This is about “exclusive”

2000110002 Kim, Seulgee
2000110004 Song Il-doo
2000110012 Lim Keun-hyuck
2000110018 Kang Youn-il
2001110101 Kim Wonjoong

Free Market Economy

1. The meaning of free market economy
   - Free market economy, economic system in which individuals, rather than government, make the majority of decisions regarding economic activities and transactions.

2. The history of free market economy
   - The origin of the free market system; The free market system economy had its origin in Europe in the 13th century, toward the close of the feudal era. The inclination toward trade and exchange, which was strongly suppressed by the medieval churches, was stimulated by the series of Crusades that absorbed the energies of much Europe from the 11th century to the 13th century. In northern Italy and northern Germany, many cities which were independent from the feudal system, had shown the primitive characteristics of the free market system.

   - The Commercial Revolution: In 15th and 16th century, after the exploration of new land in America, enormous amount of gold and resources flew into Europe. So there was a great impetus to business and trade. This era is called the age of Commercial Revolution. But still the central focus remained on the exchange of goods rather than on their productions.

   - Mercantilism: From the 15th to 18th century, European economic system not only took on a commercial flavor but also developed in a special direction of Mercantilism. In Mercantilism, the basic purpose of economic policy was to strengthen the national state and to further its aim. So therefore the fundamental focus of Mercantilism was centered on the self-interest of the sovereign, not on the self-interest of individuals. Though there was a remarkable development in Commercialism and business, still the free atmosphere of economic activity was not established yet.

   - The beginning of the free market system

     In the latter half of the 18th century, two theories of free economic activities appeared. The first one was the Physiocrats in France, and the second was Adam Smith.

     A. Physiocrats

     Physiocrats in the term applied to a school of economic thought that suggested the existence of a natural order in economics, one that does not require direction from the state for people to be prosperous. According to Francis Quesnay's Tableau, only the agricultural classes are capable of producing a surplus or net product. Other activities, such as manufacturing, were regarded as essentially sterile, because they did not produce new wealth but simply transformed or circulated the output of the productive class. This aspect of Physiocrats was turned against Mercantilism. If industry did not create wealth, then it was futile for the state to try to enhance society's wealth by a detailed regulation and direction of economic activities.

     B. Adam Smith

     Like Physiocrats, Smith tried to show the existence of a natural economic order, one that would function more efficiently if the state played a highly limited role. According to Smith, individual acting in their own economic self-interest will maximize the economic situation of society as a whole, as if guided by an "invisible hand." Ina free-market economy, the government's function is limited to providing what are known as "public goods" and performing a regulatory role in certain situations.

- The heyday of free market economy and its side effects: With a remarkable development in the technology of manufacturing, so called Industrial revolution, and also through the civil revolutions, the free market economy met its heyday in the 18th century. Without any strong regulations from the government and also with advanced manufacturing system of industrialization, European nations had earned enormous capitals. But also there were many side effects of the free economic system. Because of the gap between the bourgeois and the proletariat, Communism, a new theory of economy by Karl Mark, had flourished throughout the whole Europe and because of the lack of the government regulations, the problem of lacking public goods and the problems of pollution and the cycle of "boom and bust" had appeared. So at last in the 1930s, the whole world met the Great Depression.

- The remedy for the Great Depression; The Mixed Economy VS Communism:

To survive from the Great Depression, the European nations had adopted a new model of economy. In the western Europe including the U.S.A., they had adopted the Mixed Economy. It means that on the basis of the free market system, the government controls some vital industries and process and other economic factors in a certain level while guaranteed the welfare of people. In the eastern Europe including USSR, they had adopted Communism. Communism is an economic system, which does not admit the private property and makes all the properties the government owned. And the whole economic activities are supposed to be controlled by the government's plan. Tough there is some difference of degree in the government interference, through those systems, European nations except some Fascist nations, succeeded to survive from the Great Depression.

- The Oil Shock and Neo-Liberalism

The Mixed Economy also met its limit to substitute the operation of market through the Oil Shock and also there is a movement to return to the 18th century's Laissez-Faire, called Neo-Liberalism.

3. Advantages of free market system
   - It is the most efficient system for allocation of resources and labors and capitals.
   - The system can maximize the well-being of the whole nation and also the national wealth.
   - The freedom of economic activities in the free market system will lead to the freedom of the political freedom.

