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**THE DIFFERENCE IN ECONOMIC SYSTEMS IN  
CAPITALIST AND COMMUNIST COUNTRIES**

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**ABSTRACT**

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<p>The paper's aim is to help enterprises receive an in-depth understand about the nature of politics that effect on the whole world economy to discover a successful path to a sustainable business. In addition, foreign enterprises also take a careful look about capital investment in different politics in different countries to avoid bad debt, especially in China and United State. An economic system consists of the institutions and the method by which resources are allocated and products and services are distributed. Economic systems differ primarily in who owns the factors of production, how the allocation of resources is directed and the method used to direct economic activity. The primary distinction between the different systems is the degree to which the government participates in the economy.</p> <p>This paper also examines the pros and cons of each system, as it differ greatly from one another. It focuses on an imperative features in explaining the dimensions of the perceptual process and outlines the assessment in which reader can better understand how each economic system run as well as their advantages and disadvantage.</p>		

<p><b>Key words</b> Capitalism, Communism, Economy System, Free Market, Enterprise, Government's Intervention</p>
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## ABSTRACT

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## 1 INTRODUCTION

In February 14, 2011, Japanese government has officially confirmed that the total economic output of China has surpassed Japan in 2010 (Japan's GDP is \$5474 billion, while China reached more than \$5878 billion). Thus, China has officially become the second economy in the world, behind only the United States. The strength of China's economy is seen through many factors such as world leader in export capacity and foreign currency as well as the creditors of the economy's superpower-US. However, China is currently a communist country with a weak social welfare component administration by the capitalist countries as United State. (The Guardian, 2011)

From the miniature comparisons, it can be seen that the world's economic systems have evolved as different countries have placed different emphasis on different goals and priorities in their efforts to answer the Three Key Economic Question: What to produce, How to produce, and for whom to produce. Each economy has its strengths and weaknesses, its sub-economies and tendencies, and, of course, a trouble history. It is important to understand how different parts of the world function economically, as the economy is one of the strongest forces when it comes to balancing political power, instigating war and delivering a high (or low) quality of life to the people it serves. (Gemma, 2014)

In comparative economic systems, these economic systems are usually defined within determinate political boundaries. Thus, some would speak about a Chinese economic system as being a complex conglomeration and interaction of economic systems together with the private property right, freedom of choice and competition of US's government. Nevertheless, bounding economic systems in this way provides a way of discussing how such systems are made possible and changed by the specific effects of politico-institutional, cultural, and environmental differences.

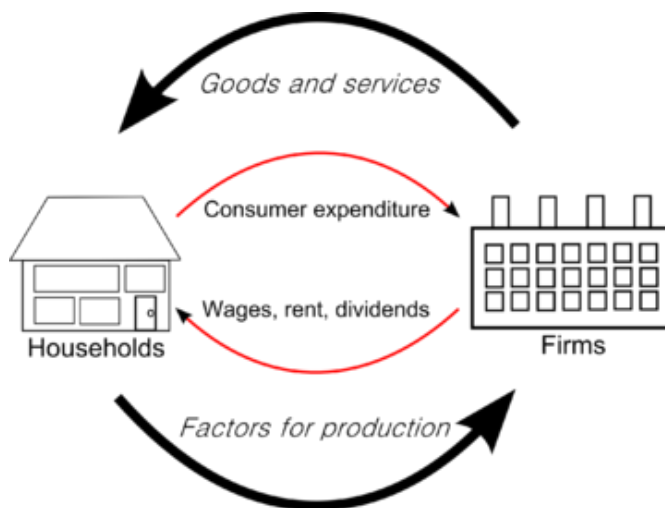
This thesis combines psychological theories and typical examples to bring together the main ideas of the different economic systems as well as a case study. Each system is examined in turn and give ample assessment to clarify the differences. Besides, the case

study covers an imperative feature in explaining the dimensions of the perceptual process and the effect of whole economy.

History has demonstrated that communism and socialism retard the growth of economies, because there is no competition between businesses, and the people who manage such businesses are often political appointees, chose more for their social connections them for their understanding of the businesses that they manage. On the other hand, capitalism works best because it promotes competition so that only the most efficient businesses survive. Survival requires that the business owners are knowledgeable about their business and can manage it effectively, that they can minimize costs to produce their product or service, and that they know what people want. But it does have serious shortcoming. Thus, the aim of the thesis is to outline the core elements of each economic system in order to better understand this interdisciplinary subject as well as attempt to provide an insight into the ways the government participates in the economy, and more than that will guide the development of future economies, fine tuning them by promoting what works and eliminating what does not work. (Spaulding, 1982)

## 2 DEFINITION OF TERMS

The existence and development of society is always associated with the production and consumption of the producers and consumers. They affect and support each other as well as co-exist and develop. The relationship between producers and consumers is expressed through the operation of various types of markets, for example, the market of production factors and the market of goods and services. Economic systems include components, such as household, enterprises, goods and services, factors for production that interact together within the economic cycle – circular flow of income.

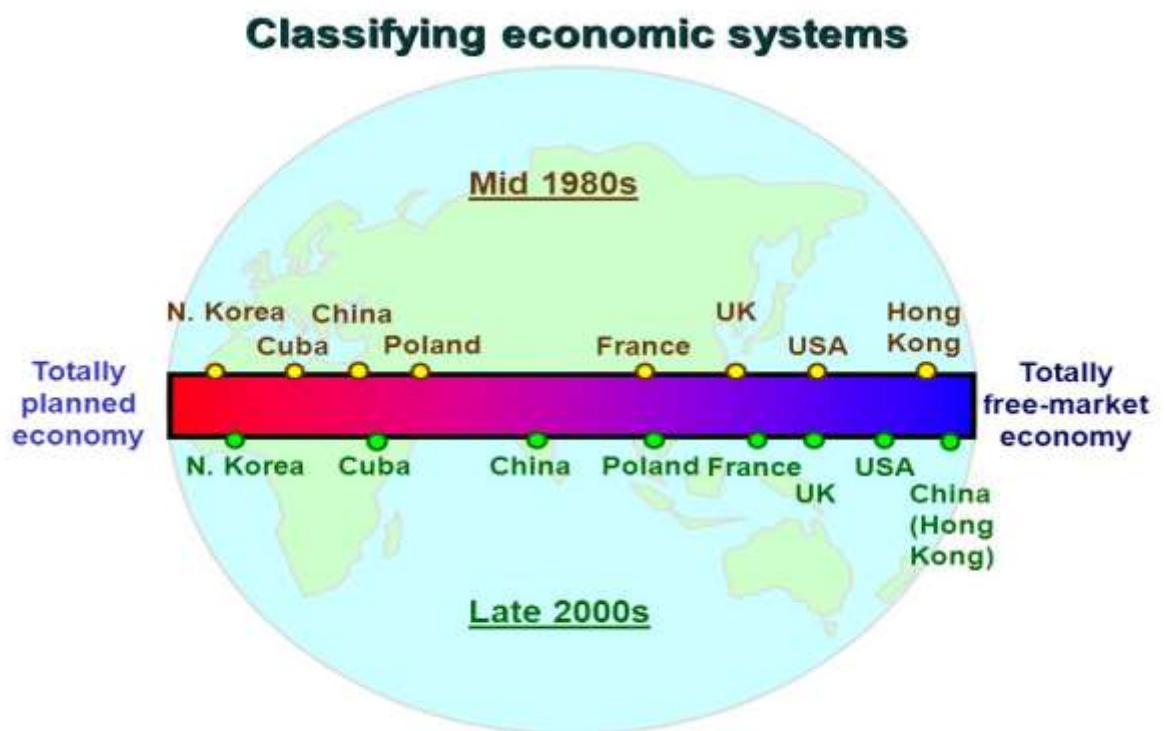


**GRAPH 1 The economic cycle- circular flow of income (Adapted from Kate Raworth, 2014)**

The circular flow begins to supply factors for production of households to businesses, households provide capital, labor and means of production for enterprises, then enterprises use these factors serving their own production and business requirements and paid to households in the form of wages, rent, interest or profit. On the other hand, after receiving factors for production from households, enterprises create goods and services that meet the demand of society (household), thus households purchase and pay in the form of consumer expenditure. Over time, the demand of society (household) for different kinds of goods and services increased in both quantity and quality, it has promoted the development of production technology and production factors, building the better response for society needs and rising new higher demands. Those interactions will promote the development of a society (Buck, 2014)

## 2.1 Three reasons of economic system

The scarcity of resources forced people to choose the most profitable thing in a multitude of goods and services to produce during a particular period. In an economic system, there are three sets of decisions to make. What to produce, how to produce, and for what to produce. Based on how to solve these three basic questions of economics above, the nations are adopting three main economic models, which are free market economy, planned economy and mixed economy. (Ukessays, 2015)



**GRAPH 2: Classifying economic system (Adapt from Darnell Gayton, 2011)**

## 2.2 Planned economy

Planned economy or controlled economy is an economic system in which all decisions on production, distribution and consumption of goods are concentrated in the government. Through its planning agency, the government directly decides what to produce, how and whom manufacturing production for. Planned economy existed in the Soviet Union and the former socialist countries. In these countries, the resources for production are allocated

centrally through the social-economic development strategies that is compiled by the agencies of government. Enterprise owned by the government and cooperatives dominated maintains most of the economic resource of society. In fact, the government has decided specific goods and services that the society needs to produce. Moreover, the government provides capital, machinery, equipment. For the enterprises, they are invested workshop construction, delivered supplies, raw materials, labor recruited. Hence, the goods is only consumed and sold according to government's regulations (Investropedia, 2016)

