Economic Systems

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Abstract

Governments worldwide employ various systems to coordinate economic activities. These systems are networks of rules that structure interactions between economic agents and the environment. Governments use them to organize the distribution and exchange of resources, wealth, goods, and services. However, the type of system (capitalism, socialism, communism, etc.) seldom determines a country's success. Rather, the administrative capacity, ethical standards, efficiency, and fairness of the officers who run political and economic systems determine a country's success. Properly allocating citizens to production and justly distributing products among them are essential to optimizing a country's economic system.

Alchian and Allen (1977) noted that "societies have prospered despite almost universal ignorance of economic analysis."

Keywords: Economic Systems, Administrative Capacity, Socialism, Capitalism, and Communism.

Introduction

Countries organize their resources through economic systems, the methodologies or rules that govern the production, distribution, and consumption of goods and services, along with political and banking systems. Countries often use different political and economic systems to set rules and produce and distribute goods and services. However, political and economic systems alone do not guarantee optimal resource use, a prosperous economy, or full employment. Many democratic, communist, and socialist governments are dysfunctional.

Successful political and economic systems rely on the effective administrative capacity of public and private officials to run the machinery of political and economic systems, including running effective central banks to control inflation, ensure credit availability and maximum employment, as well as facilitating the establishment of robust educational institutions, universal healthcare, and financial institutions for saving, borrowing, and consumption.

We use the term administrative capacity broadly across many contexts (Misener & Doherty, 2009). Here, it entails running the machinery of political and economic systems and translating political and collective will into actions through management and implementation (Farazmand, 2009). Administrative capacity is also the aggregation of the individual capacities of civil and private servants, as these capacities ultimately determine outputs, service delivery (Mentz, 1997; North, 1992), and job creation.

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Capacity is the ability to perform functions, solve problems, set goals, and achieve objectives (Milio, 2007; Fukuda-Parr et al., 2002; Janicke, 2001). Thus, it is a set of attributes embodied in efficient institutions that enables them to accomplish their missions effectively (Misener & Doherty, 2009).

A lack of administrative capacity leads to mismanagement of political, economic, and organizational systems, low productivity, and high unemployment. Productivity is a crucial component of economic activity (Just, Hueth, and Schmitz, 1982). Economic activities create and distribute the wealth that individuals, households, and society use to achieve different social and material goals (Duhaime, 2004).

Optimizing economic systems determines how countries maximize resources and create employment, universal healthcare, educational attainment, and wealth for their citizens. Most citizens seek involvement and rewards for their productive contributions to society. Unfortunately, not all citizens have access to education, vocational training, employment, and healthcare, which often limits their ability to contribute to society.

Types of Economic Systems

The Corporate Finance Institute (CFI) defines economic systems as the ways societies or governments organize and distribute available resources, goods, and services across geographic regions or countries. Generally, economists recognize four basic types of economic systems: traditional, command, market, and mixed. Amadeo (2019) noted that economists and anthropologists believe that all economies started as traditional economies. Thus, traditional economies are expected to evolve into market, command, or mixed economies over time. However, which economic system best addresses scarcity remains unresolved (Shmoop Editorial Team, 2008). Nevertheless, China's economic system has lifted more than 800 million people out of poverty (World Bank Group, 2022).

The traditional economic system is an ancient form of economic organization that remains dominant worldwide. It is also present in distressed rural areas and central cities in the United States of America (USA). Traditional economies often lack access to advanced technologies and healthcare. In command economies, a small elite centralizes power. However, if command economies are capable and ethical, they can allocate resources to citizens. Gaddafi's command economy was becoming the fifth-largest economy in Africa (Gyani, 2023). Gyani noted that Gaddafi introduced and subsidized educational policies; as a result, the poorest Libyans gained access to education, per capita income grew, and public healthcare was free. Nonetheless, elites in command of market economies often distribute most goods and services among themselves.

Capitalist governments argue that capitalism is grounded in a free-market economy. However, capitalist governments regulate trade (tariffs, and so on). Therefore, a capitalist system is not a truly free-market economy, except for a veneer of separation between government and business. A free-market economy can only exist under limited government control (Smith, 1776). However, government regulation can lead to corruption, such as bribery of public officials, and to money in politics, which some view as wealthy actors subjugating common citizens or as free speech (Kuhner, 2007). Mixed economies combine elements of command and market systems. The USA

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is a mixed economy with regulated markets and is therefore subject to bribery, favoritism, and control by the wealthy.

