

Good Capitalism, Bad Capitalism

Discussion Q's

- What drives economic growth and what role does entrepreneurialism play?
- What are the different types of capitalism identified by the authors? What are their relative strengths and weaknesses?
- What factors are needed to keep economies at the technological frontier growing?
- What can and should be done to help less developed economies?
- Why are 'big firm' economies like Japan and Germany seem to be lagging behind these days? What can be done to fix them?
- What is the optimal structure for economic growth? How can the United States maximize its potential in the 21st century?

Types of Capitalism

1. State-Guided Capitalism
2. Oligarchic Capitalism
3. Big Firm Capitalism
4. Entrepreneurial Capitalism

State-Guided Capitalism:

Traits:

- Government rather than private investors play a major role in determining which industries grow
- Ownership/control of banks/financing
- Administrative guidance and industrial policies (‘picking winners’)
- Producer-oriented

Strengths:

- Record of success in East Asia
- Helps economies to ‘catch up’, especially via export-led growth

Weaknesses:

- Believing that state guidance will work forever
- Excessive investment
- Picking the wrong winners and losers
- Susceptibility to corruption
- Difficulty ‘pulling the plug’ and redirecting government resources

Oligarchic Capitalism:

Traits:

- Government policies designed to promote the interests of the wealthy elite
- Economies based on natural resources
- Corruption
- Extensive informal economy (lack of property rights)

Strengths:

- None (unless you happen to be part of the elite!)

Weaknesses:

- Low growth (about grabbing spoils, not expanding 'economic pie')
- Corruption discouraging entrepreneurial activity
- Economic inequality
- Political instability

Big-Firm Capitalism:

Traits:

- Economic systems dominated by large companies
- Disconnected ownership via shareholding
- Professional managers

Strengths:

- Stable profits provide foundations for incremental innovations (e.g., Honda & Toyota)
- Provide cost-effective means for radical innovations by smaller entrepreneurs to become mass market products

Weaknesses:

- Oligopolistic markets decrease competition, increase prices
- Stable markets of big firms reduces incentives to radically innovate themselves
- Encourages labor market rigidity (people wanting stable jobs with big firms, e.g., Western Europe)
- May focus on rent-seeking from government instead

Entrepreneurial Capitalism:

Traits:

- Large number of innovative entrepreneurs (individuals or new firms)
- Relatively free (unplanned) markets that encourage experimentation

Strengths:

- Promoting innovations yields ‘first mover’ rewards
- Keeps economies on the ‘technological frontier’ (‘creative destruction’)

Weaknesses:

- Disruptive and unstable (‘creative destruction’)
- Creating new winners means creating new losers too
- Losers may seek political protection (e.g., backlash against globalization)

What factors are needed to keep economies at the technological frontier growing?

Four key conditions:

1. Ease of starting a business
 - (a) business registration
 - (b) bankruptcy protection
 - (c) access to finance

2. Rewards for Productive Entrepreneurial Activity
 - (a) rule of law, property, and contract rights
 - (b) avoiding onerous taxation (minimize disincentives)
 - (c) proper regulation/deregulation
 - (d) rewarding new ideas
 - (e) government supported R&D (basic scientific research)
 - (f) commercializing university inventions
 - (g) rewarding imitation

3. Avoiding Disincentives for Unproductive Activity

4. Keeping the Winners on their Toes; Playing the 'Red Queen Game'

***What is the optimal structure for economic growth?
How can the United States maximize its potential in
the 21st century?***

(1) Provide incentives for productive entrepreneurship

- Removing impediments to starting a productive enterprise
- Alter tax system to encourage investment (e.g., consumption tax)
- Reduce financial reporting requirements of Sarbanes-Oxley
- Review patent system (i.e., move to *first to file*)

(2) Disincentives for unproductive entrepreneurship

- Avoiding misuse of antitrust
- Reigning in frivolous lawsuits

(3) Encouraging competition and innovation

- Encourage joint ventures/mergers in high-tech areas
- Open (economic) borders (positive sum game)
- Facilitate the transfer of foreign technology (e.g., immigration)
- Rework stock options so as to promote innovation
- Encouraging the commercialization of university-based research
- Maintain a well-trained workforce