Incomes of the employees in the government sector are strictly regulated under the wage system which the government issues. Besides, enterprises are obliged to fulfill production targets that the government commits. Basically, the government revenues are all profits, but in return, to aimed losses, enterprises are subsidized by the government. Thus, the organization of production, or trade in the planned economy, in substance, is totally dependent on the government. In fact, there is not a purely planned economy. The complexity of decision making about all problems of social economy makes it difficult to completely implement. Even the Soviet Union-intense planned economy, a number of minor economic decisions have been made in a non-planned way. For example, when the salary is paid every month, the worker can have a right to choose specific goods to consume. However, goods and services are regulated by government so, obviously, this choices is bound in certain limits

Central planning has some potential advantages over a free-market economy. Instead of having to rely on the decisions of millions of individuals, decisions that will not always be in the interests of society as a whole, the government can take an overall view of the economy. High growth rates can be achieved if the government directs large amounts of resources into investment. Unemployment can be largely avoided if the government carefully plans the allocation of labor in accordance with production requirements and labor skills. National income can be distributed more equally or in accordance with needs. The social repercussions of production and consumption (e.g. the effects on the environment) can be taken into account, provided the government is able to predict these effects and choose to take them into account. (Chuyen De 7, 2015)

In practice, planned economy can achieve these goals only at considerable social and economic costs. The reasons are as follow:



- The larger and more complex the economy, the greater the task of collecting and analyzing the information essential to planning, and the more complex the plan. Complicated plans are likely to be costly to administer and involve cumbersome bureaucracy
- If there is no price system, or if prices are set arbitrarily by the state, planning is likely to involve the inefficient use of resources. It is difficult to assess the relative efficiency of two alternative techniques that use different inputs, if there is no way in which the value of those inputs can be ascertained. For example, how can a rational decision be made between an oil-fired and a coal-fired furnace if the prices of oil and coal do not reflect their relative scarcity?
- It is difficult to devise appropriate incentives to encourage workers and managers to be more productive without a reduction in quality. For example, if bonus are given according to the quantity of output produced, the factory might produce shoddy goods, since it can probably produce a larger quantity of goods by cutting quality. To avoid this problem, a large number of officials may have to be employed to check quality (Chuyen De 7, 2015)

Most of these problems were experienced in the former Soviet Union and the other Eastern bloc countries, and were part of the reason for the overthrow of their communist regimes (See Graph 2). Otherwise, besides the goods, there are also some negative factors involved. The most important issues, bureaucracies are increasing. They are often accused by charge of corruption and abuse of power. Moreover, people are poorly motivated with the poor living standard.

The discussion of planned economy is not complete without mentioning of Karl Marx (1818-1883). Marx saw the expansion of the factories and railways across Europe has led to massive disturbances. He argued that, if there is no control, the productivity of the market and competition will certainly cause chaos and severe recession and add to the impoverishment of workers. Marx claimed that capitalism had a doomsday and the revolutionary uprising and socialism will soon occur.

In the subsequent decades, history seems to have confirmed the predictions of Marx. The Great Depression and the economic downturn in 1890 and 1930 period caused world of 20th century a question about the viability of capitalism based on private enterprises.

Socialists who have started applying their model in the Soviet Union in 1917, and until the climax, up to 1/3 of the world was under the influence of the Marxist doctrine. Today, of course, the number of countries belonged to Marxism has rapidly decreased. However, it does not lower Marx's position as an important economist of the world (Chuyen De 7, 2015)

### **2.3 Market economy**

According to Karl Marx, "the market economy is an inevitable development phase of history that any economy would have to undergo in order to reach a higher range on the development path. This range is communism but at the beginning it was socialism. Reaching this point, market economy must grow as the end and become common in social-economic life". This is an important argument. It generalized the development process of human history, in which the market economy has been identified as an essential step. The popularity of the market economy presents is a general frame structure for any system economy. (Prychitko, 2002)

Until the late twentieth century, the market economy almost exclusively had a single development plan that was turned into capitalism. The fact that the market economy does not grow in a specific single model, is performed under many different models. For purposes of clarity the general outline of the development of market economy and especially supporting for the objectives of this thesis, market economy can be divided into 3 categories:

- Free market economy
- Social-market economy
- Socialist market economy

#### **Free market economy**

Market economy in the framework of capitalism is mainly developed in the free market model, implemented in most capitalist economies such as Western Europe and North America. This model enhances the role of individual property regime and liberal competition. Besides, the regulate intervention of the government in economic progress is limited in a lowest level. In addition, the process of economic development largely

depends on the “free-enterprises”, which operates under adjusting of liberal competition mechanism. All economy decisions are taken by households and firms, which are assumed to act in their own self-interest. These assumptions are:

- Firm seek to maximise profits
- Consumers seek to get the best value for money from their purchases
- Workers seek to maximise their wages relative to the human cost of working in a particular job

It is assumed that individuals are free to make their own economic choices. Consumers are free to decide what to buy with their incomes. Workers are free to choose what to sell and what production methods to use. The resulting supply and demand decisions of firms and households are transmitted to each other through their effect on prices. Furthermore, the price mechanism works as follows, prices respond to shortages and surpluses, shortage cause prices to rise, surpluses cause prices to fall. (Chuyen De 7, 2015)

If consumers decide they want more of a product (or if the producers decide to cut back supply), demand will exceed supply. The resulting shortage will cause the price of the good to rise. This will act as an incentive to producers to supply more, since the production will now be more profitable. It will discourage consumer from buying so much. Prices will continue rising until the shortage has thereby been eliminated. If, on the other hand, consumers decide they want less of a product (or if producer decide to produce more), supply will exceed demand. The resulting surplus will cause the prices of the product to decrease. This will act as disincentive to producers, who will supply less, since production will now be less profitable. It will encourage consumers to buy more. Price will continue falling until the surplus has thereby been eliminated.

The same analysis can be applied to factor markets. If the demand for a particular type of labor exceeds its supply, the resulting shortage would drive up the wage rate, thus reducing firms’ demand for the type of labor and encourage more workers to take up that type of job. Wages would continue rising until demand equaled supply, until the resulting shortage was eliminated. Likewise, if there was a surplus of the particular type of labor, the wages would fall until demand equaled supply. On the other hand, the primary function of government is to protect property rights and the freedom of individuals, ensuring macroeconomic stability, creating the most favorable conditions for the enterprise and for

all market. The involvement of the government in the process of redistribution, in the social welfare system to reduce the inequalities and create social justice or prevent market failure is still considered but not as much as in other models.

Besides that, the States also intervenes in the provision of public goods such as security and national defense, building roads and developing the public health system as well as many other areas. For example, in Hong Kong, in 2003, when SARS (Severe Acute Respiratory Syndrome) did outbreak in this region, the States instead of the market has made drastic measures to be able to quickly control and extinguish this epidemic. (Chuyen De 7, 2015)

### **Assessment of the free-market economy**

A free-market economy function automatically is one of its major advantages. There is no need for costly and complex bureaucracy to co-ordinate economic decisions. The economy can respond quickly to changing demand and supply conditions. When markets are highly competitive, no one has great power. Competition between firms keeps price down and acts as an incentive to firms to become more efficient. The more firms there are competing, the more responsive they will be to consumer wishes. The more efficiently firms can combine their factors of production, the more profit they will make. The more efficiently workers work, the more secure will be their jobs and the higher their wages. The more carefully consumers decide to buy, the greater the value for money they will receive.

Thus people pursuing their own self-interest through buying and selling in competitive markets helps to minimize the central economic problem of scarcity, by encouraging the efficient use of the nation's resources in line with consumer wishes. From this type of argument, the following conclusion is often drawn by defenders of the free-market: "The pursuit of private gain result in the social good". This is obviously a highly significant claim and has profound moral implications. (Sloman, 2006)

In practice, however, markets do not achieve maximum efficiency in the allocation of scarce resources, and governments feel it necessary to intervene to rectify this and other problem of the free market. For example, in Hong Kong, in 2003, when SARS (Severe Acute Respiratory Syndrome) did outbreak in this region, the States instead of the market has made drastic measures to be able to quickly control and extinguish this epidemic.

The problem of free-market is as follows:

- Competition between firms is often limited. A few giant firm may dominate and industry. In these cases, they may charge high price and make a large profits. Rather than merely responding to the customer need, they attempt to persuade consumers by advertising. Consumers are particularly susceptible to advertisement for products that are new to them and of which they have little knowledge.
- Lack of competition and high profits can remove the incentive for firms to be efficient.
- Power and property may be unequally distributed. Those who have power and/or property will gain at the expense of those without power and property.
- The practices of some firms may be socially undesirable. For example, a chemical works may pollute the environment.
- Some socially desirable goods would simply not be produced by private enterprises.
- A free-market economy may lead to macroeconomic instability. There may be periods of recession with high unemployment and falling output, and other periods of rising prices. (Sloman, 2006)

### **Social Market Economy**

"The Social Market Economy is not primarily an economic order, but a leading idea or program. An order is a concrete realization, but a leading idea gives direction for human action." (Seraphim in an essay in honor of Erhard in 1957.) It is the programme, as it were, which this paper tries to describe, though in Germany the programme and reality broadly have coincided over the last 60 years (Zweig, 2010). This model has been successfully implemented in many Western countries - Northern Europe, typically Germany (home of the model of market economy - society), Sweden, Norway and Finland. In terms of characteristics, this model is also available in some other countries such as Denmark, the Netherlands, France and Belgium at different levels.

