other *state*, including neighbors Louisiana and Oklahoma (see Exhibit 2, top tables, Page 6).

Since 1990, Texas has sprinted far ahead of other states in trade with Mexico. Exports moving south and imports moving north totaled \$188 billion last year, or more than 11 percent of gross state product, putting Texas out by itself in doing business with Mexico (see Exhibit 2, bottom chart).

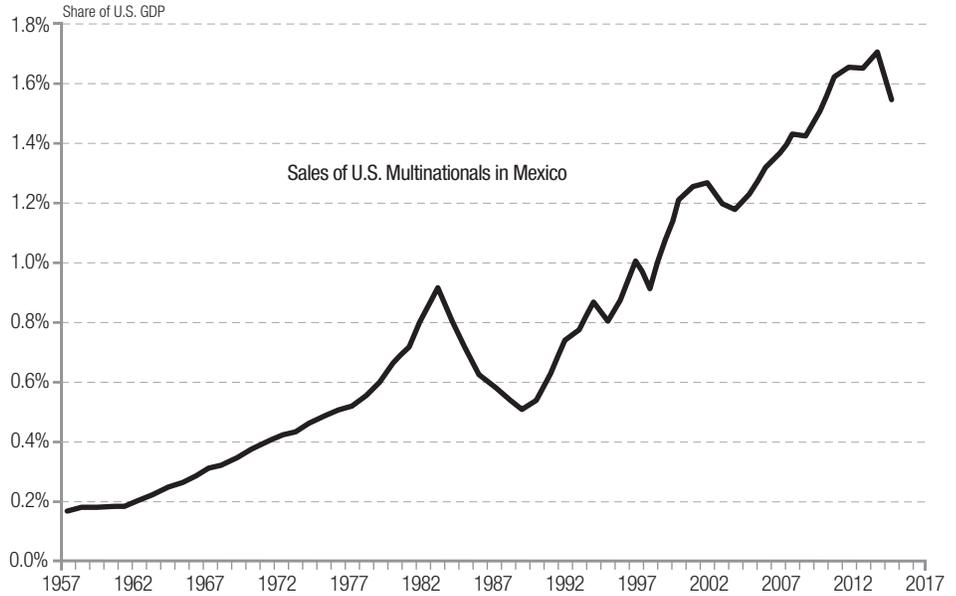
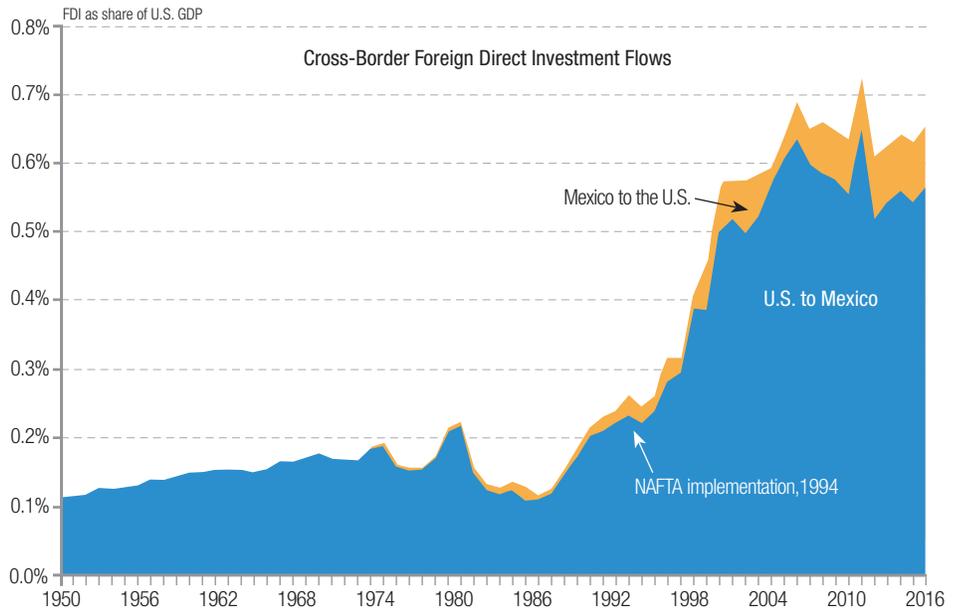
Trade with China, a low-wage competitor of Mexico's, consists mainly of finished goods ready for sale. Within Mexico, intermediate goods make up the biggest chunk of what's shipped across the border. The difference stems from geography—deliveries from Mexico usually take days not weeks.

Cross-border supply chains illustrate why the Texas and Mexico economies are more formidable combined rather than separated. In Mexico's relatively compact geographical area, companies linked by roads, railways and air service combine low-cost labor, skilled professionals and cutting-edge technology in a highly efficient production network. The companies emerge more competitive in the global marketplace, able

**EXHIBIT  
3**

**Open for Business**

With NAFTA's Implementation in January 1994, direct investment broke out of the staid pattern of the previous 40 years, reaching new heights for both the United States and Mexico (*top chart*). The surge in investment coincides with a strong rise in Mexican sales among U.S. multinationals (*bottom chart*).



to sell at a better price.

Automobile production comes to mind—for good reason. General Motors' operation in Arlington and Toyota's factory in San Antonio are among the 27 assembly plants and more than 230 parts suppliers in Texas

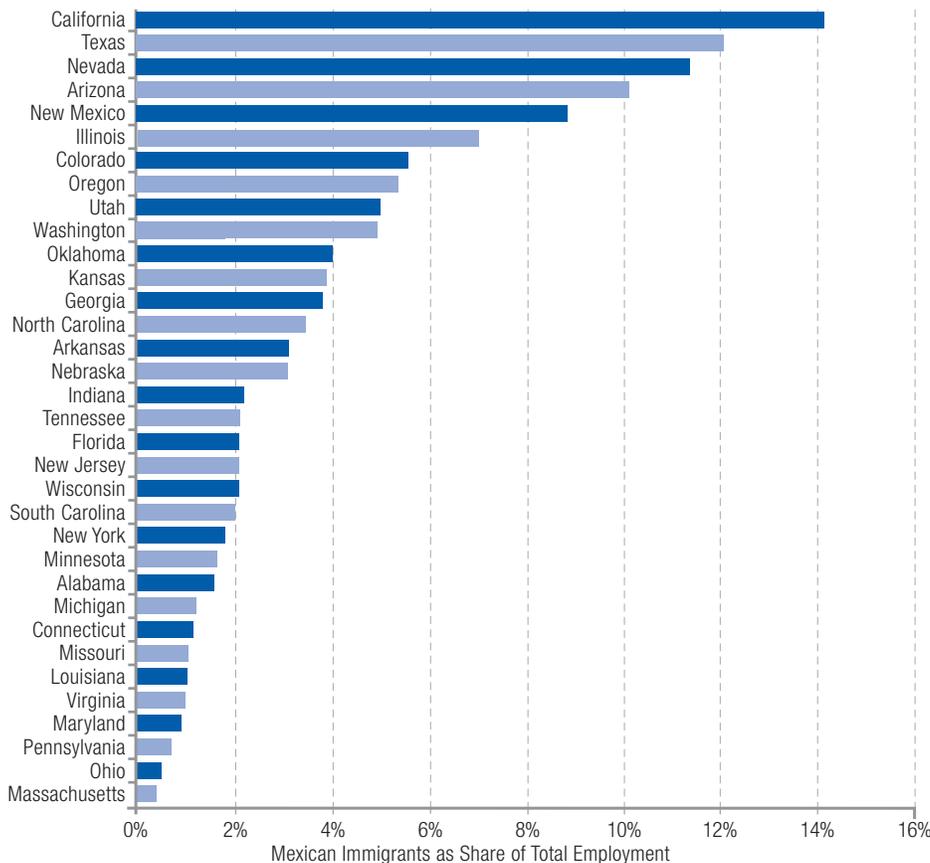
and Mexico's northern states.

Texas companies are finding business opportunities in Mexico—among them, cosmetics-purveyor Mary Kay Inc. and telecommunications giant AT&T Inc. Mexican companies are heading

**EXHIBIT  
4**

## Working for Texas

Most Mexican-born U.S. workers are concentrated in Texas and a few other states (*top chart*). Mexicans make up more than half of all immigrants working in Texas, with their biggest contribution—by far—in construction, followed by manufacturing and agriculture (*bottom table*).



INDUSTRY	Foreign Born	Born in Mexico	Born in Other Latin American Countries	Born Elsewhere
Agriculture <sup>1</sup>	20.8%	12.2%	2.3%	6.4%
Construction	41.8	33.6	6.6	1.7
Manufacturing	27.4	14.7	3.7	9.1
Wholesale Trade	20.3	10.7	3.5	6.2
Retail Trade	17.7	8.8	2.7	6.2
Transportation <sup>2</sup>	20.2	10.4	4.0	5.9
Information	16.2	4.1	2.9	9.3
Financial Services <sup>3</sup>	13.4	5.0	2.1	6.4
Professional Services <sup>4</sup>	23.1	11.2	3.5	8.5
Health Services <sup>5</sup>	16.7	6.6	2.0	8.1
Arts and Recreation, including Food Service <sup>6</sup>	25.0	15.6	4.4	5.0
Public Administration	8.5	3.4	0.9	4.1
Other	32.1	18.0	4.9	9.2
<b>Statewide Average</b>	<b>22.0</b>	<b>12.0</b>	<b>3.3</b>	<b>6.7</b>

1. Agriculture, forestry, fishing, hunting and mining. 2. Transportation, warehousing and utilities. 3. Finance, insurance, real estate, rental and leasing. 4. Professional, scientific, management, administrative and waste management services. 5. Health care, educational services and social assistance. 6. Arts, entertainment, recreation, accommodation and food services.

northward and expanding their businesses, with tortilla-maker Mission Foods and Cinépolis, a movie theater chain, both settling in the Dallas area.

Setting up business in other countries entails foreign direct investment (FDI)—money spent to gain a physical presence on the ground. For most of its history, Mexico has been labor rich and capital poor; attracting more FDI was a key goal of the country’s market opening. Data aren’t available for Texas’ FDI in Mexico, but state firms no doubt played a big role as the U.S. total soared to unprecedented levels since NAFTA went into force (*see Exhibit 3, top chart, Page 7*). Most U.S. companies invest in Mexico to establish supply chains that lower production costs.

A relative trickle before NAFTA, Mexican FDI bound for the United States picked up sharply in the past two decades. For Mexican investors, of course, the motive for FDI is almost always tapping into the rich U.S. consumer market. Many companies start U.S. operations selling to Hispanics, then broaden to a larger and more diverse market once they’ve established themselves.

Not all U.S. companies invest in Mexico to produce. Some enter the market to sell to consumers who display an affinity for U.S. brands. FDI catering to consumers has paid off: U.S. multinationals’ sales jumped from 0.5 percent of U.S. GDP in 1989 to around 1.6 percent of a much higher GDP in the most recent data (*see Exhibit 3, bottom chart*).

Integration doesn’t just entail goods and capital finding their markets. For millennia, migrants have been moving across borders to find work. Mexicans who want to work legally in Texas—or anyplace else in the United States, for that matter—face strict immigration limits intent on keeping foreigners from

competing for jobs with U.S. workers.

