

## Research on the Market Economy Model

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**Abstract**—In order to promote China's market economy reform, it's necessary to study existing market models. This paper researched on three current typical market economy models, and mainly used normative analysis approach and comparative analysis method. Through compare three different economy models, this paper found two differences may lead to the diversity of model; however, they still have three similarities in different model, and the paper concludes that there are some basic rules must be obeyed in market economy. In the end, this paper puts forward some advices for China, so that central government can play positive role in boost market reform.

**Keywords**- market economy model; free market economy model; social market economy model; government- dominant market economy model

### I. INTRODUCTION

Throughout history, every society has faced the fundamental economic problem of deciding what to produce and for whom, in limited resources. While market economies based on private enterprise, surpass command economies directed by a centralized government, for its flexibility and practically mechanism, which can auto-allocated the limited resources efficiently. According to different criterion, there are different market models. China is still in the primary stage of market economy, the market development in China is immature. Therefore, the study of different kinds of market economy models can help us to improve our market economy construction.

### II. TYPICAL MARKET ECONOMY MODEL

According to the functions of market and government in the economic development, there are three typical market economy models that are acknowledged presently: Free market economy model, social market economy model and government-dominant market model.

#### A. Free Market Economy Model (FMEM)

American is a typical country which practice free market economy model. This kind of model originated in Britain. Under the influence of Adam Smith, individual freedom is characteristic of free market economy model: freedom as a consumer to choose among competing products and services; freedom as a producer to start or expand a business and share its risks and rewards; freedom as a worker to choose a job or career, join a labor union, or change employers. In a word, anything can be determined by independent market

individuals, and the control of government will be useless. Based on private ownership, this model emphasizes the right of free choice of individual, and encourages people to pursue economic interest and welfare. In this model, through the use of market mechanism, price mechanism and competition mechanism, the target of free market economy model is promoting the development of economy.

In the model of free market economy, enterprises are the most important market participants; they can manage and use their own production factors such as capital and human resource freely, for they have independent property right and decision-making power, however, they also bear potential costs and risks. Single consumer's demand may hardly affect the price of goods, but he can use his money to buy anything he wants, however, a large number of consumers have ability to decide which products are popular, and which are out of style. The problems of market economy can be solved by market, the government, as the servant of free market economy, should not get involved directly. The regulation of monopoly, the protection of competition, the creation of equal competitive environment, and the provision of efficient public service are the primary missions of government in market economy.

Through competitive system, price mechanism, and risk mechanism, economy runs smoothly. The relationship between consumer and producer is reflected through the supply and demand, which also determines the variation of price. Once some goods supply exceeds demand, the price will go up. Consumers will reduce purchases, while producers will increase production. The higher prices for goods give every consumer and producer incentives to respond this way, because they are allowed to reap the benefits of their own decisions, while also bearing the associated costs and risks. Competition between the sellers is growing, everyone wants to sell his goods as soon as possible to earn more money, and this factor has potential strength to reduce the price. Big sellers may develop to monopolists, who can influence the market, manipulate the price and control the supply, and they could earn more profit than other small sellers, even to push them out of the market. This monopoly will destroy the competition, so the government should play important role in limiting monopoly and protecting competition. Monopoly was limited by laws which are enacted by governments. In reality, governments need to obey the laws in its behavior of economic intervention, and the enterprises also need to stay on the right side of the laws in its behavior of decisions-making.

Market system is the main adjusting means in economic operation, and governments intervene only in minimum range and special industry. That is to say, free market model is the economic model that marked by free competition, in this model, market plays very important role in economic development, and governments only intervene in the economic development appropriately and limitedly

#### *B. Social Market Economy Model (SMEM)*

Western and northern Europe is famous for their high standard of living and complete welfare system. Germany is carrying out social market economy model, this model is different from FMEM in which government only in charge of create fair environment; and it is also different from the planned economy model (PEM) in which government control all economic affairs. On the one hand, this model has the advantages of flexibility and high efficiency by means of market mechanism; on the other hand, it overcomes the disadvantage of polarization between the rich and the poor with the help of government regulation.

Under the model of social market economy, government plays an increasingly role. Both private ownership and state ownership play important role in the economy, the former is the base of economy, and the latter bear some social duty. In the range of market system, no matter which kind of ownership, everyone should observe the rule of market law; in the range of regulate and control government redistribute social fortune by means of fiscal and monetary policy. Besides go after profit, state-owned enterprises should undertake social responsibility. When the conflict between social target and business goal appears, government could offer financial subsidies to them. In the social market economy theory, social welfare can fix market unfair distribution which is caused by market failure. Therefore, in order to increase efficiency and promote fair, we should use market mechanism in the first distribute and control system in the redistribute. Make full use of advantage of market and command mechanism to promote the economic development and the social progress.

In a word, SMEM is such a model that private ownership is main body, and individual freedom and market competition are emphasized in this model. This model claims that macro-regulation and government intervention are very important in eliminating market defects, and it also stresses on the implement of extensive social security system to ensure the whole economic and social fairness and efficiency.