The Germans proudly label their economy a "Soziale Marktwirtschaft ," or "social market economy," to show that the system as it has developed after World War II has both a material and a social-or human-dimension. They stress the importance of the term "market" because after the Nazi experience they wanted an economy free of States intervention and

domination. The only States role in the new West German economy was to protect the competitive environment from monopolistic or oligopolistic tendencies-including its own. The term "social" is stressed because West Germans wanted an economy that would not only help the wealthy but also care for the workers and others who might not prove able to cope with the strenuous competitive demands of a market economy. The term "social" was chosen rather than "socialist" to distinguish their system from those in which the States claimed the right to direct the economy or to intervene in it. (Solsten, 1995)

In general, social-market economy acknowledges the common fundamentals of the market economy. However, comparing with free-market economy, this model has 2 specific features: firstly, social goals and human development, for example, social justice, welfare for poor people, rights to people's development... are the main objects of development progress. In detail, the social market economy is committed to three main ethical goals, which are essential to allow people to live in human conditions. The first and most important of these is an optimal goods supply, which can be achieved only when economic agents enjoy the freedom that forms the basis of their economic creativity. The second goal is the guarantee of decent conditions at the workplace through public legislation, while classical liberalism sees even the labour market as exclusively subject to the law of supply and demand. The third ethical goal is solidarity with the economically weak through a system of social security. In our times, a fourth ethical goal of ecological compatibility and global economic reasonableness should be added.

On this basis, the social market economy is an institutionally order-related programme based on the principles of a competition-oriented economy, linking free personal initiative with social progress, made possible through the economic effectiveness of a successful market. In order to be able to fulfill this function, the institutional order has to meet a number of constitutive conditions. The structural elements which need to be mentioned are: private property, freedom of production, freedom of action, freedom of trade, free choice of occupation, free choice of work and freedom to consume. As the main prerequisite for a free market, private property can be defined as the right of private actors to dispose goods and services. These private actors also have to accept the consequences of their own decisions by being liable – positively in the forms of profits, negatively in the form of losses (Chuyen De 7, 2015)

But the social market economy does not leave it at that. Just as it provides room for success for everybody in the market, it takes responsibility for the losers in the marketplace. For that purpose, it establishes a system of social security to protect all members of society against poverty and hardship and to provide everyone with the potential to lead a dignified life. The intention of this concept is to enable the beneficiaries of these services to live independently of assistance where possible. Answering the question about which of these solidarity services are indispensable to protect human dignity and where States responsibility ends to give room for reasonable individual contributions, the social market economy follows the principal of subsidiarity. (Eisel, 1/2012)

Secondly, the government drives the market economy not only aims to increase economy growth, but also implements goals and improves social quality. With these features above, social-market economy is variation of the capitalism economy, but it reflects an inevitable trend of development that is when it reaches a certain level of development, in specific conditions, market economy cannot efficiently solve all problems by itself. Consequently, to be effective, it should be directed to the social goals and human development. The way to achieve that goal is not to deny the market or abolish it, but place government on the role of management as well as orientate the market economy as the main factor of economic mechanism. “Consequently, the Social Market Economy does not only comprise a free market economy. It also emphasizes the importance of well-defined States responsibilities, which places the Social Market Economy between the extremes of laissez-faire and a planned economy” (Jänsch, 2010)

In reality, the question of whether or not and to what extent States intervention is necessary must be weighted carefully. This leads to a number of problems, which is evident from the fact that there are far too many regulations. For example, the ratio of public spending in Germany has risen to nearly 50 per cent, in part because of massive States intervention during the economic crisis (Jänsch, 2010)

### **Socialist Market Economy**

Nowadays, this market economy model is implemented only in China. The introduction of this model associated with the collapse of Socialist economy, which denies the role of the market economy in the process of development. The appearance of this model

demonstrates vitality of the trend forward Communism as an objective necessity of the times; at the same time, confirms the necessity and popularity of the market economy as a compulsory stage in the history of the development of any economy. China's economy has experienced spectacular growth since the beginning of the economy reform. Because of this dynamic economy growth, the Chinese economy is undergoing drastic changes and is now officially recognized as Socialist market economy.

When Deng Xiaoping- a predominant leader proclaimed: "Getting rich is glorious", he made clear that capitalism and socialism are non-conflicting ideas, as both of them are tools for managing the economy. According to him, the new economic system of China uses the virtues of both capitalism and socialism. It is based on the dominance of the state-owned sector and an open-market economy. Therefore, China's transition to a socialist market economy is a well-through decision, in light of the underlying systems in China and the experience of transition in Eastern Europe. (Holliman, 1998)

The progress of transition is divided into three stages:

- Stage 1 (1978-1984) is an outgrowth of the Third Plenary Session of the Eleventh Parties Central Committee. In that session, it was decided that the central government should be decentralized, with more autonomy to be given to the local government and collective enterprises
- Stage 2 (1984-1992) extended reform to urban areas in the framework of a socialist market system emanating from the Chinese culture
- Stage 3 (1992- 2003) allowed the simultaneous existence of the private and public sector- even if States property remains the main base of the national economy, all forms of property – State, collective and private – will have to be used in developing the economy (Holliman, 1998)

In practice, the communist regime in China quickly realized that it would be to its disadvantage to keep China's economy secluded from the rest of the world. It has been able to successfully strike a balance between the "collective" and "capitalist" approach. Policies allow entrepreneurs and investors to take profits, but within the controls of the state. Around 2004, the government began to allow a person's right to private property. Establishing a special economic zone and opening up to international trade have allowed



the country to embark on fast-paced economic growth – all courtesy to the right changes to the socialist policies at the required time.

Nevertheless, arguably the most fundamental characteristic of the Chinese political system is that the Communist Party retains its traditional "Nomenclature roles", in which party committees; make all the key personnel appointment in the States sector.

Starting from that point of view and comparing with the free market economy and the planned economy, the socialist market economy has the following characteristics:

- Market plays a significant roles in the distribution of resources
- Combining public ownership and market economy and taking the socialist market economy is a necessary choice for the liberation and development of productivity
- Macroeconomic is regulated by the state
- Macroeconomic-regulation is a distinctive concept, The inevitable in market is compensate market shortcoming, regulate the overall market and efficiency in macroeconomic
- Ownership entities of publicly owned assets should be diversified, independent, and in competition with one another
- The priority is manufacturing performance, condescend to justice, the economy is not egalitarianism, nor is economic diversification leading to the poles
- Opening to both domestic and foreign, fair competition, not the protected areas economy, administrative monopoly, seclusion...(not central planned economy)

Moreover, the States still wields power through the allocation of massive States resources and effective control of large-scale SOEs (state-owned enterprises), which continue to dominate key sectors of the economy. Despite formally being transformed into joint-stock companies (selling shares to private investors), the major banks are still effectively controlled by the state. Currently, state-owned and States holding enterprises account for roughly half of all (non-property) urban investment in fixed assets. At the same time, the party-state, a powerful apparatus with massive financial resources, continues to exercise general political direction over the economy. For example, sweeping measures taken by the regime to facilitate the recent Olympic Games- 2008 demonstrated the power of the States to mobilize resources and sweep away obstacles to its policy objectives. There was phenomenal public expenditure on the games, the government ruthlessly cleared residents

from large areas of Beijing, and heavy industries were shutdown in a desperate attempt to reduce air pollution for the duration of the games. (Socialism Today, 2008)

Even having the same characteristic with Social Economy as the aim to eliminate the need for a demand-based market for products to be sold at a profit, however, as Marx- a critique of Capitalism –the most researching, rigorous, comprehensive critique said that:

“Market socialism does away with private property, social classes and exploitation”

For some Marxists, however, it retains too many features of that economy to be palatable. Under market socialism there would still be commodity production, inequality, unemployment and the sway of market forces beyond human control. (Why Marx was right, 2011)

## **2.4 Mixed economy**

While the planned economy and free market economy which are fully free hardly exist in reality, most economies in the world are mixed economies. Mixed economy is an economy in which both the market and the state, in relation to mutual interaction all play an important role in resolving the basic economic problem of society. In a typical mixed economy, the market is mainly dominated and leads the economic decisions of millions of producers and consumers. However, the State is also actively involved and has an important role in dealing with the economic problems of a society. In the mixed economy, commodities such as food, clothing, cars and many other things are still in production, distribution and exchange according to market signals, based on relationships of voluntary transactions between buyers and sellers on the specific market.

In addition, for various reasons, the State is still directly involved in the production of some products such as defense, electricity, clean water etc. or indirectly affect the production of goods in the private sector, the State may prohibit the production and trade in commodities such as drugs, restricting the business of some products such as tobacco, beer, wine, and encourage the supply and consumption of some items such as textbooks for students, iodized salt, water etc. Moreover, the State affects the behavior of producers and consumers through a variety of tools such as legislation, taxation, subsidies etc.

Antimonopoly or acts of unfair competition, environmental protection, chemical stability and promote economic growth, income redistribution to pursue certain goals of equity etc. are the different interests of the States in the mixed economy.

