Comparative Models of the Market Economy

Economic problems

<table>
<thead>
<tr>
<th>Factors generating economic problems</th>
<th>Economic questions</th>
<th>Economic problems</th>
<th>Market functions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Scarcity of resources</td>
<td>What and how much to produce</td>
<td>Efficiency in allocation</td>
<td>Allocation of scarce resources</td>
</tr>
<tr>
<td>Technological progress</td>
<td>How to produce</td>
<td>Efficiency in motivation</td>
<td>Motivation for efficiency (incentives)</td>
</tr>
<tr>
<td>Changes in tastes and preferences</td>
<td>For whom to produce</td>
<td>Efficiency in distribution</td>
<td>Distribution of goods and services</td>
</tr>
</tbody>
</table>

Models of the Market Economy

- Market failure and social welfare function
- Different priorities in the social welfare function
- Three models:
  - The Guided Market Economy (Japan, Korea, France, Italy, Greece, Spain, Portugal, etc.)
  - The Modified Market Economy (the U.S., the U.K., Ireland, New Zealand)
  - The Social Market Economy (Germany, Denmark, Sweden, Norway, Finland, Estonia)

The Guided Market Economy

- Priority on resource allocation
- Direct government participation in resource allocation and industrial restructuring
- Long-term focus

The Guided Market Economy

Industrial Policy

- a set of instruments and techniques designed to promote economic growth on the basis of direct government participation in resource allocation and industrial restructuring
- identification of key industries and promotion of their better access to resources and faster growth
Business systems

- distinctive configurations of firms and markets, which have been established, in a particular environment as the dominant ways of structuring economic activities.
- Characteristics of the business system

The nature of economic agents

Work co-ordination and control

Market organization

The Guided Market Economy

The Business System
- A dual business structure
- Domination of big businesses
- Strong vertical and horizontal integration
- Low rate of change of activities
- Widespread subcontracting
- Small share of the medium-size firms

The keiretsu system

- Interlocking directorates
- Stock cross ownership
- Financial support (provision of loans at favorable rates)
- A built-in stable market for each other’s products
- Transfer of labor force
- Cooperation in the international expansion

The Modified Market Economy

Capital markets
- The banking system serves as a major institution of capital allocation
- The "main bank":
  - Provides debt financing
  - Raises capital for the industrial firms
  - Monitors
  - Guarantees firms’ debt
  - Participates in executives turnover and shifts in corporate strategy
The Modified Market Economy

- Motivation for efficiency
- Main goals:
  - to motivate private decision makers for efficient use of resources
  - to trigger higher living standards
  - to moderate inequality
  - to contribute to social integration
  - to guarantee efficient administration

The Modified Market Economy

- Core institution – capital markets
- The stock exchange:
  - High capital mobility
  - High liquidity of funds
  - A wide set of financial institutions

The Modified Market Economy

- Welfare goals:
  - Free choice in consumption
  - Free choice in occupation and education
  - Greater purchasing power
  - Widespread system of consumer credit
  - Social support for the poor
  - Equal opportunities to everyone
  - High capital diffusion

The Business System

- Short – term focus
- Mobile labor
- Easy hiring and firing
- High specialization of tasks, roles and skills
- High market contestability
- Strong antitrust attitude
The Social Market Economy

- Priority on equity, social equality and full employment
- Major features:
  - Strong support of workable competition
  - Promotion of asset formation among lower income groups
  - Direct transfer payments
  - Codetermination and regulation of the labor market
  - Strong role of associations
  - Extensive role played by local governments
  - Social and welfare programs for everyone
  - Faster increase in salaries than in profits
  - Restrictive monetary policies

The Business System

- Prevailing medium-size firms
- Strong competition
- High owner involvement in control
- Codetermination in the big firms
- Strong associations
- Powerful cooperatives
- Dependence on the financial decisions made by the banking sector

The Social Market Economy

Capital markets

- The banking system serves as a major institution of capital allocation
- Excessive integration of the banking institutions with the industrial enterprises in:
  - Ownership
  - Decision-making