Although labor is Texico's least-free market, foreign-born workers have become an important part of the Texas economy's success. Immigrants held 22 percent of the state's jobs in 2017, compared with 17 percent for the nation

as a whole. The largest share of Texas' foreign-born workforce comes from Texico's southern half.

With native Mexicans filling 12 percent of jobs, Texas ranked second only to California and well ahead of all but a handful of other states (*see Exhibit 4, top*

*chart, Page 8*). In Texas, Mexican-born workers make their biggest contribution to the Texas economy in construction, accounting for a third of all employment in such trades as drywall installers, roofers, carpet and tile installers, painters and cement masons (*see Exhibit 4, bottom table*). Mexican immigrants work in every other sector—with high employment shares in manufacturing, agriculture and the broad category that includes food-service jobs.

Over the past two decades, Texas added 9 million new residents and created 4 million jobs—both tops among states. Providing the homes, offices, stores, factories and infrastructure to accommodate all these new people and companies without soaring real estate prices required a massive building spree. It's hard to see how the state could have done it without Mexican workers.

With the state's unemployment rate at historic lows of around 4 percent, a persistent worry has been the possibility of labor shortages, particularly in construction and related industries. In Texas, the rapid growth of the past quarter century can't continue unless the state finds the workers it needs.

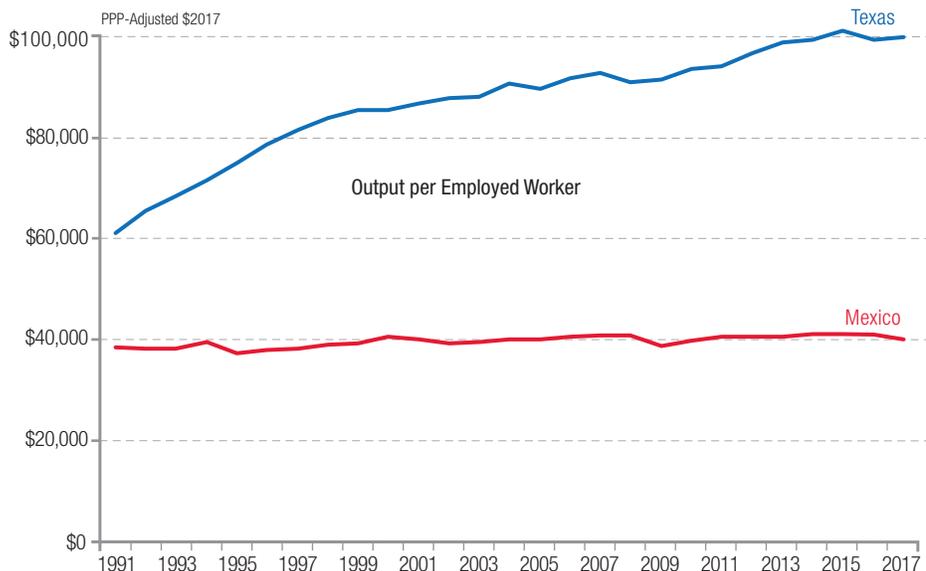
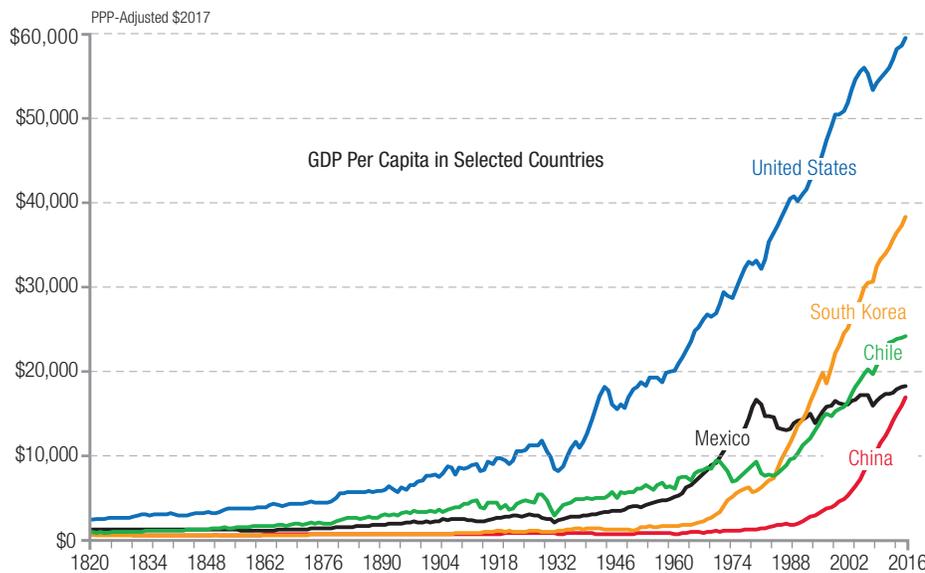
Texico offers a large pool of skilled labor that, if allocated by market forces, could meet many of those needs. The migration data in Exhibit 1, however, point to a decline in Mexicans coming to Texas, so the Rio Grande still splits Texico's labor market in two.

Soaring cross-border trade and investment flows, Mexican workers helping to build the Texas economy, multinationals erasing borders—these are proof positive of Texico's increasing integration. The deepening partnership between Texas and Mexico also shows up in other ways that are harder to measure—in particular, supply chains and knowledge transfers.

**EXHIBIT  
5**

**Falling Behind**

In recent decades, Mexico hasn't kept pace with the United States or the top emerging-market success stories in real per capita income (*top chart*). At the same time, Mexico has lost ground to Texas, with the gap in output per employee rising from \$22,654 in 1991 to \$59,687 in 2017 (*bottom chart*).



## Convergence Conundrum

While Texas and Mexico have been connecting their economies, they've both also been integrating with the rest of the world. That's just the nature of the process—open to one, open to all.

Globalization has added fuel to a Texas economy that scores well on just about every measure of success—GDP growth, job creation, income gains, innovation,

entrepreneurship, domestic and international inflows of people and businesses, the list could go on. Trade policy comes under Washington's purview, but an open economy fits well with the Texas Model of economic freedom, which keeps taxes low and government small to allow the private sector to compete both at home and abroad.

Mexico's market-opening reforms rested on the same philosophy, seeing a path to prosperity in removing the heavy hand of

government that held down the private sector. Mexico's economy went through big changes in the past three decades, and many of these changes were for the better, but the new policies didn't deliver all they promised.

Mexico's economy tanked just as NAFTA went into effect in 1994, but it bounced back and per capita GDP grew at an average annual rate of 0.9 percent for the next quarter century. The figure doesn't match the years of the Mexican Miracle; it also

## Box 2 Borderlands' Integration

# From the Periphery to the Center

It took a long time for Texas and Mexico to get serious about integrating their economies. Residents living on both sides of the Rio Grande might be justified in wondering why—they've been doing it for generations, sometimes without the consent of government.

Cultural and familial ties unite border communities in Texas and Mexico, and people have routinely made short trips to another country to shop, work and socialize. The *de facto* integration emerged in simpler times, when economics took precedence over border security.

The result was an integrated economy straddling the 1,254 mile border—a Texico in microcosm. The Texas side's well-being depended on trends in the Mexican economy, such as the exchange rate of the peso. The Mexican side's fortunes were tied to the U.S. economy because many of its factories supplied industries north of the border.

Decades before the broader Texico emerged, a few policies to promote integration helped shape the border region's economy. The U.S. *bracero* program welcomed Mexicans across the

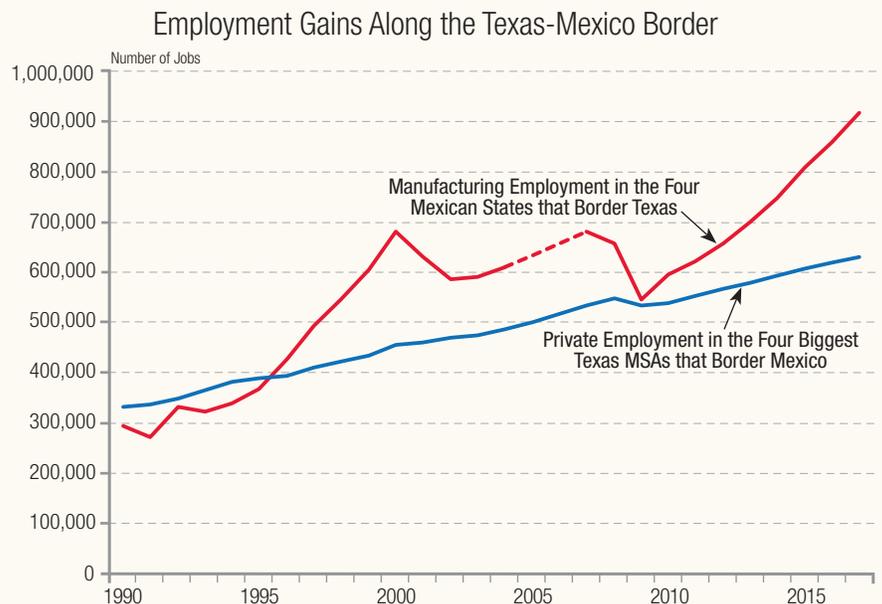
border to work on U.S. farms from 1942 to 1964. Mexico's *maquiladora* program, started in 1965, provided incentives to low-wage manufacturing by allowing duty-free entry for inputs used to produce goods sent back to companies on the U.S. side.

### Adding Jobs, North and South

Fourteen Texas counties line the north bank of the river, but most border

region economic activity takes place in four metropolitan areas—El Paso, Laredo and—in the Rio Grande Valley—Brownsville and McAllen. On the river's south bank are the Mexican states of Chihuahua, Coahuila, Nuevo Leon and Tamaulipas, home to many light manufacturing companies (*see map*).

Since NAFTA went into effect in 1994, the border region moved from the periphery of two national economies



trails the United States (1.5 percent) and the modern era's most successful developing economies. From 1993 to 2017, per capita GDP grew by 4.0 percent a year in South Korea, 3.1 percent in Chile and 8.7 percent in China (see Exhibit 5, top chart, Page 9).

Economics sees integration as an agent for convergence—the poorer side growing faster and gaining ground on the richer one. Not so in Texico; Mexico has slipped farther behind its neighbor since 1991. Output per worker,

has been flat at around \$40,000 for Mexico, while it rose from \$60,000 to \$100,000 in Texas (see Exhibit 5, bottom chart).

Statistics like these aren't the end of the convergence story. We can also look at some direct evidence of relative living standards.

In Texico, gaps between household ownership of basic and durable goods have been closing for decades. Mexico now nearly matches the United States in the

share of households with electricity and color televisions (see Exhibit 6, top chart, Page 12). Mexicans have also been catching up in ownership of some household goods, such as washing machines and refrigerators. The share of Mexican homes with complete indoor plumbing has been rising steadily toward U.S. levels. Air-conditioning shows no gains.

Convergence seems to be delayed

to the center of an emerging North American market. Big changes followed. Tarriff cuts and the breakdown of other economic barriers took away some of the advantages of producing just south of the Rio Grande, effectively ending the *maquiladora* program. Factories moved inland, but many companies also climbed up the value chain to higher-value products.

When producing goods, being close to the United States still pays off. Since 1990, manufacturing employment in the four Mexican states abutting Texas tripled to 900,000 workers, well ahead of Mexico's overall job growth (see chart left).