In many cases, the intervention of the States also has limitations as there are many issues that the States do not have the right decision or fund ineffectively (because the program is too big or too long) or even the government is dominated by the minority people, or by the incompetence, corruption,... That is inconsistent with objective rules and unable to reflect the dynamics of the market. Therefore, according to Paul Samuelson, the state's intervention should be limited "in the framework of the competition wise." (Samuelson, 2001)

According to economic and business historian Robert Hessen: "a fully free economy (true laissez-faire) never has existed, but governmental authority over economic activity has sharply increased since the eighteenth century, and especially since the Great Depression. Today the United States, once the citadel of capitalism, is a 'mixed economy' in which government bestows favors and imposes restrictions with no clear or consistent principle in mind." (Hessen, 2008)

In the 19<sup>th</sup> century, even the free market nearly allowed the British to become the most powerful nation on earth but the true free market economy has never existed. Today, the majority of decisions are made in the US marketplace. The government plays an important role in regulating the operation of markets: government regulations and the principles of law to regulate economic life, providing educational services and the police, regulating cell infected and business. Therefore, it can be said that the United States is actually a mixed economy

Overall, in a free market economy, buyers and sellers interacting with each other in a free market, which is not controlled by the government or any authority, determine the answers of all these three sets of questions. On the other hand, a planned economy which is on the opposite side of a free market economy gives the government total control over the allocation of resources, such as the government makes the major economic decisions. However, some economists have criticized these two economic systems for being too extreme and they can only be achieved in theory. People agree that we need something in

between these two economic systems, which is a mixed economy. The government will have some role in regulating the market, but all other activity will be driven by the decisions of buyers and sellers.

### **3 CASE STUDY: CHINA AND THE UNITED STATES**

#### **3.1 Take off for China's economy?**

Currently, the world is up to a question: "is China a communist country?"

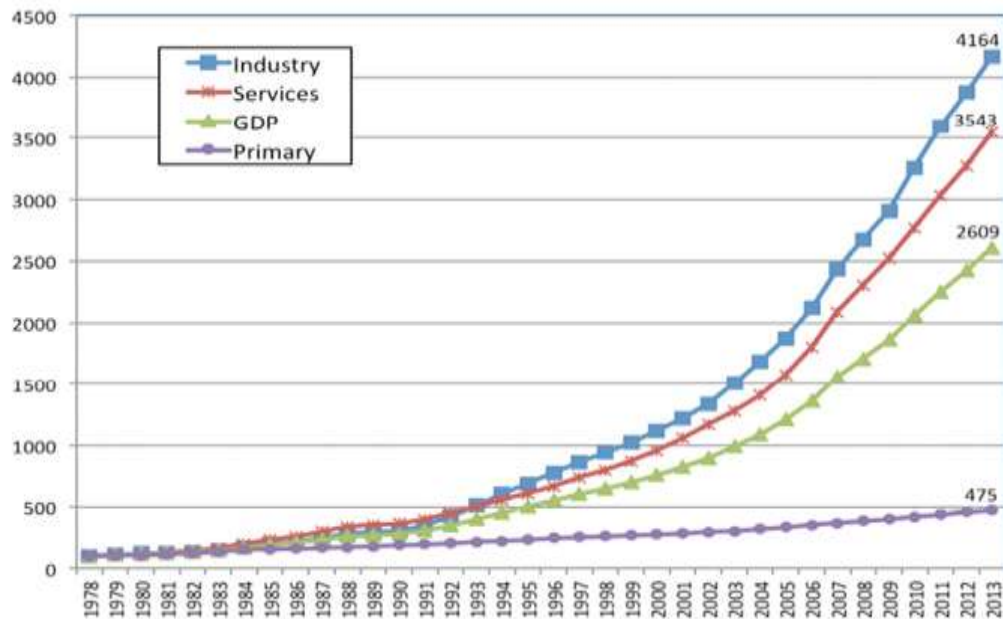
A libertarian says: "China, communist? Ha! They started to succeed when they opened up to free enterprise, and then they kept it going by privatizing the state-owned enterprises. China is a capitalist success story!"(Bloomberg, 2015)

True. China's steady and spectacular rise in the last twenty years has perplexed many experts in western circles. It has generated much intellectual debate as well as a wide range of emotions among Western academics, policymakers, politicians, and the public in large as people struggle to understand the manifold causes for the shift in international, economic, and political power. Once isolated from the world and threatened by the West, China learned to change its fortunes dramatically in the last three decades. China burst onto the world stage a little while, after the diplomatic breakthrough with the US in 1972. Particularly in the last decade, since its accession to the World Trade Organization, China astounded observers around the world with its speed of urbanization, its modernization, its reduction of the number of people in poverty, and the sheer volume of foreign-exchange reserves it holds. China has accomplished much just in the last 15 years including the following:

- 118 megacities with over 1 million people each
- Over 6 million college students graduating per year
- Over 420 million Internet users
- Over 800 million cell phone users
- 271 billionaires
- High-tech exports reaching 20 percent of the total global market
- Auto sales reaching 18 million units a year, making China the world's largest auto market

- Largest number of Initial Public Offering (IPO) issuers in the world, making up 46% of global IPO value

Over more than 35 years of reform and development (1978-2015), China has made great achievements in economy that have attracted world attention in terms of aggregate amount and growth speed (see Graph 3)



**GRAPH 3: Growth of China's GDP and its component sectors (1978-2013)**

In 30 years since 1979, China's GDP has increased 15 times, industrial production has increased more than 20 times; trade turnover is more than 100 times. In the early years of the global financial crisis, China has maintained high economic growth rates. Entering the twenty-first century, China's economy ranked sixth in the world (after the US, Japan, Germany, Britain, France) and by 2010 had surpassed Japan, becoming the second largest economy in the world (after the US)

Though China is still considered an emerging market economy, most experts would put it in a separate category from developed and developing nations because of its unique set of features. It can be described as simultaneously rich and poor, advanced and backward. Experts agreed that China is so vast, complex, and dynamic. The communists, though not seen as infallible by the Chinese, at least have been credited with freeing China from a century of foreign imperialism, a period in their history that they viewed as dark, shameful,

and never to be repeated. To the extent that the Chinese can feel proud of their nation's accomplishments and confident that the government can steer their progress, they prefer the current government to alternatives. (Lee, 2012)

### **3.1.1 Enterprise**

Once upon a time, there were two kinds of businesses. On the one hand, there were public and privately owned companies such as those that existed in Western-style democracies, which had boards of directors and accountability to shareholders, and competed openly in the free market. On other hand state-owned enterprises (SOEs) such as those in the Soviet Union and China, which were tightly controlled by government, packed with party apparatchiks, and stifled honest competition by introducing all kinds of inefficiencies into the market. The States sector in China includes three of components. First, there is enterprise fully-owned by the States through the State-owned Assets and Supervision and Administration Commission (SASAC) of the States Council and by SASACs of provincial, municipal, and county governments. Second, there are SOEs that are majority owners of enterprise that are not officially considered SOEs but are effectively controlled by their SOEs owners. Finally, there are a group of entities, owned and controlled indirectly through SOE subsidiaries based inside and outside of China. Based on the current direction of economy policy making, the States sector in China will play a fundamental role. There are several factors underlying this conclusion. First, the rule of China Communist Party (CCP) has not expressed an interest in becoming a bastion of free market capitalism. It is pursuing socialism-market economy, which mandates a prominent role for States ownership.

In almost 30 years of economy reform progress with the rise of private enterprise, it has led observers to assume that China's economic has been transformed into capitalist economy dominated by private sector. A number of economic, political and policy trends demonstrate that the Chinese economy has become more market-oriented. Chinese statistics show a dramatic rise in the number of ostensibly private enterprises since the late 1970s. China now has stock exchanges in two cities and hundreds of Chinese firms now have listings in exchanges beyond the mainland. In 1978, capitalists in China were official "class enemies" but in 2001 they were welcomed into the Chinese Communist Party (CCP). China's once insular economy—imports in 1978 were only \$10.5 billion—now

imports more than one trillion dollars annually and is one of the top destinations for foreign investments. Chinese firms, including privately owned firms, are now major competitors in advanced country export markets and major foreign investors. (Tsai, 2007).

In a world in which central planning economy has been so utterly discredited. It can be say that the Chinese government or Chinese Communist Party has been abandoning the institutions associated with the communist economy system such as reliance on SOEs as much as possible. It would be wrong so many levels. Through China's reliance on private enterprise and market-based incentive has been growing or even the ruling CCP of private enterprises has been changing, it would be a mistake to write off China has been changed the economy system. True, the private sector nominally is responsible for a growing share of economic activities, but the Chinese government and SOEs remain economic forces. Indeed, some of China's SOEs are among the largest firms in China and the world. According to Forbes Magazine, 12 in 500 largest companies in the world is almost China's SOEs. For example, the state-owned bank ICBC had the highest profits of any company, with \$45 billion. Moreover, they have been involved in some of largest initial public offerings in recent years and remain the controlling owner of many major firms. In short, SOEs is still matter. (Forbes, 2015)

In practice, despite the dramatic restructuring of Chinese enterprises, the subsequent successes of the large Chinese SOEs have become a source of friction between China and some of its trading partners, as these companies have become increasingly formidable competitors in both the Chinese and global markets. The U.S. business community has complained about the unfair competition arising from government policies that favor SOEs rather than private enterprises in the China market. In addition, the Chinese government's encouragement of overseas ventures by large SOEs is also seen to disadvantage other companies competing in the global market. Some complaints are justified. Although legislation has attempted to put SOEs in general framework for private enterprise but in fact, China's economic institutions created for SOEs too many competitive advantages.