In a free-market economy, the market regulates prices. Therefore, in a truly free-market economy, there are no government intervention, taxes, or regulations. However, a truly free-market economy cannot coordinate a natural defense plan and leaves vulnerable citizens without a safety net (Amadeo, 2019) because governments would have no revenue.

Economic subsystems, such as capitalism, fascism, socialism, democratic socialism, and communism, are generally poorly understood. Nonetheless, proponents and opponents alike believe that their preferred economic system is superior to all others, even when government officials are corrupt and seldom implement efficient economic systems.

Physical and financial wars also influence the success or failure of a country's economic system. Financial sanctions, tariffs, threats, and other shenanigans adversely affect targeted countries' ability to trade with the rest of the world (ROW) and, as a result, make their economic systems appear suboptimal. For instance, the USA has maintained a comprehensive trade embargo against Cuba since 1962 (The U.S. Department of State), which contributes to the poor performance of its economic system.

Economic System

An economic system refers to the coordination of economic activities. According to Dallago (2002), the network of "rules of the game" structures how economic actors interact with one another and with the environment; it organizes the distribution and exchange of a country's resources, goods, and services. From an economic perspective, an economic system regulates various economic issues, including the quantity of money in circulation, factors of production, the supply of capital, taxation, subsidies, foreign trade, the level of consumption, and so on.

Simon (1991) argued that until we can answer the question of the role of markets in connecting organizations and consumers, it is difficult to conclude on the relative efficiencies of different forms of ownership and control, or the comparative effectiveness of markets versus central planning.

Pham (2024) argued that in the West, many conflate socialism, communism, and Marxism and incorrectly treat them as interchangeable.

Capitalism

Capitalism is a free-market system characterized by private property rights in the production and consumption of goods and services (Alchian & Allen, 1977; Scott, 2006). Scott "defines capitalism as a system of indirect governance for economic relationships, where all markets exist within institutional frameworks that political authorities, i.e., governments, provide."

The standard definition of a market economy is that supply and demand determine the prices of goods and services, as in perfect competition. However, the economic virtues of markets exist only

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in the unrealistic models of neoclassical theory, not in real-world markets (Kotz, 2008), since perfect competition does not exist in the real world.

Additionally, markets often fail because of inefficient resource allocation. Governments that allow markets to operate without regulation or taxation cannot provide public goods or help the needy (Andreas, 2012); they also cannot reward corporations and the rich. Andreas noted that calling free markets good or bad is improper, since they are only a means of allocating resources among cooperating individuals.

In a capitalist economy, individuals with sufficient income can freely bid for goods and services; those without income cannot. Thus, the poor will struggle to afford healthcare, housing, food, education, and other necessities. Governments in unregulated (untaxed) markets cannot allocate goods and services, including public goods (roads, airports, and clearing waterways), to their citizens. Only benevolent governments that regulate markets can subsidize their citizens, and many call this type of support socialism when it targets the needy. When it subsidizes corporations and the wealthy, people call it job creation. Only the political authorities (the government) can widely redistribute resources to the most destitute and the rich. When catastrophes occur, capitalists, the wealthy, lack the capacity or desire to rescue citizens or themselves; it is too costly.

Employers, whether private or government, own capital and make decisions regarding productive private and public assets, including manufacturing, education, healthcare, utilities, roads, parks, airports, bridges, federal lands and waters, banks, the military, police, and so on. Thus, like communist and socialist governments, capitalist governments own property and employ workers. Moreover, all governments provide institutional frameworks and regulations for markets (Scott, 2006), including discriminatory policies, barriers to entry, and favoritism.

Governments also own and control central banks and use them to manipulate their economies' monetary systems. Central banks, like the Federal Reserve (the Fed), use three tools to manage the money supply: the discount rate, reserve requirements, and open market operations (Walbaum, 2012). Central banks' tools and regulations, set by political authorities (Congress and the executive branch), constitute a form of government-macroeconomic planning and control over the economy. For instance, when the Federal Reserve removes money from circulation, it slows economic activity. Conversely, when it puts money into circulation, it accelerates the economy. Additionally, capitalists, like communist and socialist governments, use regulations to socialize costs and use taxation or subsidies to redistribute income, particularly to the wealthy.