There's also been growth on the Texas side, where agriculture and services drive the economy. Employment in the four large metropolitan areas doubled to more than 630,000 workers since 1990, more or less in line with the performance of the rest of the state.

### Still a Busy Border

Crossing the border isn't as easy as it once was. Since the 1980s, the United

States has been tightening border security in an effort to deter illegal immigration and drug smuggling—stepping up money and manpower after the September 11, 2001 terrorist attacks. Annual Texas crossings by pedestrians and travelers in passenger cars, busses and trains have fallen sharply in the past two decades—from 163 million in 1999 to 86 million in 2017.

By contrast, comercial traffic is bustling like never before, largely because of the dynamism generated by Texico. In 2017, more than 3.3 million loaded truck containers and 467,750 loaded rail containers moved across the Texas-Mexico border. Among the 11 ports of entry along the Rio Grande, Laredo leads the way—it's the nation's second busiest

customs district for exports and third busiest for imports.

Combining the movement of truck and rail containers yields shows the stunning increase in the border region's commercial traffic. The total tripled from 1.3 million containers in 1996 to 3.9 million in 2017.

Unless ill winds from Washington or Mexico City undercut Texico, the border region should remain central to the deepening integration of the Texas and Mexico economies. Northern Mexico will continue its orientation toward the needs of the U.S. market, and South Texas will continue to be the part of the state with the closest ties to Mexico.



for some products. The gap in automobile ownership only began to shrink in the past five years or so. Mexican households were late in buying many popular technology products (*bottom chart*). The catch-up didn't begin until the early 2000s for computers, mobile phones and Internet access. Smartphones made their first gain just a few years ago, and laptops are still losing ground.

Mexico achieved some convergence, but why hasn't it been faster? First off, the United States and the other highly successful economies kept a good pace in running ahead, making it harder for Mexico to catch up. It's possible to find countries—and even some U.S. states—that haven't performed as well as Mexico. The goal of the market opening, of course, wasn't to converge with Argentina.

A second point centers on the nature of economic transitions. Economies don't turn at the snap of a finger—or the signing of a NAFTA-like trade deal. It takes time to unwind existing economic structures and shift resources from less competitive sectors to more competitive ones.

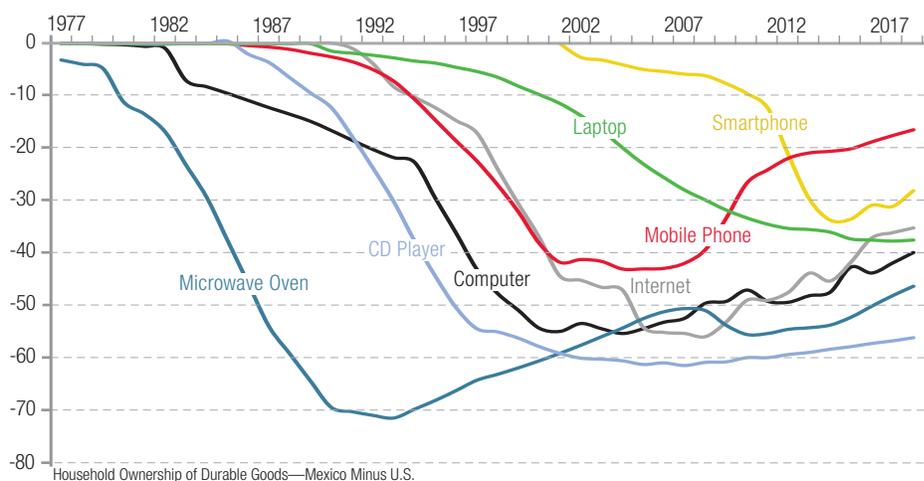
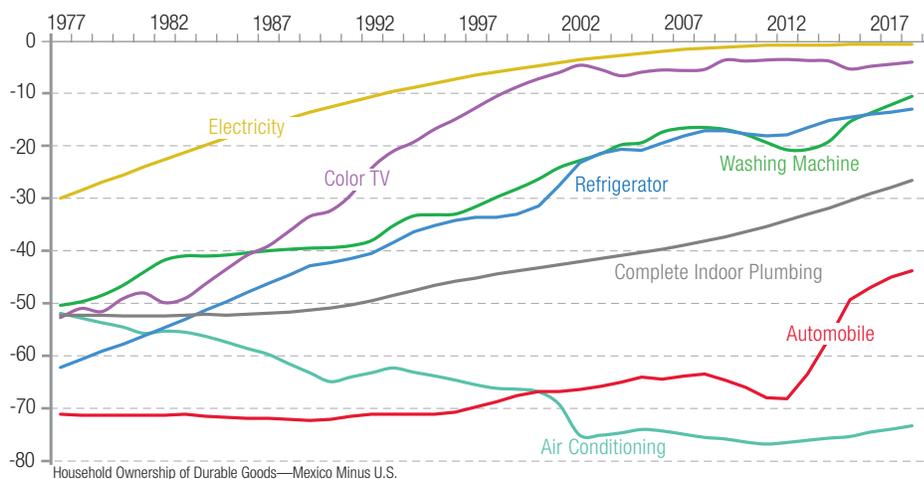
History shows that countries that throw off their import substitution strategies don't usually do it all at once and rarely get immediate and unequivocal success. South Korea, Chile and China all got off to slow starts after opening their economies—but they stuck with it and reached their sweet spots for growth.

The strategy for market opening, moreover, might involve a deliberate gradualism to ease transition costs or sway powerful interests that might oppose the new policies. For example, NAFTA compromised on free trade with provisions to protect the turf of the Mexican telecommunication and energy industries and U.S. trucking companies. When countries leave reforms incomplete, delay them or backslide, existing inefficiencies

**EXHIBIT  
6**

## Slow to Converge

Mexico has been catching up with the United States in household ownership of some basic services and durable goods (*top chart*). The gap between the two countries in computers, mobile phones and other digital goods widened in the 1990s and only began to close in the past decade or so (*bottom chart*).



persist, slowing the transition to a freer and more efficient economy.

A third reason that market-opening initiatives falter—more toxic than the others—involves institutions and governance. Integration does best with a social infrastructure that includes such things as respect for private property, effective administration under the rule of law, transparent regulation and sound money. Failure to maintain these virtues undermines confidence, discourages

foreign participation and degrades economic performance.

The factors favorable to integration are summed up in the term economic freedom, and economists have been measuring it for decades, first for nations and later for North American states and provinces. Since 1990, *Economic Freedom of the World (EFW)* scores have risen for Chile, South Korea and China, the three nations growing faster than Mexico (*see Exhibit 7, below*). The readings suggest a

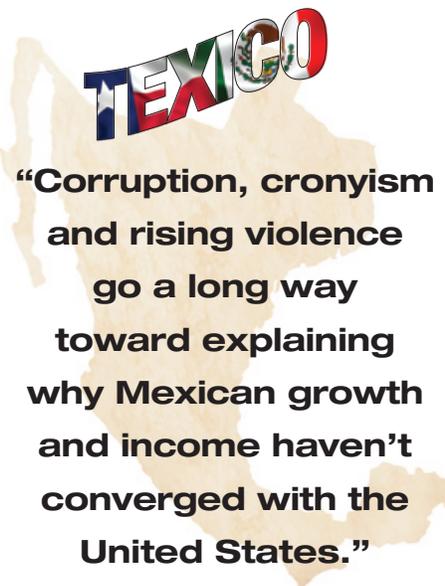
steady commitment to market opening.

Texas' policies pass muster, too. The *Economic Freedom of North America (EFNA)* report indicates there's little to worry about in Texico's north, with Texas consistently among the Top Five U.S. states in economic freedom and the United States among the freest countries.

Texico's south is another matter. Looking just at national policies, the *EFW* report indicates that Mexico's economic freedom, while low by U.S. standards, increased from 1990 to 2006; after that, it declined for a few years before starting to rise again (*solid black line*).

Mexico's overall gain in the 25-year period didn't match the performances of Chile, South Korea and China, suggesting Mexico wavered somewhat in implementing its reforms, most likely to appease domestic interests.

An occasional waver or delay on a policy, of course, isn't likely to stall convergence.



The rest of the story lies in what's happening with Mexico's state and local governments. From 1990 to 2016, the *EFNA* all-government index, which looks at economic freedom across all jurisdictions, followed the national government's line

upward (*dotted black line*). In the past decade, however, the measure began to decline sharply—an ominous sign.

Before the reforms of the 1980s, corruption and cronyism beset Mexico's economy. Recent years' declining all-government scores suggest old ways have crept back into the system, perhaps not as much with the central government as with state and local authorities. Mexican states differ quite a bit in economic freedom, but in too many places corruption has allowed drug cartels to operate with relative impunity, bringing waves of fear and violence.

Reports from Mexico and the work of independent anti-corruption organizations also point to the country's continuing struggles. Transparency International (TI), for example, ranked Mexico 135th in the world in 2017—with a corruption-perception score even lower than what TI reported two decades ago.

Corruption undermines public faith in the rule of law. It rots an economy from within, sapping the effectiveness of policies that support economic freedom and integration.

Other factors like low levels of education shouldn't be ignored, but the ongoing plague of corruption, cronyism and rising violence go a long way toward explaining why Mexican growth and income haven't converged with the United States or kept pace with the likes of Chile, South Korea and China.

### Texico at a Crossroads

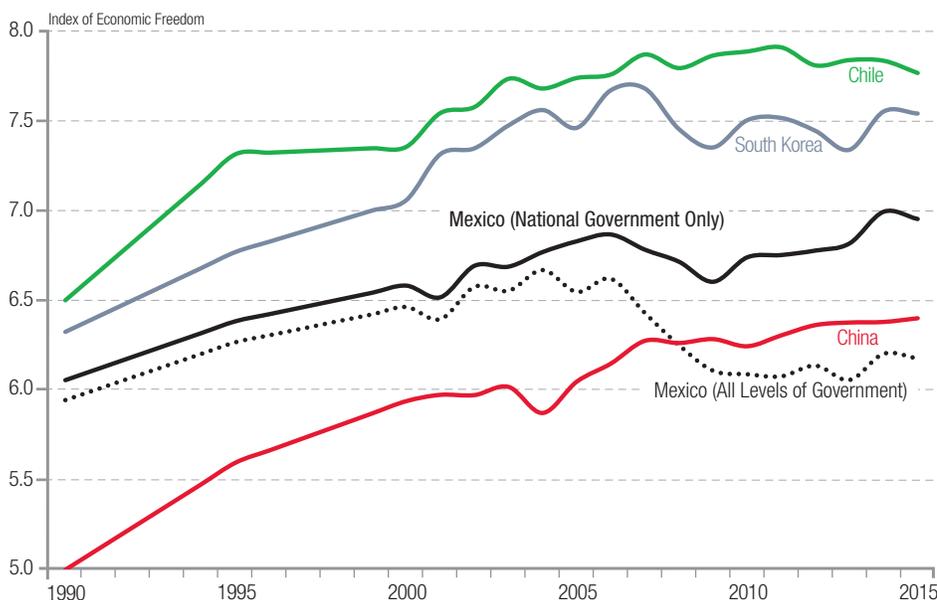
Mexico's market opening wasn't designed or executed well enough to put the economy on the fast track and deliver a quick convergence. Does that mean the policies have failed and Mexico ought to try another wrenching turn in economic strategy?