For example, banking sector, the commercial banks have been spent most priority for SOEs to be assessed inefficient operations, high credit risks with total loans of up to 20% and especially concentrated in a few conglomerates, big corporations. Moreover, the commercial banks have absolute confidence about the safety of loans to SOEs. They

expect the States will support payment when businesses do not pay their debts, and the fact that commercial banks also accept loan and extensions of credit upon the direction, the designation or the guarantee of government. The States also prevents SOEs from failing, creating “zombie” companies kept alive on a steady drip of government support. For instance, when States steel giant Sino steel tried to file for bankruptcy in 2014, the move was blocked by the government SOE agency’s leaders, reports Caxin (link in Chinese; paywall). Instead, state-owned banks kept on lending to it. By this example showing the basis of Chinese’s socialist market economy, it is based on the dominance of the state-owned sector. The efficient of state-owned enterprises is maintaining their role as the Communist-led country’s economic backbone. (Guilford, 2015)

	Bank loans to (RMB trillion)				Total Bank assets (RMB trillions)	SOE loans as Percentage of		Household loans as Percentage of	
	Non-SOEs	Households	SOEs	Total		Total bank loans	Total bank assets	Total bank loans	Total bank assets
2000	5.08	0.00	4.86	9.94	13.74	48.89	35.35	0.00	0.00
2001	5.95	0.00	5.29	11.23	15.94	47.06	33.15	0.00	0.00
2002	7.11	0.00	6.02	13.13	20.44	45.83	29.44	0.00	0.00
2003	9.13	2.33	6.77	15.90	24.40	42.55	27.73	14.65	9.54
2004	10.59	2.92	7.15	17.74	27.98	40.32	25.56	16.47	10.44
2005	12.00	3.25	7.46	19.47	32.40	38.34	23.04	16.71	10.04
2006	13.99	3.87	8.54	22.53	44.13	37.90	19.35	17.16	8.76
2007	16.45	5.07	9.72	26.17	54.12	37.13	17.96	19.36	9.36
2008	19.57	5.71	10.77	30.34	64.15	35.51	16.80	18.81	8.89
2009	22.30	8.18	17.67	39.97	80.98	44.21	21.82	20.46	10.10
2010	29.07	11.25	18.85	47.92	96.16	39.33	19.60	23.49	11.70

Source: The People's Bank of China

#### GRAPH 4: Breakdown of China’s Bank Loans (Adapted from

It is clear that, China’s SOEs still enjoy preferential treatment from the government. Figure 5 shows that SOEs still receives a share in bank loans that is disproportionate to their diminishing share in the economy. The sharp jump in SOEs’ loan share in 2009 testifies to the impact of the stimulus and its transmission primarily through the SOEs

#### 3.1.2 Privatizing

On the other hand, over several decades, thousands of companies have been privatized in both the developed world and emerging markets. While every company in the former



Soviet Union was once state-owned, now only several thousand businesses fit that description. China has gone from hundreds of thousands of state-owned businesses down to around 20,000. Meanwhile, developed countries, especially the United States has gone from hundreds to dozens of companies that are either completely or partially controlled by government. "Some of the largest state-owned enterprises are becoming almost like private corporations. They are traded in stock exchanges and have boards of directors, maybe even with external managers. We haven't always understood these changes." Since the mid 1990's, the presence of private and foreign-capital companies has grown rapidly as China made great strides in its transition to a market economy, which in turns has significant attenuated the Chinese Communist Party's insistence on States ownership of capital. The resolution of the 16<sup>th</sup> National Congress to recognize admittance of private entrepreneurs into the Party symbolizes the change in party line toward the system of ownership. (Bloomberg, 2015)

This National Congress session basically eliminated what had been left of the political restriction against ownership system reform. Privatization of state-owned enterprises, the final stage of ownership system reform, has been launched as an official policy in 2001. Economic reforms in China from now on onward will likely develop with the privatization of large enterprises as the central issue. (Imai, (ed.) [2001] for the overall development of state-owned and collective enterprises in China up to 2001)

In fact, many of China's state-owned businesses were not actually privatized at all. What happened was that they were listed as private companies, allowing outside investors to own shares in them. The government retained majority ownership, meaning that the government could always call the shots. For example, Baoshan, a Shanghai steel manufacturer, is at least 75% owned by BaoSteel, which is wholly government-owned. In reality, Baoshan is a state-owned enterprise, but in the official figures it is counted as a private company. Then there are murkier cases. For example, Qingdao Haier -- one of China's most famous appliance makers -- is 46.5% state-owned. Theoretically, that is a minority stake, though it seems to stretch credibility to think that the remaining 53.5% could ever overrule a government decision. The company has reportedly been forced to acquire unprofitable companies on occasion, which is the kind of thing you would expect a state-owned enterprise to be forced to do. PC manufacturer Lenovo is majority-owned by private investors, and its chief executive officer insists that it is a "market-oriented" company, but

the Chinese Academy of Sciences owns a significant minority stake. So the "privatized" SOEs are often not really privatized. This has stopped them from doing well – Baoshan, for instance, made a \$940 million profit in 2014. As for the SOEs that were closed after 1999, Hsieh and Song find that many were shut simply because they were unprofitable. Many smaller SOEs were allowed to survive, and many larger SOEs were consolidated into conglomerates. This isn't the free market - this is central planning. (Bloomberg, 2015)

### **3.1.3 Overview**

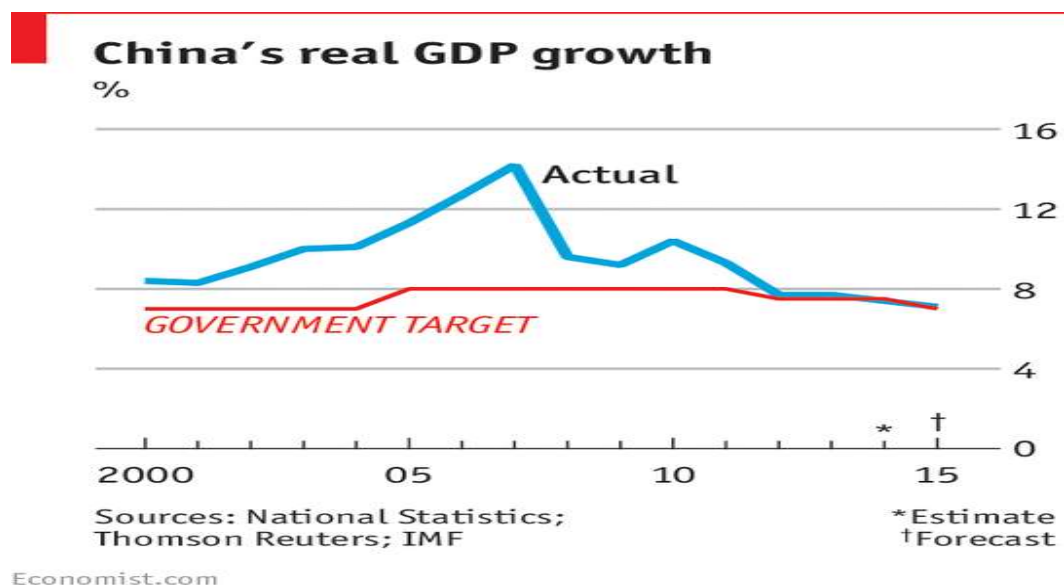
Many authors still call China a communist country. Although, in fact, according to Hu-run Research Institute in Shanghai, China now has 317 billionaires and is the second largest economy in the world after the US. Chinese Communist Party has a group of entities who mainly is the affluent class and big-spender, different than the other Party such as Vietnam or North Korea. The West has been questioned about how nature of the Communist People's Republic of China, but the perspective of Western analysts is really different. Richard McGregor in the article so-called "5 Myths about the Chinese Communist Party", issued the subtitle: "China is communist in name only" (Mcgregor, 2011)

"Communism is based on the economy- a collective, central planned economy. All the rest is just kind of secondary. Without the communist economy policies, there is no communism. So, in fact, China is communist in name only" (Mcgregor, 2011)

Many people are in the same wavelength. However, some other ideas emphasize the fact that China is still a communist country. There is no multi-party system, no separation of power, no freedom for press or human right. When speaking about the future of Communist Party, the majority supported the view that the CCP is a "party-state" that will collapse sooner or later. In the case of continue to grow rapidly, China will appear a millions of high-education people, middle-class becomes more popular, living standard will be improved and collective conscious will change. Therefore, the Communist Party will be transformed into a democratic party or will be collapsed as many communist such as Soviet-controlled Eastern bloc country or other Asian country. (Mcgregor, 2011)

Another possibility is the growth rate decreased, unemployment and poverty is rising. Those are the factors that lead to dissatisfaction with the ruling party and appeared the opposition party that was formed in a struggle for power among the Chinese community, as well as among members of the Communist Party. As many may know, what seems to be going on in China is, the economy is slowing down. According to New York times, “The People’s Bank of China cut its interest rate for one-year loans by a quarter of a percentage point, to 4.35 %, and lowered its reserve requirements by half a percentage point, to 17.5 %. It was the sixth time the bank has cut rates since November 2015”, “The government announced that the economy grew at 6.9 % in the third quarter, its slowest quarterly pace since 2009. Some independent analysts say the actual growth rate is probably much lower than the government’s estimate.” (New York Times, 2015)

“Many Chinese industries, like manufacturing and mining, are closing factories and firing workers. They are not likely to borrow money even if interest rates fall and banks are more eager to lend to them. In fact, many Chinese businesses have borrowed too much money in recent years and will struggle to repay their debts.” (New York Time,2015)



**GRAPH 5: China's real GDP growth**

There are many factors and various reasons can be discussed about the “slow down” economy in China. Many analysts have made the statements such as China no longer has the cheap labor force that keeps its fast growth or too much supply or too little demand in

too many sectors. However, one more fundamental reason is that the economy was a forced growth through States intervention and then China did not grow organically. As the communist country, China's government (Chinese Communist Party) carries a huge responsibilities to lead the country. In CCP, the Politburo plays the prominent role in regulating economy or makes a market-oriented decisions. These Politburo members are also the people heading China's States owned Industries & Financial Institutions. Becoming a member of the Politburo, every entity require a various of "elements" that manage to catch the eye of the of the leader that constitute the Politburo. However, through each era from Mao to Deng, the promotion has been adjusted to aliance on the country's purpose.