4. Disadvantages of free market system
   - There is a big possibility of appearance of monopoly economy or oligopoly economy, which are quite negative on the sound development of industry.
   - There is a problem of the shortage of public goods, which become efficient when produced or operated by the government.
   - The free market economy cannot smoothly adjust to the economic cycle of "boom and bust".
   - Problems in environment and corruptions in the economic market.
   - The widen gap between the bourgeois and the proletariat, which can hurt the stability of the whole society.

Market Failure

The equilibrium of supply and demand maximizes the sum of consumer and producer surplus. That is, the invisible hand of the marketplace leads buyers and sellers to allocate resources efficiently. Nonetheless, for various reasons, the invisible hand sometimes does not work. Economists use the term market failure to refer to a situation in which the market on its own fails to allocate resources efficiently.

☞Three general categories of market failures

1. Market power

Market power refers to the ability of a single economic actor (or a small group of actors) to have a substantial influence on market prices.

When firms have market power they tend to cut back production in order to drive up prices and increase profits. This results in too few goods being produced in noncompetitive markets and too many goods being produced in competitive markets. It also means that income is concentrated in the hands of those who have market power at the expense of those who do not.

2. **Externality**

An externality is the impact of one person's actions on the well-being of a bystander. The decisions of buyers and sellers sometimes affect people who are not participants in the market at all. Pollution is the classic example of market outcome that affects people not in the market. Such side effects, called externalities, cause welfare in a market to depend on more than just the value to the buyers and the costs of the sellers. Because buyers and sellers do not take these side effects into account when deciding how much to consume and produce, the equilibrium in a market can be inefficient from the standpoint of society as a whole.

3. **Public goods**

Public goods constitute the classic justification for government provision. They are those products and services which either would not exist at all without state intervention or of which too little would be produced and consumed.

Public goods are neither rival nor excludable. Because people are not charged for their use of the public good, they have and incentive to free ride when the good is provided privately. Therefore, governments provide public goods, making their decision about the quantity based on cost-benefit analysis.

1. Definition of Public Goods

Public goods is a word opposed to private goods, a wealth or property that is generally supplied to public association or a corporation because of some unique specialty that the property possesses.

One can divided public goods into two broad parts, one is pure public goods, which includes such goods as National defense, law, police and broadcasts, the other is local public goods, which includes fire department, parks, and highways.

2. Unique Characteristics of Public Goods

Basically, a public goods is something where everyone can use any part of the goods, and no one can be excluded from using it.

Let's take an example, a police station that provides security to one suburb. Because one family receives protection, it does not mean that other families cannot receive protection. All of the suburb may use the useful good, or service called protection and secrecy. This characteristic is called **none-rivalry**. Also, imagine that each family has to pay a certain amount of money for the protection it enjoys. Even though a certain family does not pay this agreed-upon fee, the police cannot really exclude that family from the service it gives. This characteristic is called **non-excludablity**.

Since the real focus of this presentation is on non-excludablity, let us have a closer look into it.

3. Non-excludablity of Public Goods

Private goods is something that fulfills a private demand, and in the case of this, only the person who has paid for the corresponding service or goods may enjoy the benefits, and the ones who has not paid is excluded. In other words, in consumption, the principle of exclusion is applied, and is supplied by the market.

On the other hand, a public good is signified mainly by its non-excludablity. That is, when a public good is supplied to an individual or a group, the benefits of the service or the good cannot be denied to other individuals or groups. Even if they can be excluded, it would require much effort and money.

For example, AFKN is a broadcast aimed at American forces in Korea, but for any native Korean who wants to consume it, all they have to do is switch the channel. Of course, they may install a cable so that only American forces can watch it, but this would cost much, and take a lot of effort.

As seen in the above example, no one would want to, or neede to pay the price for a public good, and everyone would become a "free rider." So, for private corporations that aims at maximum profit, they have no reason to produce a public good, and this in turn creates a market failure since there aren't enough public goods being produced to meet the demands of the society, and will require the intervention of the government.

Since many people can consume a public good at a same time, the consumption of each individual is equal to that of production, but the production of a private good is made up of sum of each individual's consumption.