Texas counts its blessings from closer economic ties to Mexico, but other places in the United States view trade as more

## EXHIBIT 7

### Faltering Economic Freedom

With policy reforms, Mexico's economic freedom score for national government rose after 1990 (*black line*)—other emerging countries had larger gains. When state and local governments are included, Mexico's all-government economic freedom declined in the past decade (*dotted black line*).



burden than blessing, with Mexico a frequent bogeyman. Should America turn to trade barriers in an effort to protect jobs?

Questions like these aren't new, of course, but now those in power seem to be asking them. In a nutshell, that's the reason why Mexico unexpectedly faces an uncertain future. It's not the economics, nor current policy, it's the politics and what they bode for the future.

Since he began running for president, Donald Trump has been hostile to Mexico,

threatening to blockade the country behind a border wall and pull out of NAFTA. He's been willing to engage in trade brinkmanship by threatening to raise tariffs. Rather than pull out of NAFTA, Trump opted to renegotiate the pact with Mexico and Canada. In late August, the United States and Mexico reached the framework for a new NAFTA deal—but its fate will depend on politics and how events play out over the next few months.

In 2018, Mexican voters added to

Mexico's uncertainty by voting to elect populist Andres Manuel Lopez Obrador, who will take office in December. The president-elect has been cryptic about whether he intends to keep Mexico open for business or veer toward the economic nationalism he espoused earlier in his political career. One of Obrador's first orders of business after being sworn in may be deciding what to do with the updated NAFTA deal.

Will either or both of these leaders try

### Box 3 Oil Production

## To Frack or Not to Frack

Knowledge transfers are a prime benefit of an open economy. NAFTA, for example, opened Mexico to U.S., European and Asian automobile companies, giving a generation of Mexican workers and managers hands-on experience in modern manufacturing methods. San Antonio-based grocer H-E-B, Walmart, Costco, Starbucks and dozens of other U.S. fast-food and specialty stores exposed Mexico to U.S. retailing practices and strategies.

Led by Houston-area firms, Texas is on the cutting edge of energy technology, and it could teach Mexico a great deal about oil exploration and production—and new policies just might provide the opportunity.

Nationalization of the oil industry in 1938 gave state-owned Petroleos Mexicanos (Pemex) a monopoly on the exploration, production and distribution of petroleum products. Mexico clung to it in NAFTA negotiations, and foreigners remained *prohibido* for the next two decades.

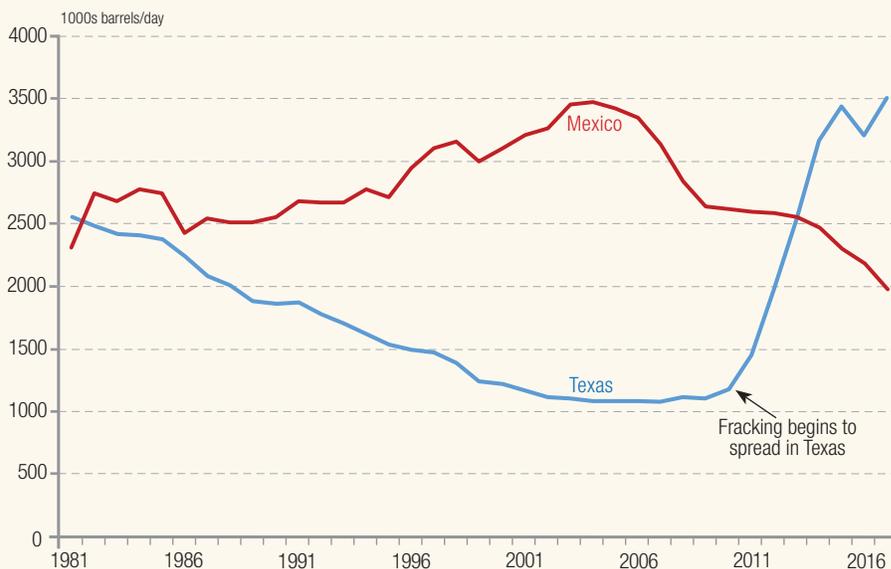
Without foreign partners or competitors, Pemex became bloated, bureaucratic and backward. Oil output fell from almost 3.5 million barrels a day in 2004 to less than 2 million barrels in 2017—with no sign Pemex could engineer a revival (*see chart right*).

A quarter century before Mexico's peak, Texas' oil production was seemingly in terminal decline, going from 2.5 million barrels a day in 1981 to less than 1.1 million in 2009. After that, the industry bounced back the American way—through innovation and entrepreneurship.

Led by George Mitchell's operations in the Barnett Shale outside Fort Worth, the industry found that a combination of hydraulic fracturing and horizontal drilling could coax huge amounts of oil and gas from shale formations. As the frackers ramped up operations and refined their techniques,

Texas oil output rebounded to more than 3.5 million barrels a day in 2017.

Recognizing the need for investment and expertise to reverse the decline in oil output, Mexico opened its industry to foreigners and private companies in 2014. In a series of auctions, the country sold dozens of leases to foreign companies, mostly for off-shore exploration in the Gulf of Mexico. New reserves have already been found, but Mexico has so far shied away from ventures for fracking, despite the record for boosting oil production in Texas.

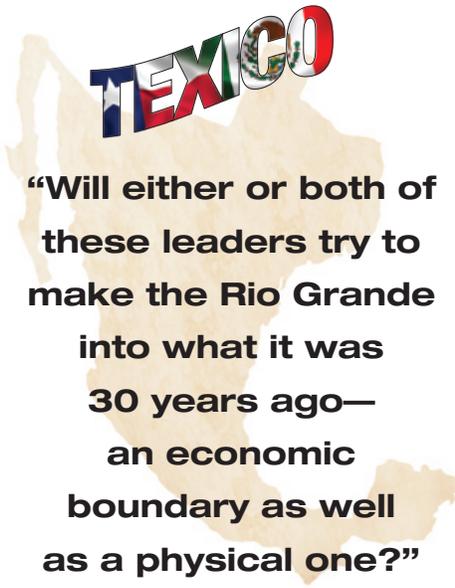


to make the Rio Grande into what it was 30 years ago—an economic boundary as well as a physical one? No place has a bigger stake in what happens than Texico, where decades of expanding cross-border business created a large constituency for open trade and investment. Supporters on both sides of the border proclaim, often and loudly, that the best course lies in allowing integration to continue, perhaps with a little NAFTA fine-tuning.

The gains from trade and investment already realized make a strong case for maintaining the connections across the border. Looking to the future makes the case even better because of the vast untapped potential for business in Texico, especially if Mexico reverses the erosion of its economic freedom.

Take a quick look at energy. Mexico’s oil output peaked a decade ago, prompting the country to open a long-closed industry to foreigners (*see Box 3, Page 14*). Meanwhile, innovation and entrepreneurship reversed the decline in Texas’ oil production and sent it soaring to record heights.

The synergies are obvious and just starting to kick in. To Texico’s south, there’s an oil-rich country with a land mass three times greater than Texas and a coastline nearly 16 times as long. To Texico’s north, there’s a state with world-class expertise in oil exploration and



production and a track record of success around the world. The payoff could be enormous on both sides of the border.

Beyond the oil sector, opportunities abound. Goods now dominate Texico trade, but the No. 1 country in services exports starts just north of the Rio Grande. What Texico north and south did for automobile supply chains could be extended to other industries. Texas and Mexico firms could combine their talents to penetrate export markets in places like Europe, Asia and South America. Led by builders and landscapers, Texas employers worry about labor shortages while willing workers wait in Mexico. With changes in

immigration laws, benefits would flow to both parts of Texico.

Before gaining real momentum, the integration of the Texas and Mexico economies had to wait for the moment that both economics and policy were right. The challenge for the future lies in keeping them right.

The outlook couldn’t be brighter on the economics because of the myriad connections made in the past three decades and the potential for so many more. The uncertainty lies in policy—or rather politics. In the short term, Texico’s businesses will be looking to the completion of the NAFTA negotiations for signals on how the current political mood will impact integration’s standing.

Perhaps Trump and Obrador will decide that the best course lies in expedient practicality—recognizing the fact that Texico built a large constituency because both sides recognize it works better than the alternative of economic nationalism. If these two leaders can see that, the businesses of Texas and Mexico can take it from there—as they’ve been doing for three decades.

*W. Michael Cox is founding director of the William J. O’Neil Center for Global Markets and Freedom (wmcox@smu.edu). Richard Alm is writer in residence at the center (ralm@smu.edu).*

## Notes and Data Sources

The authors would like to thank José Torra, Roberto Salinas León and the Mission Foods Texas-Mexico Center at SMU for their help with this project.

### Exhibit 1: Slow to Gain Traction

*Historical Statistics of the United States: Millennial Edition*, U.S. Census Bureau, U.S. Department of Commerce; *Statistical Abstract of the United States*, U.S. Census Bureau, U.S. Department of Commerce, available at census.gov; Federal Reserve Bank of St. Louis, FRED data retrieval system, available

at fred.stlouisfed.org; Bureau of Economic Analysis, U.S. Department of Commerce, available at bea.gov; *Yearbook of Immigration Statistics*, Office of Immigration Statistics, Department of Homeland Security, available from dhs.gov; *Statistical Abstract of the United States*, U.S. Census Bureau, U.S. Department of Commerce, available from census.gov. U.S.-Mexico trade is for merchandise only. Data for 1820 to 1979 are estimated on the basis of total immigration from Mexico to the U.S. in those years and later-year statistics on the share of Mexican immigrants to the U.S. whose state of intended residence is Texas.

*Continued next page*

### Box 1: Mexico and Texas, By the Numbers

Geographic Terms and Concepts, Census 2000 Geography Glossary, U.S. Census Bureau, U.S. Department of Commerce, available at [census.gov](http://census.gov); World Development Indicators Databank, The World Bank, available at <http://databank.worldbank.org>; OECD Main Economic Indicators, Organization for Economic Cooperation and Development, available at <https://stats.oecd.org/>; Bureau of Economic Analysis, U.S. Department of Commerce, available at [bea.gov](http://bea.gov); American Community Survey, U.S. Census Bureau, U.S. Department of Commerce, available at <https://factfinder.census.gov>; Euromonitor International; *Credit Suisse Global Wealth Report 2017*, Credit Suisse Research Institute, available at [credit-suisse.com](http://credit-suisse.com); Zillow Group, available at [zillow.com](http://zillow.com); Bureau of Labor Statistics, U.S. Department of Labor, available at [bls.gov](http://bls.gov); UNESCO Institute for Statistics, available at <http://data.uis.unesco.org>; *Statistical Abstract of the United States*, U.S. Census Bureau, U.S. Department of Commerce, available at [census.gov](http://census.gov); *The World Factbook*, U.S. Central Intelligence Agency, available at [cia.gov](http://cia.gov).

### Exhibit 2: Trade Among Neighbors

U.S. Census Bureau, U.S. Department of Commerce, available at [census.gov](http://census.gov); Instituto Nacional de Estadística y Geografía, Secretaría de Hacienda y Crédito Público de México, available at [inegi.org.mx](http://inegi.org.mx). Data are for merchandise trade only.