Beckert and Rockman (2016), in their introduction to "Slavery's Capitalism: A New History of American Economic Development," noted that the brutal system of enslavement was indispensable to the economic development of the USA. Thus, between the American Revolution and the Civil War, USA capitalists kidnapped Africans and forcibly took their labor without compensating them. Enslaved African labor, along with native lands, made rice and indigo production profitable (Walton & Shepherd, 1979). Walton and Shepherd noted that white colonists passed laws to reduce Africans from humans to mere property. In 1705, the slave code defined enslaved Africans as nonhuman and as a form of property. Therefore, capitalism has always exploited workers from its inception.

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Under contemporary capitalism, workers and capitalists enter contracts in which they exchange labor power for wages, with capitalists retaining the products of workers' labor (Roemer, 2008). Thus, most producers are employees of firms rather than owners (Simon, 1991). Roemer noted that because capital is scarce relative to the available labor supply, those with access to capital capture the workers' surplus, while workers receive only wages. He also argued that an abundance of unemployed workers benefits capitalists because workers must bid for the "privilege" of using their labor power on privately and government-owned productive assets. Excess labor supply depresses wages and increases capitalists' profits.

Unemployment occurs when the economy is not operating at full employment (capacity). However, many mainstream economists believe that true full employment is neither possible nor desirable (Tcherneva, 2014). Tcherneva argued that “It is not possible due to automation, outsourcing, and other structural shifts in the economy that prevent the market from creating jobs for all who want them.” Moreover, she noted that we cannot count on the private sector to guarantee full employment even in good times.

Economists such as Malcolm Sawyer (2003) argued that the government should be prepared to provide work to anyone who seeks paid employment but cannot otherwise find it. This mirrors the central bank's willingness to provide reserves to the banking system during market failures. Unfortunately, conservative politicians do not see unemployment as a societal problem.

Fascism and Nazis

Fascism and Nazism were predominant political ideologies in the early 20th century and were very similar; the concept of race was the central tenet of Nazism. However, it was not central to Fascism. The term Fascism derives from the Italian fascio or the Latin fasces; fascio and fasces denote a bundle, referring to organized political groups (Layton, 2006; Waxman, 2019).

Under the leadership of Benito Mussolini, militants attacked, beat, and killed fellow Italians (Waxman, 2019). Waxman noted that Mussolini directed the brutality in Ethiopia and allied with Hitler to persecute Italy’s Jewish population, as well as other populations. Renton (1999) noted that "Capitalism generates the myths of racism and elitism, which fascists use for themselves " (p. 35).

Fascism is an authoritarian system that promotes nationalism at all costs (Szalay, 2017); it is an aggressive nationalism and imperialism with the domination of the economy by the state. For Szalay, Fascism requires some primary allegiances to the nation, to national grandeur, and to a master race or group. He also indicated that one element of Fascism is a collaboration with capitalists and the conservative elites. Thus, Renton (1999) argued that if Fascism is a recurrent feature of capitalism, then Fascism is not just a historical aberration, but a living and dangerous tradition which would repeat the crimes of the past.

Colin Sparks (1980) noted that for the white working class, racism and Fascism offer economic solutions to inadequate housing, unemployment, and falling living standards. He argued that materialist pressures lead some whites towards racism and Fascism and claimed that to destroy these tendencies, it is necessary to remove the drive for materialism or to raise the standard of

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living. However, racism is also prevalent among many well-to-do whites. Therefore, racism is not about economics; rather, it is about ingrained irrational hatred towards non-white neighbors, a rejection of the second greatest commandment, and hence the first greatest commandment. Racists do not love their neighbors and therefore do not love God.

For fascists, groups that impeded their views of national unity had to violently disappear (Waxman, 2019). Waxman noted that Mussolini used colonialism to abuse people of color and that the fear of white decline was a component of the abuse. Fascists obtained power by killing and intimidating the Socialist Party; landowners and business people supported the suppression of socialism, allowing Mussolini to gain power.