While in the past (Mao's) times, the fastest way to the top of the Politbure was by mobilizing a member from the Red Army. However, in Deng Xiaoping's time, the Provincial Leader who showcased increased economic activity within his province was guaranteed a promotion. This led to Provincial Governors became bigger and bigger about infrastructure and building projects. This increased activity of infrastructural development gave States owned Corporations & Banks more business which in return helped the leader who ran these enterprise (Industries & Bank) yield considerable clout within the Politburo. There was a race to top among provincial governors. they initiated infrastructure projects on mammoth scale of which neither there was demand nor requirement. These led to huge swaths of land resembling Ghost towns. (Rapoza, 2015)

Obviously, this mad race rush to build ghost cities also helped other developing countries such as Brazil, or Russia growly exponentially. For example, most of that iron ore being shipped to Guangzhou from Rio de Janeiro and Port Hedland, Australia was going to build Chinese cities...But all issues had to end sooner or later, after Xi Jinping started taking remedial measures to cool down the economy. Moreover, credites are not as easy to get as they were in the earlier times, more roadblocks have been erected in infrasturcture development speding, more restrictionist measures have been taken.To sum up, the China's economy currently is more sustainable development. This led a positive view for many investor wishing for imperishable business structure. The fact that the private sector now has dominated in the Chinese economy and do not interfere with the process of socialist-market economy developing. Nowadays, almost country are capitalist economy which based on the private ownership of capital and production inputs, but the distinction

between China and the rest is from the redistribution of income and wealth, social justice, the narrow bounds in rich and poor or high level of ethnic solidarity and humanism in social relation.

### **3.2 How the United States maintains as a top economy?**

The USA entered the twenty-first century with a gigantic economy than ever. It has not only endured two world wars and the global recession in the first half of the twentieth century, but also overcome the challenges of the Cold War with the Soviet Union for 40 years until cumbersome inflation, high-rate of unemployment, and government's budget deficit in the second half of the twentieth century. America finally has been a period of economic stability in the 1990s. In next 20 years, the US could claim to be the World's Top Economy with a GDP of approximately \$16.8 trillion due to many policies are planned, the US has maintained its position as an economy with high competition, large output and the most influential in the world. (Report & Publication in Vietnamese, 2009)

Many global investors are worried about a series of issues such as risky monetary policy of the Bank in Japan, the debt crisis of Europe or the credit crisis of China ... that affect the US economy. However, the following achievement of US economy can demonstrate that the anxiety of investors is completely unfound. (Report & Publication in Vietnamese, 2009)

- US population is only 4.5 % of the world population but the country now accounts for 1/5 Total Domestic Product (GDP) globally.
- Large-scale US economy nearly double China's economy if calculated in dollars, according to US Trust.
- Manufacturing output of US goods worth a total of \$1,900 billion in 2012, up 27 % compared to 2009.
- The number of employees in this sector has increased by 500,000 people since 2010, according to statistics of the US Trust.
- Capital foreign direct investment (FDI) in the United States in the years after the crisis hit 736 billion US dollars, equivalent to 15 % of total FDI capital of the world, according to statistics of the US Trust.
- 9 of the 10 brands with the highest values of the world are American companies, according to the annual BrandZ research

However, the largest economy in the world is facing with a number of current challenges in which the greatest one is actual rival China's economy. China's economy is been at the front and center over the last few decades. It has a potential to surpass the US as the world's largest economy. In fact, once China did lead US as measured by purchasing power- according to the International Monetary Fund. The IMF estimates that China's GDP rose to \$17.63 trillion in 2014 versus the US GDP of \$17.42 trillion last year. Moreover, comparing different economies by Purchasing-Power Parity (PPP), which is the most accuracy way of comparing economies with different currencies, the size of the Chinese economy, exceeded the size of the US economy in 2014 for the first time. Calculating PPP is the method used by the IMF and other reporting agencies. Even the US Commerce Department estimates that US GDP was \$17.42 trillion in 2014, the same as reported by the IMF and others. And if measured in US dollars, China's GDP is around \$11 trillion (Report & Publication in Vietnamese, 2009)

However, in case of foreign exchange ratios between the US and China, the official currency of the People's Republic of China is the renminbi, often referred to as the yuan. The distinction between the terms "renminbi" and "yuan" is similar to that between British "sterling" and "pound," which respectively refer to the British currency and its primary unit. Currently, the foreign exchange rate between the renminbi and the US dollar is about 6.22 to 1, meaning that it takes 6.22 renminbi to purchase one US dollar. But the exchange rate masks an important point: 6.22 renminbi will buy you a lot more goods and/or services in China than one US dollar will buy you in America. (Report & Publication in Vietnamese, 2009)

The US's economy also confronts some ongoing challenges in the long-term continuity. Although many Americans have a guarantee of living and some who amassed a lot of wealth, but also a significant number of people, especially single mothers and their children who have a poor living standard. Disparities in wealth, though not as high as some other countries, but also larger than many countries. Environmental quality is still a major apprehension. Moreover, there is a significant number of Americans without health insurance. High rate of aging people are definitely a burden to the health care system and the national pension... The global economic integration brings certain instabilities besides

the advantage. In particular, the traditional manufacturing industry has cumbersome deterioration as well as country's trade deficit (Report & Publication in Vietnamese, 2009)

Throughout the continuing upheaval, the nation has adhered to some basic principles of their economic activities. Firstly, and most important object is that the United States remains a "market economy". Americans strongly believe that an economy generally operates in the best way when decisions about what to produce, how to produce, and for whom to produce are formed through the mutual exchange activities of millions of buyers and independent sellers, not by the government or by private interests with public powers. Americans believe in a free market system, prices almost reflect the true value of things, and therefore it may be optimal indications for the economy.

Besides believing that free markets economic system, Americans see them as a way to enhance their political values - especially their commitment to individual freedom and political pluralism as well as their opposition to the excessive concentration of power. Indeed, government leaders have launched a new commitment to market forces in the 1970s, 1980s and 1990s with the removal of the protective provisions of the aviation industry, railway industry, the transport companies, banks and telephone monopolies, and even electric utilities must also derived from the market competition. Besides, Americans vigorously pressed for other countries to reform their economies, which do an extra operating for the US's economy based on the market principles. However, the Americans belief in "free enterprise" does not eliminate the important role of government. Sometimes, Americans alliance on the government intervention to prevent or to adjust a bunch of companies which overdevelop and do not pursue the market forces. Additionally, they rely on government to come up with solution of the problems that private sectors take it slide from education to environment protection. (Report & Publication in Vietnamese, 2009)

The United States is often described as the "capitalism" economy, a definition by Karl Marx named to illustrate a system in which seek to abolish capital. Marxism believes that private ownership of the means of production enriches capitalists (owners of capital) at the expense of workers. In brief, they argue that the owners of the means of production exploit the workforce. They also concluded that capitalism would eventually stagnate due to internal contradictions and be followed by socialism. Marx and those who followed his doctrine claimed that the capitalism economy concentrated on the power into the hand of a

few wealthy entrepreneurs who had a main purpose was profit maximization. Conversely, the socialism economy enhances the prominent role of government and set the political objectives above profit. (Report & Publication in Vietnamese, 2009)

In these categories, despite be overly simplified, there are elements of truth has been changed nowadays. If the pure capitalism has ever existed as Marx described, it would have changed in many levels. In case of US, the government had intervened into their economy in order to restrict central power and deal with many social problems related to commercial interest. Hence, although there were periods in U.S. history when it was closer to a true free market economy, the US's economy may be describe as a "mix" economy, in which the government of the U.S. has always played some role in economic affairs. Over time, more and more services have come under the influence or direct control of the public sector. Although, Americans often contradict by themselves about an accurate boundary between their belief in free enterprise and government intervention, but the mix economy brings many significant achievement for US in many years.