### Exhibit 3: Open for Business

*Historical Statistics of the United States: Millennial Edition*, U.S. Census Bureau, U.S. Department of Commerce; *Statistical Abstract of the United States*, U.S. Census Bureau, U.S. Department of Commerce, available at [census.gov](http://census.gov); *Selected Data on Foreign Direct Investment in the United States, 1950-79*, Bureau of Economic Analysis, U.S. Department of Commerce, December, 1984, available at <https://fraser.stlouisfed.org>; *The Maturing of Multinational Enterprise*, Mira Wilkins, Harvard University Press, Cambridge, MA, 1974; *Survey of Current Business* and online data, Bureau of Economic Analysis, U.S. Department of Commerce, available at [bea.gov](http://bea.gov).

### Exhibit 4: Working for Texas

American Community Survey, U.S. Census Bureau, U.S. Department of Commerce, available at <https://factfinder.census.gov>. Data are for 2015.

### Exhibit 5: Falling Behind

Maddison Project Database, version 2018. Bolt, Jutta, Robert Inklaar, Herman de Jong and Jan Luiten van Zanden (2018), available at [ggdc.net/maddison](http://ggdc.net/maddison); World Development Indicators DataBank, The World Bank, available at <http://databank.worldbank.org>; Bureau of Economic Analysis, U.S. Department of Commerce, available at [bea.gov](http://bea.gov); Bureau of Economic Analysis, U.S. Department of Commerce, available at [bea.gov](http://bea.gov); World Development Indicators Databank, The World Bank, available at <http://databank.worldbank.org>.

### Box 2: Borderlands' Integration

Bureau of Labor Statistics, U.S. Department of Labor, available at [bls.gov](http://bls.gov); Instituto Nacional de Estadística y Geografía, Secretaría de Hacienda y Crédito Público de México, available at [inegi.org.mx](http://inegi.org.mx).

### Exhibit 6: Slow to Converge

World Development Indicators Databank, The World Bank, available at <http://databank.worldbank.org>; Instituto Nacional de Estadística y Geografía, Secretaría de Hacienda y Crédito Público de México, available at [inegi.org.mx](http://inegi.org.mx); Euromonitor International, available at [euromonitor.com](http://euromonitor.com); W. Michael Cox and Richard Alm, "Onward and Upward: Bet on Capitalism—It Works," 2015-16 Annual Report, O'Neil Center for Global Markets and Freedom, Cox School of Business, Southern Methodist University, available at [oneilcenter.org](http://oneilcenter.org); Bureau of Economic Analysis, U.S. Department of Commerce, available at [bea.gov](http://bea.gov).

### Exhibit 7: Faltering Economic Freedom

*Economic Freedom of the World: 2017 Annual Report and Economic Freedom of North America 2017*, Fraser Institute, available at [fraserinstitute.org](http://fraserinstitute.org).

### Box 3: Oil Production

U.S. Energy Information Administration, U.S. Federal Statistical System, available at [eia.gov](http://eia.gov).



# 2017-18: Year in Review

The O’Neil Center’s headline event for the 2017-18 academic year was a packed house for a speech by renowned economist Walter Williams, who warned that government growing bigger and more powerful posed a danger to individual liberty (*see box right*).

Before and after that October evening, our scholars published almost 50 articles for academic and general interest publications, and delivered nearly 70 speeches, presentations and lectures. They produced new data on economic freedom.

In addition to Williams’ speech, the center’s public events included lectures by five distinguished scholars, and the Texas Economic Forum discussed DFW’s innovation economy in the fall and the impacts of President Trump’s policies on the state economy in the spring.

The center’s Annual Report essay explored the long-run interaction of technology and economic progress, with the goal of helping readers better understand today’s upheavals and angst. Teaching Free Enterprise in Texas, a program providing instruction and curriculum materials to improve economic education in high schools, had its biggest year ever with more than 1,000 teachers attending workshops, plus six new curriculum units.

O’Neil Center professors taught over 700 students in SMU classes, with 72 more attending the center’s six reading groups. The Workshop Series for academics featured seven presentations of research in progress. In the spring semester, the center began commemorating the 10<sup>th</sup> anniversary of its founding (*see inside back cover*). Recognition of the 10-year milestone will continue in the fall semester.

Williams’ speech took the place of the O’Neil Center’s annual conference, which for eight years had brought together well-known economists, authors and business

leaders to discuss current issues within a framework of economic freedom. In the upcoming academic year, the conference will return. Before the end of May, the center had already received commitments from speakers, including Nobel laureate Vernon Smith, for a September program on the “Ethical Conundrums of Capitalism.”

The O’Neil Center studies why some

economies are rich and growing rapidly while others are poor and growing slowly. To this end, it fosters an understanding of economic freedom among students, policymakers and the general public. We’re the only research institute with expertise in measuring economic freedom at all three levels of economic analysis—national, state and metropolitan areas.



## A Free-Market Icon at SMU

Walter Williams began with a few data points on the growth of public spending and taxing over the past century. The George Mason University professor said these numbers showed that government had expanded far beyond its legitimate functions, such as national defense, policing, adjudicating disputes and providing true public goods.

Williams told an audience of nearly 500 people at SMU’s Hughes-Trigg theater exactly what he saw in this bigger government—a threat to individual liberty. “The ultimate end of this process, ladies and gentlemen, is totalitarianism and tyranny.”

“I am not saying we are a totalitarian nation yet,” he continued. “But if you ask the question, ‘Which way are we headed tiny steps at a time? Are we headed toward more personal liberty or are we headed toward more government control over our lives?’ It would almost unambiguously be the latter. And remember, if you take tiny steps toward any goal, you’re sooner or later going to reach it.”

Williams conceded that government grows out of people’s desire to do good—to help, for example, the poor or elderly. Yet, government has no resources of its own, and political leaders in Washington and state capitals don’t reach into their own pockets when trying to do good. “The only way the government can give one American \$1 is through coercion, threats and intimidation to confiscate that dollar from some other American.”



*Robert Lawson*



*Albert W. Niemi*



*W. Michael Cox*



*Dean Stansel*



*Richard Alm*



*Meg Tuszynski*

The center relies primarily on donors to fund its operations. With an annual budget of over \$2 million, the center is grateful for the generous support of the William E. Armentrout Foundation, McLane Company, Inc., the Charles G. Koch Charitable Foundation, the William J. O’Neil Foundation, the Deason Foundation, Richard W. Weekley, Tucker Bridwell and numerous other individual donors.



The O’Neil Center’s staff remained unchanged—with one exception. Managing director **Derek Yonai** left in October to become the director of the Koch Center for Leadership and Ethics at Emporia State University. **Meg Tuszynski**, who joined the center in 2016 as a research associate, was promoted to faculty rank and replaced Yonai, with the title of assistant director.

In addition to Tuszynski, the O’Neil Center finished the academic year with:

**Robert Lawson**, the Jerome M. Fullinwider Centennial Chair in Economic Freedom, completed his third year as director;

**Al Niemi**, the William J. O’Neil Chair in Global Markets and Freedom, stepped down as SMU Cox dean, returning to teaching and research as a member of the

center in August 2017;

**W. Michael Cox**, founding director of the O’Neil Center, led the Texas Economic Freedom initiative and co-authored the center’s Annual Report essay;

**Dean Stansel**, research associate professor, co-authored the Economic Freedom of North America (EFNA) report and led student reading groups;

**Richard Alm**, writer-in-residence, collaborated with the Cox on the Texas Economic Freedom initiative and Annual Report essay;

**Mike Davis**, senior lecturer, once again shouldered the center’s heaviest teaching load and was a versatile and quotable resource for local TV and other media;

**Ryan Murphy**, research assistant professor, primarily worked with Lawson on economic freedom research and led the center’s advanced reading group;

**Daniel Serralde**, economic education coordinator, continued to expand the Teaching Free Enterprise in Texas program;

Program specialist **Liz Chow** assisted with logistics and marketing of the center’s events and initiatives;

**Dwight Lee** continued his affiliation with the O’Neil Center as a Senior Fellow, visiting the SMU campus twice during the academic year and using his SMU affiliation

for his writings and other professional activities. Lee decided to retire fully at the end of the 2017-18 academic year.



This Review reports on the center’s activities and accomplishments for the academic year that began on June 1, 2017, and ended on May 31, 2018. It starts with the center’s three mutually supporting research agendas:

- Global Economic Freedom, which concentrates on measuring economic freedom and its impact on key metrics of national performance;
- Economic Freedom of North America, which takes a similar approach to studying state and metropolitan-area economic freedom;
- Texas Economic Freedom, which studies Texas and its largest cities, all of which rank highly in economic freedom and outperform the rest of the nation on key metrics.

These three research agendas support the O’Neil Center’s fourth initiative: Student Enrichment and Public Outreach. The O’Neil Center spreads the ideas of liberty and economic freedom to SMU students in classrooms and reading groups and to the broader community through public programs and the media.



*Michael Davis*



*Ryan Murphy*



*Daniel Serralde*



*Liz Chow*



*Dwight R. Lee*



*Derek Yonai*

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# Global Economic Freedom

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Global Economic Freedom addresses the O’Neil Center’s founding mission with research on why economies succeed and fail. Its centerpiece is *The Economic Freedom of the World (EFW)* report, an empirical measure that gives researchers a powerful tool to test ideas about free enterprise and its consequences. Studies find that high EFW scores correlate with higher incomes, faster economic growth, lower poverty rates, higher life expectancy and many other positive outcomes.

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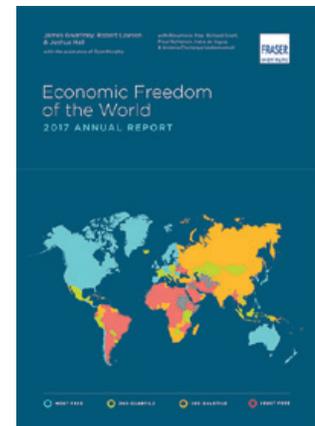
## EFW Report

Lawson has been a key researcher on the EFW index for over two decades. At the O’Neil Center, he and Murphy compile the EFW data and calculate economic freedom ratings for 159 countries.

Released in September 2017, the latest *EFW* report by Lawson and co-authors James Gwartney and Joshua Hall showed that the most economically free places in the world were Hong Kong, Singapore, New Zealand, Switzerland and Ireland.

Regarding the United States, the report found a slight uptick in its economic freedom score, pushing the country from 13th place in 2014 to 11th place in 2015. The United States ranked highly in sound money and labor market regulation. Its lowest ranking was in size of government.

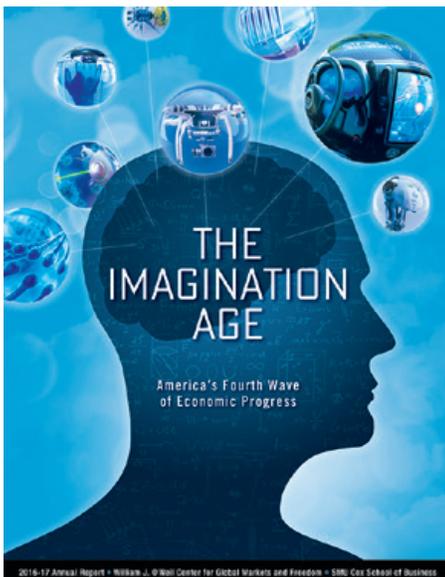
Lawson gave public lectures on the EFW index and its implications at Ball State University, University of North Carolina Wilmington, Mackenzie University in Brazil, Oklahoma State University and Samford University.