Yad Vashem - The World Holocaust Remembrance Center - defines Nazism as a German political movement led by Adolf Hitler. It noted that in 1919 in Munich, Germans founded an antisemitic right-wing political party called the German Workers' Party, which adopted the combined "national-social" ideology. In 1920, the party added "National Socialist" to its name, becoming the National Socialist German Workers' Party. Adolf Hitler became the leader, or Führer. Yad Vashem also noted that "Nazism brought together the ideas of racial antisemitism (that Jews were inferior by virtue of their race or genetic makeup) …"

In 1924, Adolf Hitler claimed that "Propaganda is truly a terrible weapon in the hands of an expert (un.org)." UN.org noted that propaganda is biased information designed to shape public opinion and behavior; it uses truths, half-truths, or lies; selectively omits information; simplifies complex issues or ideas; plays on emotions or advertises a cause; attacks opponents; and targets desired audiences. Thus, propaganda aims to divide a nation's social fabric. Today, some governments use artificial intelligence to distort images.

The Nazi Party carried out a deliberate, calculated attack on European Jewry; it targeted Jews as the main enemy, killing six million Jewish men, women, and children by the time the war ended in 1945 (Meinecke Jr., Zapruder, Kaiser, Glassman, and Hart, 2007).

Contemporary economic analyses of privatization do not account for the National Socialist (Nazi) Party's privatization policies in Germany (Bel, 2009). Bel notes that the Nazi government opposed widespread state ownership of firms, similar to the position of capitalist governments in the West today. The Nazi drive for privatization aimed to secure increased political support and, in particular, to achieve a combination of increased revenue and expenditure relief for the German Treasury (Bel).

These two ideologies, Nazism and Fascism, had many commonalities, and they were extreme right-wing political ideologies with cult-like leadership and the use of violence. Nazism is a form of Fascism with a stringent concept of white racial superiority.

In Germany, there was a fascination with Hitler, and they consistently described him as given by God (Koehne, 2012). Koehne (2014) noted that a 1935 tapestry made by ordinary Christian women combined the Lord's Prayer, a church, and the swastika flag, in a genuine belief that these three should be interwoven. There was a bond between the Christian faith and the National Socialists among those who wove the tapestry.

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However, some, such as Broszat, argued that the Nazis systematically concealed the "Final Solution" from an unperceiving German population (Friedländer, 2009). Friedländer questioned everyday life in the Third Reich before the onset of the "Final Solution" by showing the extraordinary impact of the regime's anti-Jewish propaganda on the national-racial community and the awareness of the open persecution of the Jews. We see a similar persecution of Hispanics under the second Trump administration.

Communism

According to Engels (1847), "Communism is the doctrine of the conditions of the liberation of the proletariat." He classified the proletariat as the class of individuals in society who live entirely by selling their labor and do not profit from capital. Profit is the difference between revenue and cost.

Communism is an economic and political system that aims to distribute resources according to need, with the government controlling all resources.

Bandura and Kosta (2018) stated that "Communism began in Russia in 1917 and spread through Eastern and Central Europe, China, Vietnam, Cambodia, parts of Africa, Afghanistan, Korea, and Cuba." They estimated that communism killed over 100 million people. For Haque (2018), the death toll was awful. However, researchers, to be credible, must present both sides of the "facts." Therefore, Haque noted that 13 million kidnapped and enslaved human beings were sold to the "New World." He also noted that "In the United States, by 1860, just 400,000 North American slaves had become 4 million new ones, born into slavery." That is 17 million enslaved Africans under capitalism.

Haque (2018) also noted that 100 years later, due to capitalism, a global depression emerged, and capitalism poured the fuel of fascism all over the world, in nations like Germany and Italy that had high debts. It only took a handful of demagogues to set the world alight. He conservatively estimated the death toll resulting from World War II to be about 120 million people. Therefore, if communism killed 100 million people, capitalism indeed killed more. In Congo, for instance, Leopold II of Belgium assassinated more than 15 million Congolese (Bates, 1999).

Pure communism is an economic and social system in which a classless society, rather than individual citizens, collectively owns all (or nearly all) property and resources. It is based on the 1848 publication "Communist Manifesto" by two German political philosophers, Karl Marx and his close associate Friedrich Engels (Philosophy.Institute; Wall, 2011). Wall noted that communism held that all land and capital should be commonly owned and that the state's coercive power would wither away. It would regulate social relations on the fairest principle of all: ability and need. He also argued that no country has ever been genuinely communist. Marx believed that individuals' pursuit of self-interest would lead to class struggle, increased income inequality, underutilization of resources, and business cycles (KIM, 2012).