While the States owner enterprises bring a significant role in China's economy, in contrast, US undertake the free private enterprise as the major of whole economy system. So why has America been such an economic success and being the top in the world economy? Certainly, they have the open land, natural resources and uninterrupted flow of immigrants with different backgrounds and experience all contribute. However, the key factor has also been the American tradition of the free enterprise he social and political commitment to giving people the freedom and flexibility to try out their business ideas and compete in the marketplace. The U.S. economic system of free enterprise operates according to seven main principles:

- Economic freedom in the United State: Individuals have the right to choose their occupations and to work wherever they can find jobs. Businesses can make their own decisions on whom to hire, what to produce, how much to produce, and how much to charge for their products and services. The government generally does not interfere in these decisions.
- Competition: Producers have the right to engage in rivalries to gain business. Competing producers have an incentive to create new and better products. This gives consumers more economic choices.



- Private Property: Individuals and businesses have the right to buy and sell as much property as they want. Property owners may prohibit others from using their property
- Contracts: Individuals and businesses have the right to make agreements to buy and sell goods. Such contracts may be written or oral. They are legally binding
- Self-Interest: Consumers and producers may make decisions based on their own benefit. Their decisions do not have to benefit or please the government or other consumers and producers
- Voluntary Exchange: Consumers and producers may freely buy and sell goods when the opportunity costs of such exchanges are worthwhile. In a voluntary exchange, both parties expect to gain from the transaction.
- Profit Motive: American free enterprise is driven by the desire for profit, the gain that occurs during financial dealings. Profit is a powerful incentive that leads entrepreneurs and businesses to accept the risk of business failure. (Report & Publication in Vietnamese, 2009)

Americans always keep the faith that they were living in the land of opportunities, where anyone having a good idea, determination or energetic in character can start a business and have a successful path. In fact, that trust in business is represented very diverse from an individual small business to the giant international business conglomerate. Nowadays, the US economy takes a pride on the network-wide businesses from single shareholder company to the international corporations. As the statistic in 2013 Country Business Patterns, the United States has 16.4 million limited liability companies, 1.6 million partnerships and 4.5 million corporations - 22.5 million free enterprises. (Report & Publication in Vietnamese, 2009)

### **3.2.1 Small economy**

The US economy has not totally driven by giant corporations. According to the Small Business Administration of the United States (SBA), small businesses account for 52 % of total US employment. Approximately 20.5 million Americans work for companies with fewer than 20 people, 19.6 million work for firms with between 20 and 99 workers, 16.6 million work for the company from 100 to 499 workers. By contrast, 56.8 million

Americans work for firms with more than 500 employees. (Report & Publication in Vietnamese, 2009)

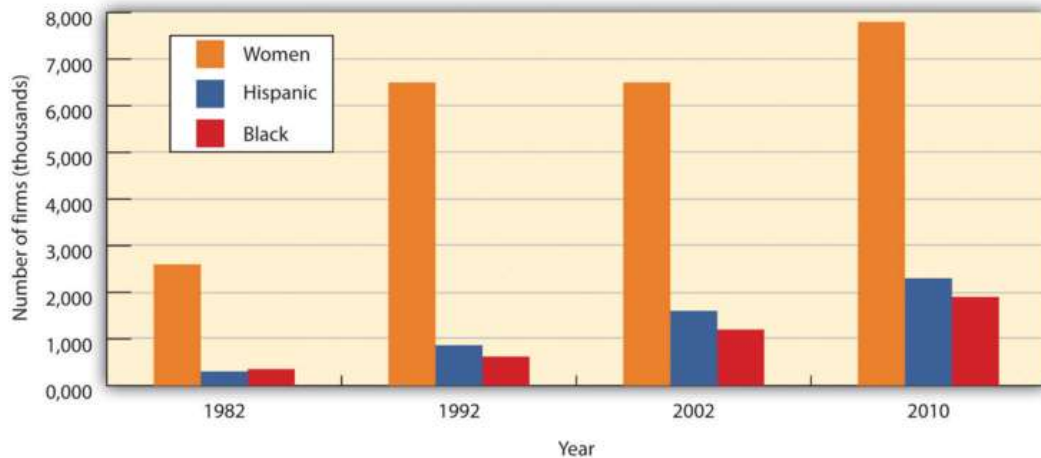
A particular strength of small businesses is able to react very quickly to changing economic conditions. They often know their customers personally and especially suitable to meet the local needs. Small businesses - for example, the trading company in the field of computers in "Silicon Valley" of California and other high-tech are the source of technical innovation. Many computer industry reformers started as "repairman" who worked by hand in their own workshop, and quickly developed into the powerful corporations. Small companies quickly become the main player in the national economy and international including computer software company Microsoft, transportation services company Federal Express, Nike, or even an ice cream company Ben & Jerry's. (Report & Publication in Vietnamese, 2009)

On the other hand, there are also many small businesses bankrupt. However, in the US, failure in business is not a social stigma as in some countries, especially in China. Often, failure is seen as valuable lessons for entrepreneurs, who can be successful in the coming time.

The appreciation of the public for small enterprises has turned into a significant lobby for the interests of small businesses in USA parliament. The small company has won holding down many federal regulatory activities, such as the regulations on safety and health. Congress also established the Small Business Administration in 1953 as an independent agency to aid, counsel, assist and protect the interests of small business concerns, to preserve free competitive enterprise and to maintain and strengthen the overall economy of US. In the typical year, Small Business Administration guaranteed \$10 billion in loans to small businesses, normally for production capacity, infrastructure, machinery and equipment. Moreover, the small investment firms have been supported more \$2 billion in venture capital by the SBA. (Report & Publication in Vietnamese, 2009)

Additionally, SBA pursue to supporting programs for ethnic minorities, especially African Americans, Asians and Hispanics. It carried out an active program to identify markets and business opportunities for small businesses with export potential. While the majority of small businesses are still owned by white males, the past two decades have seen a

substantial increase in the number of businesses owned by women and minorities. Figure ... "Businesses Owned by Women and Minorities" gives you an idea of how many American businesses are owned by women and minorities, and indicates how much the numbers grew between 1982 and 2007



**GRAPH 6: Businesses Owned by Women and Minorities (Adapt from Census, 2012)**

Besides, this agency also sponsored a program in which the retired entrepreneurs get assistance for the new small businesses in the term of management. Furthermore, SBA granted 26,000 million USD by credit in the form of loans with low interest rates for home-owners, renters and all sizes of businesses which are damaged due to floods, windstorms natural disasters and other catastrophes.

### 3.2.2 Corporation

Although there are so many small and medium companies but the large companies still plays the fundamental role in the US economy. Some reasons have been debated about this situation involve with operation, business conditions and customer follow up. The point is that the large firms can provide goods and services for many customers and more effective, productive than small business. Moreover, they often sell the product with lower price due to the larger quantity of product. And the well-known brands ensure the certain level of

quality. Therefore, the goods can simply approach the customer's demand. (Report & Publication in Vietnamese, 2009)

The large firms are highly critical in one piece of economy. On the ground that they often have greater financial resources to conduct research and develop new products. And generally, they are offered the opportunity for employees more diversified, more stable including higher wages and health benefits as well as high-quality pension than small businesses.

However, Americans have conflicting attitudes towards large companies. On the one hand, they recognize the importance of their contribution to the prosperity of the economy, but on the other hand they anguish large firms becoming powerful and stifle small new businesses and deprive consumers of choice. Moreover, large businesses sometimes demonstrate inflexible in adapting to changing economic conditions. For example, in the 1970s, the American automobile manufacturers were slowly realized that the rising of gasoline prices will create demand for small cars using less gasoline. As a result, they lost a significant market share in the country for foreign manufacturers, mainly from Japan. (Report & Publication in Vietnamese, 2009)

In the United States, most large businesses are organized into corporation. The corporation is a form of business organization in particular legal, protected by one of the 50 States and are treated under the law as a legal entity. The corporation can own property and may sue or be sued in court and may conclude a contract. On the ground that the corporations have independent legal status, hence the corporation owners are partially protected from legal responsibility for its activities. The owners of a corporation has only limited for finance. For instance, they are not responsible for the debts of the corporation. Due to the stock of a corporation can be transferred so the private corporation cannot be ruined in case of an owner dies or corporations abandon. Owners can sell their shares at any time, or leave to heirs. (Report & Publication in Vietnamese, 2009)

However, the side back of corporation demonstrate in some cases, for example, corporations are taxed twice - first, when the company makes a profit, and again when dividends are paid to shareholders. Because corporations are highly regulated by federal,

state, and in some cases local agencies, there are increased paperwork and recordkeeping burdens associated with this entity.

Nevertheless, the corporation may own over millions employees who are permitted to hold corporation's share, but only in miniature of the corporation's stock value. About half of American households own shares to normal way or by mutual funds or by pensions funds. Christopher Cox- former Chairman of the U.S. Securities and Exchange Commission is in his speech in 2007: "Almost American workers engaged in marketing capital market. This fact is increasingly common that what is good for the (Report & Publication in Vietnamese, 2009)

American investors are good for the American people. By the same principle, the degree to which a business serves its investors' interests is a measure of its success. After all, if we're talking about common stock holders, the investors own the business. If the business succeeds, so do they. And if the business fails, they do, too" (Christopher Cox, 2007)

This can be seen that in USA, every employee has right to decide their own destiny even in economy which seemed to be impossible in communist country. Moreover, in the mix economy, most businesses and industry can be left to private firms. Private firms tend to be more efficient than state-owner firms because they have a profit incentive to cut cost and be innovative. However, as a definition of mix economy, the government's role always exist but in the lowest level.