Cover of EFW, 2017

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## The Imagination Age



*The 2016-17 annual report was the eighth in a series that began in 2009. After reading the essay, Dean Matt Myers of SMU Cox wrote: Cox and Alm “urge us not to forget the past—that the arrival of new ages has always brought pain and progress.”*

The center’s Annual Report essay addressed the job losses and income inequality that challenge many Americans’ faith in capitalism. Written by Cox and Alm, “The Imagination Age: America’s Fourth Wave of Economic Progress” tied today’s angst to a fundamental transformation of the U.S. economy, brought on by the arrival of digital technologies, particularly the Internet.

The country endured previous periods of rapid economic change, the essay noted. The first came after the Civil War, when new technologies turned an agricultural economy into an industrial one. Then in the 1970s a new wave of technologies began to erode the industrial economy, ushering in the Information Age.

Today, the arrival of another new age is disrupting the foundations of the existing economy—from the skills workers need to the goods and services available to consumers. These disruptions are causing today’s dislocations and hardships, but they’re part of a capitalist economy’s orderly progression toward higher living standards.

Cox and Alm identify the economic logic of shifts from one age to the next. “At any point in history, a key scarce resource limits basic living standards,” they wrote. “Some binding constraint keeps the resource in short supply and expensive, and societies can’t rise until a breakthrough technology comes along. What was once scarce and costly becomes plentiful and cheap.”

Earlier ages ended when machine power started making food cheaper and when the microchip started making information cheaper. It’s now relatively cheap to store, process and transmit ideas. The next scarce resource is the ability to imagine what to do with a wealth of knowledge—thus the Imagination Age.

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## Academic Publications

In “Taxation in the Classical Liberal Tradition,” published in the *Review of Austrian Economics*, Lawson and J. R. Clark urged classical liberals to take more seriously problems of market failure associated with externalities and public goods. This paper was based on Lawson’s May 2017 talk at the Mont Pelerin Society meeting in Seoul.

Lawson and Murphy wrote “Economic Freedom and Growth Specification Debate: A Retrospective” for *Applied Economic Letters*. The paper takes a fresh look at a 10-year-old debate on the best way to use the EFW index in regressions.

The *Cato Journal* published “Extending the Economic Freedom of the World Index to the Cold War Era,” written by Lawson and Murphy. They take the EFW back two decades to 1950 for major countries.



In addition to his articles with Lawson, Murphy published “Aggregate Demand Shortfalls and Economic Freedom” in the *Review of Austrian Economics* (with Taylor Leland Smith). The paper found restrictive monetary policy might undermine economic freedom through the election of populists.

*Economic Affairs* published “U.S. Immigration Levels, Urban Housing

Values, and their Implications for Capital Share,” an article written by Murphy and Alex Nowrasteh.

Working with Colin O’Reilly, Murphy wrote two papers on the relationship between the discovery of economically important natural resources and economic freedom—“Exogenous Resource Shocks and Economic Freedom” in *Comparative Economic Studies* and “Do Institutions Mitigate the Risk of Natural Resource Conflicts?” in *Contemporary Economic Policy*.

Murphy and Lee joined forces to consider the implications of disenchanted voters in a *Public Choice* article titled “An Expressive Voting Model of Anger, Hatred, Harm and Shame.”

Murphy contributed “Immigration and Its Effects on Economic Freedom: An Empirical Approach” to the *Cato Journal’s* theme issue reviewing economic research on immigration and the economy. Murphy focused on how the arrival of foreigners changed institutions.



*Libertas: Segunda Epoca* published “A Call for Out-of-Sample Testing in Macroeconomics” by Murphy and Robert Gelfond, who recommend the methodology while pointing out it has very rarely included a government spending multiplier.

*The Independent Review* ran Murphy’s “The Best Cases of Actually Existing Socialism,” which looked at the more functional systems in Hungary, Israel and China and found that these countries eventually retreated from socialism by liberalizing. Murphy responded to comments from Mike Munger of Duke University in a subsequent issue of the *Review*.



Tuszynski and Murphy explored the topic of “Aging Populations and the Size of Government” in the Institute for Research in Economic and Fiscal Issues’ *Working Paper No. 201802*.

In *Public Choice*, Lee and J.R. Clark published a critique of an emerging branch of economic research, titled “Can Behavioral Economists Improve Economic Rationality?”

Lee’s “Voting with Your Ballots versus Voting with Your Feet” was the featured article on the Library of Economics and Liberty site on February 5.

Murphy summarized the recent effort to improve the EFW index in “New Changes for Economic Freedom of the World,” which appeared in the *Mustang Business Journal*, an on-line publication by SMU Cox students.

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## Presentations and Speeches

Lawson and Ben Powell, director of the Free Market Center at Texas Tech University, presented a May seminar at George Mason University’s Mercatus Center on their forthcoming book titled *Socialism Sucks: Two Economists Travel the Unfree World*.

Lawson spoke on his study of the pro-market economic reforms in the country of Georgia at Utah State University, University of North Carolina Charlotte,

Oklahoma State University, West Virginia University and Texas Tech.

At April’s Association of Private Enterprise Education (APEE) meeting in Las Vegas, Lawson presented new research on the determinants of economic freedom. At July’s annual FreedomFest, held in Las Vegas, Lawson represented the O’Neil Center as an exhibitor and served on a panel about the EFW index.

Lawson met with other scholars working

on the EFW index at the Economic Freedom Network meeting in Kiev, Ukraine. On the trip, he lectured at Tbilisi State University, Black Sea International University and Gori State University.



In May, Lee gave a series of talks at Universidad Francisco Marroquin in Guatemala City. With groups of students and professors, he discussed his research

*Continued next page*

with Murphy on “An Expressive Voting Model of Anger, Hate, Harm and Shame.” Lee also spoke on “The Moral Appeal of Government Action” and “Making the Case for the Market: Overcoming a Moral Misunderstanding.” At the graduation ceremony, the university gave Lee an honorary doctorate.

Lee also discussed the findings of “An Expressive Voting Model of Anger, Hatred, Harm and Shame” at the Public Choice Society Meeting and a faculty seminar at the University of Georgia. At the SMU Summer Economics Conference, Lee took up a provocative

question: “Are Economists Evil?”

“Can Behavioral Economists Improve Economic Rationality?” was the topic for two of Lee’s talks, one at the Southern Economic Association meeting in November and the other at the APEE conference in April. At APEE, Lee made a presentation titled “Did Nancy MacLean Read any of Buchanan’s Work?”—a discussion of the controversy started by a recent book on Nobel Prize-winning economist James Buchanan.

Murphy presented a paper titled “The State Economic Modernity Index: An Index of State Building, State Size and Scope,

and State Economic Power” at an August American Institute for Economic Research conclave in Great Barrington, Mass. In the fall, he presented the paper at George Mason University, Creighton University and the Southern Economic Association meeting.

Murphy’s visit to Creighton also included a talk to undergraduates on “Cross-Country Measures of Institutions in Academic Research.”

At the Public Choice Society annual conference in Charleston, S.C., Murphy made a presentation on “The Long Run Effects of Government Ideology on Economic Freedom.”

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## State and Metro Economic Freedom

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Since 2013, Stansel has been the primary author of the *Economic Freedom of North America (EFNA)* report, a data-driven assessment of the balance between markets and government control in each of the continent’s states and provinces. Stansel also created the first index that measures economic freedom for the nation’s 380-plus metropolitan statistical areas (MSAs).

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### EFNA Report

In December, Stansel and co-authors Jose Torra and Fred McMahon released EFNA’s 2017 report. At the top of the U.S. list—the most economically free states—were New Hampshire, Florida, Texas, South Dakota and Tennessee. At the bottom of the list, exhibiting the least amount of economic freedom, were New York, California, New Mexico, West Virginia and Hawaii.

The latest EFNA results were grist for several newspaper columns. In December, Stansel’s “New York, California Are Rock Bottom on Economic Freedom—Again” appeared in *Investor’s Business Daily*.

The next month, Stansel and Orphe Divounguy wrote “The Incredible Shrinking of Illinois: High Taxes and Low Economic Freedom Have Led to State Crisis” for *The Daily Caller*.



EFNA grew out of EFW work.

In “Americans are on the Move to Freer Pastures,” published in January in the *Washington Examiner*, Stansel and Tuszynski used moving company data to show that people are relocating to states with greater economic freedom.

In the spring semester, Stansel completed a revision of the metropolitan area economic freedom index, which uses nine variables to rank 382 local economies on government spending, taxes and labor-market restrictions.

In the updated version, Stansel used more recent data, but he also extended the measurement back in time to 1972. The new and improved U.S. Metropolitan Area Economic Freedom Index will be published as a Reason Foundation Policy Study in the fall and be available to researchers shortly thereafter.

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## Academic Publications

Stansel and Tuszynski compiled a comprehensive review of empirical research articles on state-level economic freedom, which will be published as “Sub-national Economic Freedom: A Review and Analysis of the Literature” in the *Journal of Regional Analysis and Policy*.

The two O’Neil Center authors examined the extent to which economic development incentives might lead to an uptick of failing companies in “Targeted Business Incentives and Firm Deaths,” which has been submitted to *the Review of Regional Studies*.



Economic freedom and other state-level issues were central to five of Murphy’s articles:

- “Economic Freedom of North America at State Borders” in the *Journal of Institutional Economics* used data for counties on either side of state borders to gauge the impact of economic freedom;
- Both “Beggaring Thy Neighbor at the State and Local Level” in the *Journal of Financial Economic Policy* and “Valuing the Government Spending Multiplier: Why Monetary Offset Must Be Recognized” in *Mercatus on Policy* assessed whether states

have been rebounding from recession by siphoning jobs from elsewhere rather than creating new ones;

- “A Short Empirical Note on State Misery Indexes” in the *Journal of Regional Analysis & Policy* took advantage of newly available data on state-level inflation to calculate misery indexes by state;
- “U.S. Immigration Levels, Urban Housing Values and Their Implications for Capital Share” (with Alex Nowrasteh) in *Economic Affairs* found only a few communities where increases in the foreign-born population play a role in explaining higher housing prices.



Stansel published “An Exploratory Empirical Note on the Relationship between Labor Market Freedom and the Female Labor Force Participation Rate in US Metropolitan Areas” (with Crystal Wong) in *Empirical Economics Letters*.

The research found that areas with greater labor market freedom tend to have higher labor-force participation rates among female workers, suggesting women may be disproportionately harmed by state interventions in labor markets.

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## Presentations and Speeches

For a third straight year, the O’Neil Center hosted the Economic Freedom of North America conference in June, which brought together the scholars from three countries to discuss the EFNA index and its value in economic research. Stansel made opening remarks on “Economic Freedom of North America: Overview & U.S. in Focus.”

Murphy discussed “The Legal System and Protection of Property Rights at the Subnational Level” at the Public Choice Society meeting in Charleston, S.C., in March and at the APEE annual conference in April.