Before Marx and Engels, followers of Christ shared everything. Acts 2:44-45 (KJV) states, "**44** All the believers were together and had everything in common. **45** They sold property and possessions to give to anyone who had need." Acts 4:32 (NIV) states, "All the believers were one in heart and mind. No one claimed that any of their possessions was their own, but they shared everything they

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had." Similarly, in Acts, the disciples' economic system was characterized by collective ownership of resources, much like pure communism. Still, in Acts 5:1-2, Ananias and Sapphira chiseled from their own contributions, showing the tension between collective ownership and self-interest.

In the parable of the talents in Matthew 25:14-30, Jesus gives the example of a master who had eight talents and, before traveling abroad, distributed them to his servants, expecting them to invest the talents while he was away. One servant received five talents, another two, and another one (Matt. 25:15). Although they received different amounts, the master expected them to increase their talents. He expected them to serve their own interests by not shirking their investment responsibilities. The parable says the unprofitable servant buried the talent and did not return a profit to his master. Thus, he failed to consider the master's interests. So, the master took the talent away and cast him out into outer darkness.

The parable of the talents refers to using our abilities for the prosperity of the Kingdom of God, such as caring for the environment, increasing productivity, looking out for our neighbors, feeding the hungry, visiting the imprisoned, helping the sick, and so on.

Communism, as often practiced, lacks incentives, leading to shirking responsibilities and the free-rider problem. Typically, people expect to receive benefits without contributing to societal welfare. Thus, the central concern of communism and socialism is the principal-agent problem: how communist and socialist states (principals) can motivate managers and employees (agents) to act as profit maximizers, given the difficulties of monitoring agents (Sappington, 1991).

Without ownership of capital, it is harder to design incentives for the efficient use of state-owned capital (Layard & Walters, 1978). Sappington (1991) argued that if the principal shared the agents' skills and knowledge, she could induce the agents to behave exactly as she would. Thus, communist countries with strong administrative capacity can mitigate agents' disincentive behavior. However, government officials' administrative capacity, whether communist or not, is often lacking.

According to Greaves (1991), "von Mises believed that communism, or socialism, could not succeed, von Mises wrote in 1920, because it had abolished free markets so that officials had no market prices to guide them in planning production." Lange (1936), however, disputed this argument regarding socialism. He argued that public ownership of the means of production does not preclude markets for the efficient exchange of capital goods. China's economic success suggests that a well-managed mixed economy (capitalism, socialism, and communism) can succeed by relying on market prices to guide it and on wage differentials to address free-rider and principal-agent problems.

Thus, China and European socialist countries have markets that facilitate efficient exchange. Even in capitalist economies, some markets are inefficient. For instance, Golimowsky (2008) found that the Pentagon overspent on washers.

No industrial society has achieved communism, despite attempts (Phan, 2024; Wall, 2011), because, wherever it has been implemented, it has not fully abolished private property or class distinctions as Marx and Engels (1848) called for.

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Socialism

Socialism is a political and economic theory of social organization that advocates community ownership or regulation of the means of production, distribution, and exchange*;* the means of production are socialized (von Mises). Unfortunately, multiple definitions of socialism make it difficult to understand. Both communism and socialism emerged in response to the Industrial Revolution and to workers' struggles to reorganize society (Pruitt, 2019). Socialism differs from communism in that it is a theory of social organization; it advocates distributing wealth according to effort and holds that citizens own the means of production. People manage resources, and private property and capitalism coexist.

The London Company established the Jamestown colony in 1607. It initially operated collectively but performed poorly because it disincentivized work and innovation (Walton & Shepherd, 1979). Innovation, however, is not inherent to capitalism. Cuba's pharmaceutical innovations showed the capacity to innovate within a communist system (Kotz, 2008), even while under a Western embargo. Additionally, Reynolds (1998) argued that the collapse of the Soviet Union and its former captive states in Eastern Europe heavily influenced contemporary economists and the public's view of the historical experiment of socialism (Surbhi, 2018).

