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\*Broad and Shallow Knowledge for Intellectual Conversations\*

Vol 1. [Reality] Part 2. [Economics] Chapter 2.

> \*\*[Free Market and Regulated Market]\*\* - Which will you choose

In Capitalist society, market is no different than the entire society. Market doesn’t exist inside society but rather market enabled abstract society. Today, market is the whole society.

There are two economic units in this market: Households and Firms. These two form the market. They’re friendly but there’s a third unit who tries to bother them, the government. We’ll look at the government just as an economic unit that sometimes intervenes the market and sometimes not.

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Households🧑‍🤝‍🧑Firms 🏛️

<Market> ↔ <Government>

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What does intervention mean? There are mostly two types of government intervention: Taxation and Regulation. We’ll be focusing on taxation. Government intervenes the market through taxation and mediates market activities by controlling amount of taxes. Higher taxation stabilizes government finances, and the government actively improves social welfare. Lower taxation reduces government finances, and thus also social welfare benefits. Taxation and social welfare are directly proportional, and we shouldn’t think one without the other.

To summarize, there are two possible economic policies. Pursuing free market and minimizing government intervention, or minimizing free market and reinforcing government intervention. Intervention means taxation. Bigger free market means less government intervention, thus less taxes. More government intervention means less free market, thus more taxes.

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free market > government intervention = taxes ↓, social welfare ↓

free market < government intervention = taxes ↑, social welfare ↑

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From now on, taxation and social welfare will be extremely important in the whole discussion throughout this book. To put it simply, two core concepts of understanding social problems are taxation and social welfare. Let’s simplify their problems.

There lives A, B, C in two different society ①, ② with a different taxation policy. They’re salaried employees. A receives 1,000 dollars a month, B 500 dollars, and C 100 dollars. But society① demands only minimal taxes, with 10% taxation rate. Then subtracting taxes, the real salaries are, 900 dollars for A, 450 dollars for B, and 90 dollars for C. Taxes they pay are, A 100 dollars, B 50 dollars, C 10 dollars. Some might feel unfair. They all receive the same social welfare, but A must pay 10 times more than C? Some would say society① forces A’s sacrifice.

But society② is even less fair. Not only they have to pay the same rates of tax, but it also even has a Progressive tax. Progressive tax is in short, higher income, higher tax rates. People in society② likewise receives 1,000, 500, 100 dollars each. But with a progressive tax system, they are imposed 50%, 30%, and 0%. So taxes they pay are, 500 dollars, 350 dollars, and 0 dollars. What kind of daylight robbery is this, some people might say, but most modern countries are enforcing this policy to some degree. But it doesn’t stop here. Society② takes all the taxes they got from a progressive tax and use it for C’s welfare who didn’t even have to pay it. This is unacceptable for A. To A, he has his hard-earned money stripped by taxes, and stripped again by C because of its welfare policy.

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🙂 🙂 🙁 <-(depiction of ill-looking powerless person hunched over)

A B C

1000 500 100

Society1 900 450 90

Society2 500 350 100

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Now I’ll ask you. You’re seeking asylum, and you must make a choice between society① or society②. If you had to live in one forever, which society will you choose? Your choice might differ depending on your income level. Or let’s change the question. Which society is more just? Which society is more ethical? We’ll analyze your choice in [Politics] chapter later. Let’s hear from A, B, and C for now.

A will of course choose society① with lower taxes and thus poorer welfare, where free market is formed without government intervention. To A, society② is just straight-up robbery. Righteous society to A is a society which protects their wealth earned from their own ability and effort.

C on the other hand will of course choose society② with higher taxes and better welfare. To C, society① is an inhumane society which doesn’t look after second-class citizens like himself. Righteous society to A is a society with minimal life support ensured for everyone.

What about B? It’ll be a hard choice. Looking at his salary, society② feels like a robbery, but it will reduce his income gap between A with his high taxation rate.

What are the pros and cons? Society① seems freer with less taxes. They can spend as much as they earned. So A, B, and C will all try their best to make money. Trying their best means they’re competing individually in whole society’s scale, and through competition, technologies will develop, production will increase, and quality of services will increase. But there are downsides. Even if it’s a difference in ability and effort, income gap gets too high with no redistribution. A may be content with his high income, but C will feel relative deprivation looking at A. He can try to catch up to A, but this much gap will discourage and even make him give up from the competition. C will realize he can’t close the gap with his effort and look for expedients or antisocial ways. Or he may be hostile to A. C’s behavior will destabilize society①, raise social conflicts, and social expenses will increase by that amount.

Society which solves this problem seems like society② with more taxes and better welfare, where government actively intervenes the market. And actually, if you flip society①’s downside, it becomes society②’s upside. A’s income gets redistributed to C by imposing heavy taxes, C’s life will stabilize, social conflicts will be lowered, and social expenses will decrease by that amount. Plus, C might think it’s doable to compete even with an income gap between A. So he may work harder and spend.

But society② also has its own set of problems. Now A will feel defeated. If his hard-earned money is taken away by taxes, A won’t put in his best efforts, and will try to avoid fierce competitions. If A’s an entrepreneur, he won’t try to take risks on investing in the market. Competition between individuals and entrepreneurs will weaken, so production will decrease, innovation on technology and service may come to a halt. Or A might move to different society with less government intervention. This will lower production and efficiency in the whole society. It might not be a problem if society② was the only one out there, but it will always lose to society①, and could lead to recession in the whole society.

It's hard to choose. A society without shortcomings not only does not exist, it is impossible. The problem of choosing is not to find a perfect society but to decide reducing whose profit can be accepted. It will be discussed in the [Politics] and [Society] chapters.

Let’s summarize. We tried to learn the relationship between the market and the government. Government intervening the market is a problem of how the government imposes taxes. Government relates to the market by increasing or lowering taxes. And the increased or decreased taxes will decide the level of social welfare. Increase or decrease of taxation and welfare brings economic growth or recession, and effects social conflicts and stability.

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┌ Tax↓, welfare↓ ┬ Pros: competition↑, efficiency↑, economic growth↑

┤ └ Cons: wealth gap↑, social tension↑

└ Tax↑, welfare↑ ┬ Pros: competition↓, efficiency↓, economic growth↓

└ Cons: wealth gap↓, social tension↓

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Now that we looked at the relationship, now’s a time to divide economic systems based on it.