At the Western Economics Association in June, Stansel and Tuszynski reported on their 2016 paper titled “Targeted State Economic Development Incentives and Entrepreneurship,” which found negative relationship with patent activity but no relationship with two other measures.



Stansel presented “Oil Rents and State Economic Policy,” based on research

with Colin O’Reilly, at a conference on Governing Natural Resources in the American West, held by the Texas Tech Free Market Institute in August. They found oil windfalls didn’t lower economic freedom.

Stansel and Tuszynski (with Alex Padilla) found no consistent relationship between economic freedom and domestic migrants as a percentage of state population. Stansel discussed the research at the Southern Economic Association meeting in November, with a talk titled “The ‘California Horse’: Do Domestic Migrants Impact State Institutions?”

Stansel discussed “Housing Prices and Economic Freedom in U.S. Metropolitan Areas,” based on work with Tim Allen, at the American Real Estate Society conference and a Florida Gulf Coast University research seminar, both in April.

Tuszynski and Stansel were awarded a research grant from SMU’s Mission Foods Texas-Mexico Center for a study titled “Institutions and Trade: An Examination

of the U.S. States and Mexico.” It found that states with higher economic freedom tend to engage in a more trade with other states. Stansel made presentations based on the research at the Public Choice Society conference in March and the Texas-Mexico Center’s annual meeting in April, held in Mexico City.



“Institutions and Trade: An Examination of the U.S. States and Mexico” was one of two presentations by Tuszynski at the APEE conference. The other was “Economic Freedom and Environmental Quality in the United States,” which found no conflict between economic freedom and environmental quality.

At the meetings of the Southern Economics Association, Public Choice Society and APEE, Stansel organized and served as chairman for five sessions of academic research related to state-level economic freedom.

# Texas Economic Freedom

The O’Neil Center developed a research interest in the Texas economy early on, focusing its first two Annual Report essays on the Lone Star State. The Texas Economic Freedom initiative, launched in 2015, expanded our efforts to understand key trends shaping the state’s future. The research involves comparing Texas and its major cities to their counterparts across the United States.

## Texas Economic Forum

Started in 2016, the Texas Economic Forum focuses on trends and issues important to the Texas economy. For a fall semester event on “The Innovation Economy,” the O’Neil Center partnered for the second straight year with SMU Cox’s Maguire Energy Institute and Folsom Institute for Real Estate.

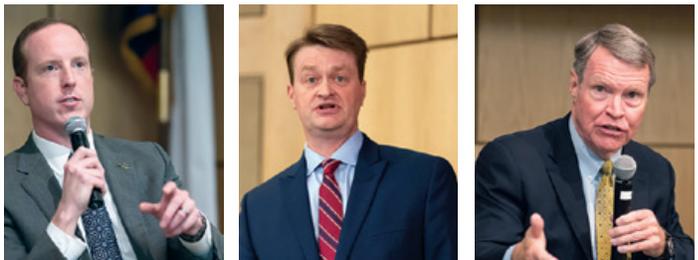
Cox put a Texas spin on “The Imagination Age,” identifying key technologies remaking the economy and assessing Texas’ assets in taking advantage of them, particularly its high degree of economic freedom. Maguire and Folsom collaborated on a panel of energy and real estate entrepreneurs, who discussed their experience starting and growing companies in DFW and Texas.



For the spring Texas Economic Forum, Cox joined three invited speakers to discuss “Trump and the Texas Economy”—an analysis of how the president’s policies might impact the state.

Vance Ginn of the Austin-based Texas Public Policy Foundation portrayed the Texas economy as booming, but he warned of the state’s vulnerability to protectionist policies. Doug McCullough of Dallas’ Lone Star Policy Institute saw benefits for the state in Trump’s tax cuts, particularly the sharply lower corporate rates.

Cox warned that tightening immigration laws could lead to labor shortages in Texas, with construction especially vulnerable. Merrill Matthews of Plano’s Institute for Policy Innovation said that deregulation could benefit the Texas energy industry.



At the Texas Economic Forum, Cox (top), Ginn, McCullough and Matthews

## Writing About Texas’ Economy

Cox and Alm continued to write *D CEO* magazine columns on the Texas and DFW economies. Their first article appeared in October 2010—so the relationship has lasted almost eight years.

The series’ titles and topics for academic year 2017-18 were as follows:

- “Lagging Behind” (left) presented data showing that Dallas proper hasn’t kept pace with its suburbs in the growth of median family income.
- “Taking a Closer Look at Dallas’ Housing

Prices” found the largest increases in DFW home values in North Dallas and the northern suburbs.

- Just after Internet retailing giant Amazon.com launched its search for a second U.S. headquarters, “Dallas and the Innovation Economy” made the case for DFW being highly competitive in innovation and entrepreneurship.
- “Foreign-Born Workers Important to Building Texas” argued that Texas faces labor shortages and needs more immigrants not fewer.



• “Dallas’ Place in the Texas Triangle” put a spotlight on a dynamic region roughly bordered by DFW, Houston and San Antonio, which is a tenth of the state’s land area but accounts for about three-quarters of the state economy.



O’Neil Center research on state and local economies has been featured in *The Texas Economy*, the center’s online newsletter. The quarterly published the following articles in academic year 2017-18:

• In “Listening for the Texas Twang in the Innovation Economy,” Alm summarized the proceedings of the fall Texas Economic Forum on innovation and entrepreneurship in the DFW area.

• Alm continued his study of the development of Texas’ economy in “Entrepreneurs on Horseback,” which chronicled the rise of the cattle industry after the end of the Civil War.

• In “Foreign-Born Workers in the Texas Economy,” Cox and Alm presented data showing that Texas ranked sixth among states in employing immigrants. Foreign-born workers are particularly

important in construction, an industry vital to a state with an expanding population.

• In “Trump and the Texas Economy,” Alm summarized the Texas Economic Forum presentations on how the president’s policies on trade, taxes, immigration and energy are likely to impact the state.



Stansel partnered with Vance Ginn on two op-ed articles discussing economic freedom in the state—on September 6, “Six Missed Opportunities in Special Session That Could Have Aided Economic Prosperity” in the *Fort Worth Star-Telegram*; on January 5, “Texas Ranks Near the Top (Again) for Economic Freedom” in the *Dallas Morning News*.

After Hurricane Harvey hit the Texas Gulf Coast, Davis wrote “Want to Help Storm Victims? Cash is King,” a *Dallas Morning News* op-ed contending that money would allow the battered region to decide its recovery priorities for itself.

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## Student Enrichment and Public Outreach

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Engaging with SMU students provides an opportunity to shape the next generation of American leaders, workers and voters. O’Neil Center professors teach classes and offer programs that introduce the ideas of liberty and economic freedom. Our commitment to education extends to the general public. The center sponsors speakers at SMU, makes presentations to non-academic audiences and responds to media requests.

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### Teaching Free Enterprise

The donor-supported program began in 2015 and offers workshops and curricular materials for high school teachers, with the goal of helping them meet Texas’ mandate to provide economics instruction with an emphasis on the free-enterprise system and its benefits.

Under Serralde’s direction, Teaching Free Enterprise moved forward during 2017-18 with 18 workshops and a total attendance of 1,072 teachers. These teachers returned to their jobs and taught classes with an estimated 162,000 students, suggesting a large impact for the program.

O’Neil Center staff members continued to play a big role in Teaching Free Enterprise. The first four curriculum units came from Lawson (“Trade” and “Economic Freedom of the World”) and Cox (“Paradox of Progress” and “Time Well Spent”).

Stansel and Tuszynski wrote the lesson plan for “Taxation and Public Finance.” Before leaving, Yonai contributed “Morality and Markets” and “Culture and Trade.” Tuszynski wrote two of the six curriculum units added in the 2017-18 academic year—“Public Choice 1: Governments and Markets” and “Public Choice 2: The Political Process.”



Texas Tech’s Adam Martin leads a session on economic development.

Lawson, Cox, Stansel, Tuszynski and Alm lectured at events in 2017-18. Toward the end of the spring semester, Grand Prairie economics teacher Ray Hughel came on board as a full-time contractor to assist Serralde in running the TFE program.

Teaching Free Enterprise continued to expand its reach beyond Texas. Traveling to Mexico City, Lawson and Serralde attended the graduation ceremony for high school students who completed the TFE program with our partner, Caminos del la Libertad.



Graduates of the TFE program at Caminos del la Libertad high school in Mexico City.

## Flourishing & A Free Society Forum

Each year, the O’Neil Center invites prominent speakers to the SMU campus to share their perspectives on liberty and economic freedom. In addition to Walter Williams, the 2017-18 roster of speakers included Deirdre McCloskey, now at the University of Illinois-Chicago.

She’s the author of an expansive trilogy on the origins of capitalism—*Bourgeois Virtues*, *Bourgeois Dignity* and *Bourgeois Equality*. In her O’Neil Center lecture, attended by more than 300 students and members of the business community, McCloskey discussed how the ideas of the oft-maligned bourgeoisie led the world out of poverty through the rise of capitalism.

Scott Sumner, a monetary policy expert at George Mason University, presented an

analysis of the Federal Reserve’s missteps during the Great Recession of 2008-09, contending that the central bank would have performed better if it had paid more attention to the ups and downs of nominal GDP.

William J. Luther, a Kenyon College economics professor, provided a timely lecture on bitcoin, which had soared in value for several years before sharp declines in the months before the forum. According to Luther, bitcoin is better justified as a store of value rather than medium of exchange.

David Henderson, an economist at Stanford University’s Hoover Institution, discussed how sound economic arguments contributed to ending the military draft and replacing it with an all-volunteer armed forces.



Deirdre McCloskey

## O’Neil Center Reading Groups

The O’Neil Center launched its first free market reading group in 2014. During 2017-18, three groups, each meeting once a week, held fall and spring sessions. Stansel led the McLane Teammates Scholars and Armentrout Scholars reading groups, while Murphy guided an advanced reading group for students who wanted to build on their participation in a previous O’Neil Center reading group.

The six reading groups included a diverse

mix of 72 SMU students, including majors in economics, finance, public policy, philosophy, statistics, history, political science, math, international studies, health and society, marketing, anthropology, religion, English and Spanish. In both the fall and spring semesters, SMU hosted a reading group summit with students from similar programs at Texas Tech, Baylor and the University of Central Arkansas.

Stansel’s two fall reading groups focused

on “Economics and Social Issues: Markets and the Marginalized,” and participants examined how disadvantaged groups fare in wealthy societies, reading works by such scholars as Claudia Goldin, Walter Williams and Thomas Leonard.

The students explored such questions as: How do markets and government help or hinder disadvantaged groups? What role has race played in the history of economic thought? What are the effects of

*Continued next page*

discrimination in labor markets? What are the consequences of mass incarceration? Why do women typically earn less than men? What explains persistent poverty among Native Americans?

The summit with Tech, Baylor and Central Arkansas students was scheduled to give students the opportunity to attend the Walter Williams lecture and participate in workshops with the economist the next day.

In the spring, Stansel led his two reading groups on “Freedom and Human Flourishing: Poverty, Prosperity and Quality of Life around the World.” Course materials included works from scholars such as George Ayittey, Daron Acemoglu, Bill Easterly and Deirdre McCloskey that examine the role of personal freedom, markets and culture in promoting human flourishing.