### **3.2.3 Intervention of government**

Back to history, economy policy of US government was summarized by a French term "laissez-faire" which mean as an economic system in which transactions between private parties are free from government interference such as regulations, privileges, tariffs, and subsidies. This concept derived from the economic theories of Adam Smith- a Scottish economist in the eighteenth century, whose work had a great influence on the development of American capitalism. However, in many cases, the implementation of free enterprise policy does not prevent individual interest groups towards the government for asking help. Government's intervention for private enterprise can be divided into 2 categories. First, regulate economic activities mainly to control the prices. It was built in the theory of protecting consumer and certain company (especially small company) away from forceful

company. This action is often defended on the ground that the perfect competitive market has never existed. Second, regulate social activities boost noneconomic goals such as working conditions or environment. Regulate social activities seek to limit or prohibit the harmful behavior for social security, for example, the government restrict the exhaust fumes from factories and cutting taxes for standard company which attach special important to retirement or healthy benefit of employee. (Report & Publication in Vietnamese, 2009)

There were a many achievements that US government gained to remain a sustainable successful economy including regulating monopoly power was a most fundamental accomplishment. The monopolies are the first business entities that US government tried to regulate for public interests. The merger of small companies into larger companies has created an opportunity for the corporations avoid market principles by "fixed" price or eliminate competitors. Practically, the government intervened to split the Standard Oil Company of John D. Rockefeller's and several other big firms alleged to have abused their economic strength. Nevertheless, banking is a special case applying regulates activities of US government. On the one hand, all of those banking company are private enterprise as many manufacturing company. On the other hand, they also play a prominent role in the economy and therefore it affects the welfare of their own customers as well as affects the welfare of Americans.

One of the most important regulate activities is deposit insurance. During the Great Depression, the decline of the US economy was exacerbated by many people who are afraid that the bank saving their money could collapse; hence they did withdraw all deposit at the same time. In the "flocking" race to the bank, depositors were often in long queues on the street with panic mood and all's one have to retrieve the money. Many banks, including banks operating very cautiously, have collapsed because they did not catch up fast enough by transfer their own properties to cast that satisfied their customers. Finally, the bank's provision for loan to enterprise was shrunk and made the decline of economy more serious (Report & Publication in Vietnamese, 2009)

Deposit insurance is designed to prevent those flocked cases. The government claimed that the coverage for those deposits was up to a certain level - currently \$100,000. Now, if the bank has difficult financial, the sender will not have anything to worry about. Bank

insurance agency of the government, also called the company federal deposit insurance, paid out to the sender by the insurance fund is formed from the premiums of banks. If necessary, the government in general also use revenues from taxation to protect the sender get away with excessive risk. Besides, the supervise agencies regulate and order the adjustment of each bank whose activities are too much risky.

### **3.2.4 Overview**

The US economy is the system that is united by the philosophic commitment about ideas of the free market. In fact, the US's economic often alliance on the government to regulate the private enterprise, identifying unmet demand, ensuring a certain stability limit to the entire economy. It can be seen that the US's economy system is marked by continuous changes. The dynamism of US's market is accompanied with the loss and hitch from the consolidation of banking sector to determine the dispute over monopoly. After the reform of economy, small and medium companies or even corporation can be smaller or distinct, but the Americans strongly believe that it will be stronger, more sustainable. Moreover, it is equipped to withstand the rigorous of global competition. Businesses can be loss but they are likely to replace by a new line of businesses in the greater potential industry. For example, the decline of employment in the manufacturing industry has been offset by the rapid of employment in high-technology industry such as computer industry and biotechnology.

However, success in economic also spawned other problems. One of the most concern things is that the Americans now are facing with the growth. Economic growth is central of the America's success. As the economic pie has grown, the new generation has a chance to carve a piece for themselves. The fact is, economic growth and its opportunities helped to keep class conflict in the United States in a lowest level. By all means, economic growth is never permanent. Since 1854, the US economy has been through totally 32 cycles of growth and recession. However, in the modern period, the growth's cycle becomes longer and the recession's cycle becomes shorter. Furthermore, the Americans are covered by the diminish living standard. They set up the question; will the growth deserve if it brings too many highways, air pollution and overload social issues?

Moreover, the matters of Americans middle class are increasing about career security more than ever in case of facing with the rapid changes such as changing in technology, competitive pressure from foreigner cheap labor.

However, the US maintained the highest position in the global economy, and still, on the ground that the regulation and adjustment in education as well as training of the US government.

According to economic and business historian Robert Hessen: "a fully free economy (true laissez-faire) never has existed, but governmental authority over economic activity has sharply increased since the eighteenth century, and especially since the Great Depression. Today the United States, once the citadel of capitalism, is a 'mixed economy' in which government bestows favors and imposes restrictions with no clear or consistent principle in mind"

To sum up, the US is likely to lose the most important position in the global that is an unavoidable due to the changes in structure of many countries, especially China – go after US. However, pursuing the mix-economy with free enterprise and lowest level of government's intervention turn the US into the most prospective country in the world in many different sectors involved economy, education, living standard which China is struggling to come up with the solution to neutralize.



#### **4 WHAT CHINA CAN LEARN FROM THE UNITED STATES?**

Setting aside prognostications of the decline of the US and the rise of China, everyone must not forget the enormous contribution the US has offered the world, namely its model for liberalized thinking that has led to innovations in many areas. The US is still among the most free of societies and has generated a lot unconventional thinking that has propelled the world forward.

Many developed nations in both Asia and Europe suffer from the stigma of failure, For instance, entrepreneurship is not respected in China. NYU Professor Edward Lincoln recalls being surprised to see three men from China at a Young Presidents' Organization (YPO) meeting, given that YPO members are 50 or younger, and most Chinese CEOs are older than 50. He later learned that these men were all sons who replaced their fathers at these companies.

In contrast, many YPO members from the US had started their own business, a sign that risk-taking is more acceptable here. This phenomenon is further supported by Silicon Valley venture capitalists who indicated in conversations that they almost unanimously preferred to invest in entrepreneurs who had experienced failure at least once with a previous start-up, an attitude that many Chinese find strange because they go out of their way to avoid failure. Because U.S culture is more forgiving of failure and has bankruptcy law to protect failed businesses, people here have been able to bounce back from economic setbacks more easily than in many other places in the world. China should recognize this strength and choose to embrace it as its own, especially when it reaches a point where its economic growth no longer allows it to depend on modifying foreign technology to suit its needs.

Aside from developing a culture that embraces entrepreneurialism, the China must be prepared to slow growth in the short term by investing more in people doing pure research, which is riskier than applied research from the standpoint of return on investments. Pure research can be far from certain in yielding anything immediately useful or commercial, but it can lead to quantum leaps in innovation. Most private companies do not have the financial resources to make such investments, so governments must lead the way on this front.

Another things China can learn from the United States is sales, public relations and branding. The U.S culture has a worldwide reach. Its fast food restaurants, movies, celebrities, consumer products and even politics have attained global recognition through mass marketing. The effectiveness of the United States to sell the world everything it has to offer is a skill, the importance of which cannot be underestimated. While a couple of Chinese brands, such as Huawei and Haier, are gaining recognition in overseas markets, China has a great deal to learn in this regard. In order to complete in a globalized world, the ability to stand apart from the crowd is a necessary survival. If China wants to go global with its own brands, it must learn not only how to break into new sales channels, it must also learn how to create brands that can compete against American brands, such as Apple and Nike, which have won widespread customer loyalty.

China should also continue to reform its judicial system to emulate the standards of fairness found in the US. While the jury system exists on paper and has been tried in China, its use is still not widespread for unclear reasons. Moreover, China cannot give up its fight on corruption, especially among local officials in the lower rungs of government. Despite the high incidence of corruption among economic and political elites in the US, it is still perceived to be much less corrupt than China in many levels. China needs to tackle provincial corruption much more thoroughly if it plans to avoid more serious societal unrest down the road. Currently corruptions in China are a serious problem. It also the main reason of China's economic downturn in 2014, but the fact that the top leader in China cannot put an end to it indicates how difficult it is even in China to drive constructive political changes.

## 5 CONCLUSION

This thesis provides people a basic guide of the world's economic system and how politics effect organizations. In every nation, no matter what the form of government, what the type of economic system, who controls the government, or how rich or poor the country is, three basic economic question must be always answered.

Moreover, the purpose of this study was to explore the different aspects of each economic system, especially communist and capitalist country. The various topic covered in this text defined many ways political system affects the whole economic and the broad observation about economic world's leader such as United States and China. The themes analyzed in this text also established a broader understanding of the reason why China's economy take off or how the United States maintain as the world largest economy.

China and United States - communist country and capitalism country, presented as a case study, is a typical example for the different in economic system. The outstanding feature of the two political institutions is clearly expressed through specific examples. A strong economy includes not only accelerate the economic data, but it also has a positive impact on other aspects such as social, education and health. Despite the great growth in the economy, but China is still a lot of flaws which is also a reason why the analysts currently estimate that China's economy is going down while United States always maintain as stable economy. The political system and the intervention of the States is one of the main reasons to make up this difference. This essay also show the dark side in the political system of the Chinese economy, which should learn from the United States.

To sum up, since society can be part of economic systems, it is also an important factor in people getting along in a balance of nature. Humans are social by nature therefore an economy that promotes this social interaction will also increase the effectiveness of the economic system in place and the balance of one's life. Therefore, the enterprises should have an in-depth understand about the nature of politics to discover a successful path to a sustainable business.

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