Anti-socialists argue that central planning is ineffective. However, all capitalist organizations use some form of central planning and coordination, including capitalist governments. In Japan, the Ministry of International Trade and Industry (MITI), established in 1949, steered economic and social development through centralized planning. The MITI was one of the most powerful agencies in the Japanese government, and its mission was to coordinate trade policy (Howell, 2006). It also oversaw domestic industries and businesses. Thus, central planning works; any household, institution, or organization that does not operate under some form of central planning is dysfunctional.

Democratic socialism

According to the World Population Review, "Democratic socialism describes a socialist economy where production and wealth are collectively owned, but the country has a democratic system of government. The goal of democratic socialism is to achieve socialist goals of equality while opposing socialist ideologies. Democratic socialism is opposed to the Soviet economic model, command economies, and authoritarian governance."

Democratic socialism is often difficult to define because advocates and scholars offer differing, often radical, definitions. However, its central tenet is to promote a democratically governed economy and society that meet public needs rather than generate profits for a few. The World Population Review describes a socialist economy as one characterized by collective ownership of the means of production and wealth, as well as a democratic system of government.

Democratic socialists believe achieving a just society requires radically transforming many government and economic structures through greater economic and social democracy, allowing ordinary citizens to participate in decisions that affect their lives (Home | Northern Illinois DSA). Democratic Socialism advocates democratic employee ownership and administration of the means

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of production and the distribution of goods, such as employee cooperatives, and opposes command-and-control authoritarian governance.

Many countries, including the United States of America, combine elements of capitalism and socialism. However, they differ in how much they lean toward capitalism and socialism. For instance, Scandinavian countries, such as Denmark, Norway, and Sweden, are market economies with a balanced mix of socialist policies and comprehensive social safety nets. Thus, countries can simultaneously be capitalist and socialist. However, some countries emphasize socialism more than capitalism, which democratic socialism represents. For instance, Sweden exhibits greater socialism than most countries because it has more social programs.

Society's Economic Challenge

All societies have a variety of resources at their disposal- land, capital, and the time of their citizens- that they can use to generate societal benefits (Layard & Walters, 1978). Modern societies also have monetary authorities (central banks) and financial institutions (banks, insurance companies, credit unions, etc.) for saving and credit. Credit expansion increases the money supply (Dornbusch & Fisher, 1978; Ellis, 2009; Xiong et al., 2016), thereby increasing demand for goods and services. Productive societies use credit from central banks and financial institutions to build productive capacity and allocate citizens to products, thereby determining production techniques, quantities, and quality, as well as product distribution among citizens (wages).

The challenge of economic systems is to effectively allocate credit (loans) across communities to create profitable local production and employment. That is, how best to allocate local citizens to local products and services (jobs) and how to equitably distribute products and services among citizens (Layard & Walters, 1978). However, allocation and distribution schemes are seldom, if ever, egalitarian or efficient; not everyone benefits.

Many government officials administering economic systems are less concerned about the fair distribution of economic outputs, as reflected by discrimination, sexism, wage stagnation, non-livable minimum wages, nepotism, corruption, and so on. Furthermore, they allow high remuneration for top corporate officers and a low (non-living) minimum wage for low-wage earners. Many government officials lack administrative capacity.

Conservative economists, politicians, and voters argue that equity (fairness) and efficiency are in trade-off, and that subsidies to low-income individuals create disincentives to work. They do not argue the same for more significant subsidies to corporations, farmers, oil extractors, oppressive countries, and so on.

We cannot eliminate poverty. It is an intractable societal problem stemming from differences in individuals' abilities, opportunities, and motivations. However, societies can manage poverty through adequate social programs, including free education, job creation, housing expansion, and universal healthcare. Deuteronomy 15:11 encourages us to support the poor: "For there will never cease to be poor in the land; that is why I am commanding you to open wide your hand to your brother and to the poor and needy in your land." Likewise, Jesus said, "The poor you will always have with you, but you will not always have Me (Matt. 26:11). So, the Bible asserts that the poor

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will always exist and commands us to help the poor. Unfortunately, many who call themselves Christians despise the poor due to their lack of understanding of the teachings of Christ.

Many economic systems rest on extreme human selfishness and fail to consider low-income people. The father of capitalism, Adam Smith (1776), claimed: “It is not from the benevolence of the butcher, the brewer, or the baker that we expect our dinner, but from their regard to their own interest.” KIM (2012) argued that “Adam Smith regarded self-interest as love to oneself without harming others, whereas selfishness refers to self-love that undermines the interests of others.” However, selfishness is not inherent to capitalism; many political and private officials who manage other economic systems are also greedy and uncaring. All economic systems can feature these undesirable human behaviors.

