

Political Economy



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Political Economy

- The political economy is the study of the **interactions of politics and economics.**
- Politics is the **study of power** and the economics is the study of the **creation and distribution of wealth.**
- Both **power and wealth** are closely connected.
- So, the **understanding of contemporary politics** requires an understanding of its pervasive **linkages with economics.**

Key concepts

- Market
- Property
- Public goods

Market



- ❑ Not a physical place.
- ❑ Aggregation of individual's buying and selling behaviours.
- ❑ Natural forces of supply and demand.

Property



- Ownership of goods and services.
- Property rights.
- State and property rights.

Public goods



- ❑ Diffused to all and not individually held.
- ❑ States hold a monopoly.
- ❑ Example- national defence, flood control systems, and street lighting

Types of political economies

- Three different types of political economies:
 - ▣ (1) the *market economy*;
 - ▣ (2) the *command economy*; and
 - ▣ (3) the *mixed economy*.

	Command	Market	Mixed
<i>Who <u>controls</u> the factors of production?</i>	The state owns all significant factors (land, labor, and capital).	Every private actor (household) controls her own factors.	The state and private actors each control some factors.
<i>Who <u>determines</u> what goods are produced?</i>	The state devises a detailed economic plan that specifies what <u>level of each</u> good will be produced.	<u>All actors</u> (firms) make their own separate decisions about production in an attempt to maximize their own utilities.	Some firms are under direct <u>state control</u> , but most make <u>decisions in the market</u> . The state regulates some actions of many firms and households.
	The system is supply-oriented.	The system is demand-oriented.	The system is mainly demand-oriented.
<i>Who <u>establishes</u> the <u>value</u> attached to different productive factors and goods?</i>	The <u>state sets the</u> value (price) in all exchanges.	The market (via the "invisible hand") sets the value, based on the equilibrium of supply and demand.	The market sets the value. The state regulates some prices to serve national priorities.
<i>Who decides how factors and goods will <u>be distributed</u>?</i>	The state's <u>plan</u> indicates who will receive which goods and in what amounts.	Distribution is based on a summation of the actions of all consumers and producers <u>in the market</u> .	The market is the main <u>decision maker</u> . The state <u>intervenes</u> in some cases to ensure that certain actors have access to particular goods.
<i>What is the <u>role of the state</u>?</i>	The state is dominant, controlling <u>almost all</u> aspects of the <u>political economy</u> .	The state <u>plays a minimal</u> role in the political economy. The state enforces the "social contract," protecting all from violence and lawbreakers.	The state attempts to strike a <u>balance between</u> : (1) state control and competition; and (2) private profit and a sharing of societal resources.

Benefits and Problems of market and command economy

	Benefits	Problems
Market Economy		
<i>Competition</i>	Energetic and efficient production	Ruthless interactions; huge inequalities in wealth and resources
<i>Demand orientation</i>	Goods' cost and quality responsive to consumers' <u>desires</u>	Creation of demand for and proliferation of goods that have <u>limited social value</u>
<i>No central plan</i>	Local decision and "invisible hand" stimulate <u>innovation</u> , facilitate freedom	Economic cycles of boom and bust, inflation and recession
Command Economy		
<i>No competition</i>	Work for common good; relative equality of wealth and income; minimal conflict	Little initiative; shoddy products; low productivity; limited innovation
<i>Supply orientation</i>	Production and distribution for social and individual needs	Oversupply and shortages; lack of coordination
<i>Central plan</i>	Rational use of societal resources	Overcentralized control; lack of responsiveness to changing circumstances

Connections with different 'isms'

- In their most straightforward form, capitalism, communism, and socialism correspond loosely to market economy, command economy, and mixed economy, respectively.

Market economy	Command economy	Mixed economy
Capitalism	Communism	Socialism

Capitalism

- **Capitalism** is a system in which *private economic actors are quite free from state constraints, private property rights are fundamental, and the state engages in few actions that might shift resources among private actors.* Ex: Switzerland,
- It is praised for its economic **dynamism, innovativeness, and responsiveness to market demand.**
- It is criticised as a system of **self-interested individualism that denies the need for collective action** to protect the disadvantaged, to nurture society as a whole, to promote social values and culture, or to protect the ecology

Communism

- **Communism** has as its centerpiece the socialization of resources—the notion that the **state must actively control society's land, labor, and capital** to achieve substantial equality for all citizens. Example- Cuba and the former Soviet Union (1917–1991).
- Consistent with the command political economy model, the state guides the **utilization of all these major means of production with a central plan** so that the production and distribution of goods serve **the best interests of the entire population**.
- Its critics disparage communism as an **inefficient economic system with a nondemocratic government** that denies individual freedoms and rights.
- In recent decades, most countries have **abandoned the command economy** that is central to communist principles, leading some to suggest that communism is dead.

Socialism

- **Socialism** is in the **middle of the two “isms,”** and thus it is not precisely differentiated from the other two.
- It seeks a **complex balance between state involvement and private control of the economy,** and a key policy goal is a relatively equitable **distribution of benefits to all citizens.**
- As in the mixed political economy, some **major productive resources are owned or controlled by the state,** and the state actively intervenes in planning and regulating the economy; but most production decisions are private, and value is established primarily by supply and demand.
- Socialism is distinguishable from communism because the state **only controls a few important factors of production and allows private actors considerable freedom** of action.
- Finland and Denmark are examples.

Suggested readings

- Danziger, J. N., & Smith, C. A. (2016). *Understanding the political world: A comparative introduction to political science*. Boston :Pearson, pp. 199-225.

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