The students explored such questions as: Why are some nations prosperous while other remain impoverished? How should we measure socio-economic progress? What role does foreign aid play in helping the poor? How has the quality of life changed over time around the



Walter Williams answers questions at a reading group event.

world? How do government policies and markets affect our well-being?

The summit featured a keynote lecture by George Mason University professor Donald Boudreaux on “The Myth of Middle-Class Stagnation” and a workshop with the economist later in the day.

Murphy’s fall reading group, titled “Rational Choice in Law and Politics,” offered a crash course in Law & Economics and Public Choice. The two

primary readings were *Law’s Order* by David Friedman and *Government Failure* by Gordon Tullock, Arthur Seldon and Gordon L. Brady.

The theme for the spring was “Numeracy,” which focused on interpreting data in ways not usually covered in standard academic coursework. The two primary readings were *The Signal and the Noise* by Nate Silver and *Superforecasting* by Philip Tetlock and Dan Gardner.

## Teaching SMU Cox Students

In the fall semester, Lawson taught three sections of Managerial Economics to MBA and MS students. He was back in the classroom in the spring with two sections of Microeconomics for EMBA’s,

Cox taught Managerial Economics to PMBA’s and MS students. His Markets and Freedom summer course gave non-business majors important lessons on America’s free-enterprise system.

Davis taught International Finance and Corporate Finance for both undergraduate and graduate students, Macroeconomics and Decision-Making under Uncertainty for graduate students, and he was the faculty adviser on student trips to China (Hong Kong and Shenzhen) South America (Colombia and Peru) and Europe (England, Czech Republic and Germany).

After stepping down as dean, Niemi



Davis at work in the classroom

continued to teach his Evolution of American Capitalism. A shortened version formed the basis for the Certificate in American Capitalism, offered through the SMU Cox continuing education program.

During the 2018 May Term, Tuszynski taught 21 juniors and seniors in Markets and Freedom, a course that examined the interaction between free markets and broader measures of economic prosperity.

## Working with Standout Students

In April, Tuszynski led a group of 16 undergraduate students and faculty from five local universities in a daylong discussion of the works of Frederic Bastiat and F.A. Hayek. The sessions were moderated by Bradley Hobbs (Clemson University) and Stephen Gohmann (University of Louisville).

Luke Yeom was Murphy's research assistant the fall semester. The two co-authored "The Long-Run Impact of Agricultural Diversity on Economic Freedom," which appeared in the *Journal of Regional Analysis & Policy*.

Eric Li was Murphy's research assistant in the spring semester. They will continue their collaboration this summer on a working paper begun in the spring semester.

During the spring, Murphy worked with O'Neil Center research assistant Nick Whitaker on an independent study project focused on rationality and economic methodology. The tutorial involved reading parts of *Predictably Rational* by Richard McKenzie and *Beyond Positivism* by Bruce Caldwell.



Tuszynski and Stansel worked together to advise Whitaker on various data projects, including a state-to-state mapping of vehicle miles traveled for a working paper titled "Institutions, Trade, and Economic Prosperity: An Examination of the U.S. and Mexican States."

Tuszynski and Stansel teamed up to advise David Shirzad, an SMU Tower Center scholar, on a project titled "Economic Development Incentives in Texas: Do They Actually Bring the Promised Benefits?"

The O'Neil Center funded Student Research Fellowships. Seth McKelvey (English Ph.D. student), Kyle Carpenter (History Ph.D. student), Eric Li (SMU Cox undergraduate), and Luke Yeom (SMU Cox undergraduate) received research funding from the O'Neil Center in 2017-18. Overall, this program is considerably under budget as it has been more difficult than expected to recruit students for research fellowships.

## Radio, Television, Print

At the end of the 2017-18 academic year, SMU Cox recognized Stansel, Cox and Davis with Media Appreciation Awards, this year based on the single story with the greatest potential national exposure.

Stansel ranked second among SMU faculty with work cited in two *Forbes* articles—"Competition Among Government Is Important for Economic Freedom" and "Florida Remains One of the Most Economically Free States." Cox scored big with Yahoo! Finance Television, where he was featured in "Dallas Former Fed Chief Economist: The Fed Has Been Behind the Curve Over and Over Again." Davis received plaudits for a contribution to "Proposed Gas Tax Increase Could Harm Americans," an article in the *Wall Street Journal's* "The Street."

Davis gave dozens of interviews to reporters seeking commentary on economic trends in Texas. For

example, his insights were in "Labor Shortage Straps Eateries" in the *Dallas Morning News*, "The Trouble with Tariffs" in the *San Antonio Express* and "As Trump Tweets on Mexico, GM Expands in Arlington in the *Fort Worth Star-Telegram*.

In addition to Yahoo! Finance, Cox gave interviews to Reuters and NPR-affiliate KERA radio in Dallas. *The Federalist* cited his expertise in "Evidence Says Income Inequality is Not a Problem."



Stansel appeared as a guest commentator on 49 radio shows, including 22 times on the Ed Dean Show, the No. 1 statewide radio program in Florida. Stansel's research was cited in the print media at least 16 times, including the *Orange County Register* and three articles in *Forbes*.

PJ Media covered Murphy's provocative working paper explaining



Stansel on the air

how the fad of American teens eating Tide pods just might be rational.

While in Guatemala in May, Lee gave an interview on free markets and liberty for Universidad Francisco Marroquin's website and YouTube channel.

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## Workshop Series

The O’Neil Center Workshop Series brings professors from other institutions to SMU Cox for seminars focusing on research in progress. Building these relationships with other academics is an important source of professional development for the center’s scholars.

Some of the 2017-18 academic year’s eight seminars jibed with the O’Neil Center’s mission of studying economic

freedom—most notably, the development of a state economic freedom index for Brazil (Vladimir Maciel, Mackenzie University). In addition to her public lecture, Deirdre McCloskey presented a seminar on aspects of her current work.

Other topics addressed in Workshop Series included the role of cultural values in economic reforms (Scott Sumner, George Mason University); peer comparison and

CEO pay (Korok Ray, Texas A&M); the regulatory state (Art Carden, Samford University); links between immigration and corruption (Ben Powell, Texas Tech); populism in Latin America (Nicolas Cachanosky, Metro State University); the origin of institutions (Boris Nikolaev, Baylor University); and measuring human trafficking (Greg DeAngelo, West Virginia University).

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## Speaking and Writing

Cox delivered the optimistic message of capitalism as a driver of American progress in 14 speeches. A sampling of his titles: “Good News: Why America Is Better Off Than You Think;” “Economic Outlook for the U.S.: A Tale of Two Economies;” “Age Shift: An Optimistic Perspective on America Today and Tomorrow;” and “The Imagination Age: Fourth Wave of American Economic Progress.”

Most of Cox’s speeches were to business groups and investors, such as the National Association of Manufacturers, KPMG, the Association of Private Investment

Consultants, United Capital and Jackson National Life Insurance.

Stansel’s August article in *Investor’s Business Daily*, headlined “It’s Time To Reduce Spending — Unfortunately, GOP Budgets Don’t Actually Do So,” took issue with alarmist reports about the Republicans’ supposedly draconian spending cuts.

For *Regulation* magazine, Davis wrote “Regulating Banks by Regulating Capital,” which argued that it would be better to require banks to maintain ample capital to pay off creditors rather than attempting to

police foolish decisions.

Before leaving the O’Neil Center, Yonai delivered several speeches: “Rational Irrationality Operationalized: Incivility, the New Normal” at June’s Western Economic Association meeting in San Diego; “Markets and Morality” at the American Teaching Initiative in July; and “The Need for Free Enterprise in Business Education” at Wheeling (W.Va.) Jesuit University in October. In September, he moderated a session on “The Rule of Law” for the National Review Regional Fellows Program.



Murphy’s wide-ranging interests and economic research led to the following publications, which did not expressly focus on issues of national or state-level economic freedom.

- In *The Independent Review*, “The Diseconomies of Do-It-Yourself” argued that high transaction costs rather than

pocketbook savings better explains the popularity of home improvement projects.

- A *Journal of Private Enterprise* article titled “The Perils of Buying Social Capital Locally” contends that feel-good campaigns urging consumers to “Buy Local” results in an overinvestment in social capital.



Lee was a regular book reviewer for *Regulation* magazine. He had the following contributions during the 2017-18 academic year.

- “Diminishing the Case Against Empathy,” a review of *The Case Against Empathy* by Paul Bloom.

- “Pride in Staying Out of Jail,” a review of *Read my Lips: Why Americans are Proud to Pay Taxes* by Vanessa Williamson.

- “Loving the Poor, but Loving Political Privileges More,” a review of *Dream Hoarders: How the American Upper Middle Class is Leaving Everyone*

- “Sorry, Europe, America is Already Great,” published in May by *Arc Digital*, pointed to several things Europhiles claim are evidence of European superiority are actually evidence of American superiority. A review of the book *Choice* by Richard Harper, Dave Randall and Wes Sharrock for *Contemporary Sociology*.

*Else in the Dust* by Richard Reeves.

- “Becoming More Sympathetic with Black Lives Matter,” a review of *Locking up Our Own* by James Forman Jr.

- “Imagine What Future Generations Will Think of Us,” a review of *WTF: An Economic Tour of the Weird* by Peter T. Leeson.

# THE O'NEIL CENTER **10** 2008-2018 *years*

After its founding in 2008, the O'Neil Center made its public debut with a conference on the theme "What Do Businesses Need to Succeed in Today's Competitive Global Economy."

The inaugural conference's speakers included Dallas Fed President Richard Fisher, O'Neil Center donor William J. O'Neil and Texas Instruments CEO Richard Templeton. Another speaker on the

program: Bob Lawson, who would join the O'Neil Center in 2011 and become its director in 2014.

The conference was the start of one of the O'Neil Center's signature contributions to SMU's intellectual climate—inviting distinguished scholars and business leaders to public forums.

Here are some of the O'Neil Center speakers from the past 10 years:



2009: Thomas Sowell  
Hoover Institution



2011: John Mackey  
CEO, Whole Foods



2012: James Tooley  
*The Beautiful Tree*



2015: George Will  
Political Commentator



2015: Phil Gramm  
Former U.S. Senator



2016: Matt Ridley  
*The Rational Optimist*

## Other Voices ... (affiliations at time of SMU speeches)

**2009**  
Thomas J. Falk  
CEO, Kimberly-Clark

**2010**  
John Allison  
Ex-CEO, BB&T Bank  
Stephen Moore  
Wall Street Journal

**2011**  
John Stossel  
Fox News

Warren Stephens  
Stephens Inc.  
Michael Tanner  
Cato Institute  
**2012**  
Russ Roberts  
*EconTalk* podcaster  
Ben Powell  
Free Market Institute  
Texas Tech University

**2013**  
Bryan Caplan  
George Mason  
University  
Arthur Brooks  
American Enterprise  
Institute

**2014**  
David Boaz  
Cato Institute  
Michael Munger  
Duke University

**2015**  
Arthur Laffer  
Laffer Associates  
James K. Galbraith  
University of Texas

**2016**  
Steve Forbes  
*Forbes* magazine  
Edward Glaeser  
Harvard University  
Sylvia Nasar  
*A Beautiful Mind*



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