Socialization of Costs

Most economic systems privatize profits and socialize certain business expenses, such as harmful business externalities, fertilizer runoff into streams and oceans, air pollution, and the injection of chemicals into the earth or aquifers. They also socialize education, roads, air and seaports, the police and the military, subsidies to foreign governments, business bailouts, and so on. Capitalist governments treat business earnings as shareholders' rightful property, while treating some business losses as a societal responsibility (Kenton, 2019). The socialization of costs for the wealthy is evident in taxpayer subsidies to businesses, such as banks and the automobile industry; bailouts for farmers; tax giveaways to the rich; and so on.

Many elected officials prefer to funnel taxpayer funds to large corporations rather than to citizens in need. Dr. M. L. King, Jr. (1968), in his Minister to the Valley speech, said, “Whenever the government provides opportunities and privileges for white people and rich people, they call it ‘subsidized’; when they do it for Negro and poor people, they call it ‘welfare’.” Thus, the United States of America has a society with free enterprise for the poor and socialism for the rich (King, 1968; Gillespie, 2008; Adams, 2008; Roubini, 2008). Thus, socializing corporate losses through government subsidies does not carry the same negative connotations for the public as subsidizing low-income people.

According to Abeel (2013), Gore Vidal claimed that "The genius of our ruling class is that it has kept a majority of the people from ever questioning the inequity of a system where most people drudge along paying heavy taxes for which they get nothing in return." CNBC reported that 100 Fortune 500 companies paid no federal income taxes in 2018; see the Institute on Taxation and Economic Policy report of December 16, 2019.

Business externalities are sources of market failure. They occur when consumption or production decisions of one agent affect the consumption or production opportunities open to others (Layard & Walters, 1978). Their effects do not operate through the price system (Layard & Walters; Hirshleifer, 1980); if they did, many businesses' production costs would exceed the prices they can charge for their products.

Economic Optimality

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The critical elements of economic optimality are efficiency in consumption, production, and the product mix, as well as the optimal allocation of citizens to the production process and the "equitable" distribution of the resources produced among citizens (Layard & Walters, 1978). Over time, a skewed distribution of resources toward the rich leads to increased borrowing by the poor and the middle class for consumption; if they cannot borrow, consumption and gross domestic product will decline. High levels of personal credit can potentially cause inflation and, if individuals cannot borrow in the future, deflation, inventory accumulation, and layoffs- the typical boom-and-bust cycle. The term "equitable" is difficult to define and somewhat subjective. Nonetheless, we can define it as the minimum income necessary for all citizens to live; it is a matter of fairness, treating everyone equally.

Decision-makers in different countries prefer different economic systems for reasons of tradition rather than economic optimality. Because they often are not seeking societal optimality. Instead, they are seeking to optimize their own self-interest and that of corporations, with little or no regard for societal welfare. Therefore, many policymakers implement policies that are not socially desirable, do not make everyone better off, and fail to compensate losers. Hence, citizens should evaluate politicians' policy records before electing them to office and elect only those whose records or proposals maximize social welfare.

Moreover, many voters are partisans; even when a policy outcome benefits them, if the candidate is not affiliated with their party, they will find that candidate unacceptable (Ellis, 2016).

The challenge, however, is that principal-agent theory does not apply to government authorities. Once politicians (agents) are elected (hired by voters), most are not accountable to voters (the principals); the elected officials reverse the process and become the principals, treating voters as their agents. Principal-agent theory is about incentives (Sappington, 1991). In politics, the principals (voters) hire the agents (politicians) through the electoral process. However, voters seldom can motivate politicians to do what they want, even when they can monitor their actions. No expedient mechanism exists to remove politicians from office immediately when they fail to promote the public good, as in private industry.

The framers' institutional framework of the U.S. Constitution is a representative republic, not a democracy (Higgs, 2017). The word "representative" implies that public officeholders are agents of the people, not bosses. Elected officials serve the citizens, not the other way around. However, Higgs argued that no one could take the "representative" part of a representative republic seriously, and that is the problem.