#### *C. Government-dominant Market Economy Model (GMEM)*

East Asian countries such as Japan and Korea are use government-dominant market economy model, in which government dominate the economic development by draw up kinds of plans and even control some price. However, GMEM is different from planned economy, because it still belongs to market-oriented economy instead of plan-oriented economy in nature.

In this model, private ownership is still the base of economy, but government can dominate the development direction of economy. Government has its own target such as

national security and social stability or keep high employment rate and restrain inflation. Monopolies have close link with government, competition is constrained in some industry. The tasks of government are not only to provide public services and keep competition environment, but also include guide the direction of economic development and intervene the price. The role of government in the development of economy is becoming more and more important. GMEM is different from FMEM and SMEM, this model puts more emphasis on demand management. Besides the using of money government policy and monetary policy on demand management outside, GMEM also pays special attention on supply management, and the role of country's economic planning and industrial policies.

As the main part of market, on the one hand, enterprises make their own decisions by analyzing market information; on the other hand, under the government's influence, enterprises should also cooperate with the government, and respect the government's decision to achieve the economic goals and social goals. It's necessary to undertake their risk at the basis of independent and free running, so it can make the enterprise brave and prudent.

### III. COMPARATIVE STUDY IN THREE MODELS

#### *A. Difference*

Despite those apparent similarities, if we compare such market economies between those of North America, Western Europe, and Japan, the processes used to determine what products to make, how to make them, what prices to charge for them, and who will consume them are different. Due to the factors in economic conditions, political traditions and cultural backgrounds, different market economy models have different traits in market participant, market mechanism, and market rules.

##### *1) Ideologies of economic develop*

Due to the factors of traditional custom and culture background, the three different models have different economic ideology. FMEM stresses on free competition, so the economy is always in freedom surroundings, and the whole social also relies on fundamental principle of individual freedom; SMEM stresses on equality, which regard accordance of social progress and economy development as important, this model believes that the completely welfare system can overcome the disadvantages of market; GMEM stresses on the administration guidance, this model can form powerful strength to produce the best possible results, however, it may cause enormous waste when mistakes occurred.

##### *2) Government's function*

As important participant, government plays different role in different models. In FMEM, government's main responsibility is maintaining favorable economic environment to stimulate efficiency; in SMEM, government has more duty on manage the social welfare; and in GMEM, besides two duties above-mentioned, government also regulates some industries development and intervenes in some products' price directly. The table I shows government's function in different models.

TABLE I. GOVERNMENT'S FUNCTION IN DIFFERENT MODEL

	Improve market environment	Manage social welfare	Government Regulation and control	Government Command and plan
FMEM	√	×	×	×
SMEM	√	√	×	×
GMEM	√	√	√	×
PEM	√	√	√	√

(PEM=planned economy model)

### B. Similarities

All market economy countries have similarities, such as private ownership, competition mechanism, freedom of market participant. However, the following three important parts show the similarities in all developed market economy models.

#### 1) Market can promote the rational allocation of resources

The three market economy models are based on market regulation primarily. Market play important role in optimizing production elements and allocating economic resources rationally, and different participants of market can be encouraged by market mechanism. Another key point about market economies is that the prices of products for sell aren't set by a government planning committee. Instead, every seller is free to raise or lower prices according to the changing of market conditions.

#### 2) Government plays a role in economic development

Market economies provide no magic solutions, however, and government plays a critical role in helping correct problems that can't be fully solved by a system of private markets. The purpose is to offset and solve problems due to market failure, such as externalities problems and the increasing gap between the rich and the poor. Moreover, market economies are by no means immune to pressing public policy issues in today's global economy—issues, such as inflation, unemployment, and barriers to international trade.

#### 3) Market participants should obey market rules and protect legal rights

Market economy has some basic rules are should be obeyed: exchange of equal values rule; fair competition rule; and survival of the fittest rule. All the market systems reflect the three rules: price, competition, and risk system. Only everyone obey these rules and systems, market could display its advantages such as efficient and promote innovation. Governments in market economies must establish and protect the right of private property and the economic gains derived from the use of that property. Without such assurances, few people are going to risk their time and money in enterprises whose rewards may possibly go to the state or some other group.

## IV. CONCLUSION

China is carrying on the market economy reform now and had acquired a successful achievement. However, due to

the market economy is from planned economy system change over, some problems appear in China. In the current legal incomplete condition, illegal phenomena are common, such as administrative monopoly and local protectionism, which against the basic principles of market economy. Business fraud and insufficient investment in public goods also restrict the normal development of the market. Market operation is not standard, and the market economy still needs further perfection in China. The comparative study of market economy model can help us understand the essence of market system.

Firstly, it's necessary to combine market with government, comprehensive use of advantages of both of them, establish sound market system and all-sided social security system, and boost economic growth while ensuring social equity and justice.

Secondly, the excessive dependence on developed countries and hasting in policies should be avoided in economic development. Practice has proved that the excessive dependence on developed countries will lead to industrial structure adjustment constrained by developed countries, and the hasting in policies may cause the ignoring of the quality of economic development.

Thirdly, in an excellent economic model, dynamic is an important characteristics, throughout the world, along with the economic development, no country's market economic model is invariable. Because of the different historical background, cultural, political and economic situation in different countries, every country in the world would choose the market economic model according to the country's actual circumstances.

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