If, however, the citizenry established a legal, contractual agreement with its political candidates specifying remuneration, performance, and conditions for dismissal, we could take the representative part of the Constitution seriously. Moreover, candidates (agents) could not make vague, uncorroborated promises to voters (principals).

Central Planning

Successful institutions/organizations use central planning to maximize output and profits. Layard and Walters (1978) indicated that a robust, centrally planned society aided by artificial intelligence

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(A.I.) could implement optimal solutions. They also stated that capitalism performs well under sweeping assumptions: perfect competition, no increasing returns to scale, no external technological effects, no market failures associated with uncertainty, and, finally, each consumer must be able to purchase the consumption bundle corresponding to the economy's welfare-maximizing configuration. Neoclassical economists make these unrealistic assumptions (Kotz, 2008).

As noted previously, Simon (1991) indicated that it is difficult to determine the relative efficiency of different forms of organizational ownership and control, or the comparative effectiveness of markets versus central planning.

Gallant (2019) noted that for perfect competition to exist, the following conditions must be present: (1) all firms sell an identical product, (2) all firms are price-takers, (3) all firms have a relatively small market share, (4) buyers know the nature of the product sold and the prices charged by each firm, and (5) freedom of entry and exit characterize the industry. Unfortunately, we rarely observe these five requirements together in any industry. Thus, perfect competition is rarely, if ever, observed in the real world (Gallant). However, many Western government officials adhere to the false mantra of perfect competition, even when many consumers cannot afford the consumption bundle associated with the economy's welfare-maximizing configuration.

Economic systems involve choices subject to constraints (Layers & Walters, 1978). However, many societal decisions made under any economic system are seldom optimal. For instance, many countries cannot assign the right people to production processes, whether in government, churches, manufacturing, educational institutions, and so on. Misallocation of factors of production cripple economic systems, businesses, and institutions. That is, when policymakers are incapable of, or not interested in, maximizing individuals' and organizations' comparative advantages, the operating economic system, whatever it may be, is unlikely to operate at optimal capacity. Many decision-makers allocate jobs based on friendship, likability, homogeneity, and racial and gender preferences. Thus, they hinder optimal outcomes.

The inability to place the right individuals in the right jobs restricts the techniques, quality, and quantity used to produce products and services. Favoritism undermines optimality; it often reduces administrative capacity and does not yield Pareto improvements, movements from an inferior to a superior state (Just, Hueth, and Schmitz, 1982). Societies should codify rules to achieve Pareto-improving states and reduce inequality.

In depressed areas, regardless of the economic system, policymakers rarely allocate resources, including citizens, to production and service processes, depriving those citizens of a living income and limiting their access to available goods and services. In the United States, these outcomes are evident in Appalachia, the southern states, and central cities, and they are also beginning to affect the middle class nationwide. In China, poverty is evident in rural areas, and in Russia, the poorest areas are in the south (d'Amora, 2015). The World Bank estimated that in 2023, 27 million Chinese

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people were lifted out of poverty using the $6.85/day (2017 Purchasing Power Parities (PPP)) poverty line, compared with approximately 50 million per year in 2018 and 2019.[1]

Therefore, decision-makers in any economic system do not appear to favor lifting neglected areas. One reason is that low-income people cannot buy public officials' attention. Depressed areas receive little investment in education and finance, which limits individuals' skill development and the creation and expansion of bank money.

Individual Well-Being

From an economic perspective, individuals' well-being depends on the income available for consumption (Hirshleifer, 1980). Furthermore, in regions without credit creation (i.e., borrowing), the economy's wealth is fixed at any point in time; if there is no production and only consumption, that wealth will diminish over time; therefore, when capital owners' wealth increases, workers' wealth decreases. Any decrease in workers' wealth adversely affects the consumption of goods and services by the middle class and people with low incomes, except if they can borrow from the owners of capital to make purchases.

Economic systems that are not ideally configured (optimal) will, over time, become unstable and widen the wealth gap between the rich and the poor, because most citizens' income will not be able to purchase all the goods and services produced. That is, in a competitive economy, wages equal the marginal revenue product of labor, which equals the selling price of the goods and services produced. However, because we do not operate under perfect competition, wages are less than the marginal revenue product, since that is the only way that owners of capital can make a profit. Thus, the aggregate selling price of goods and services produced will exceed aggregate wages. Hence, over time, wage earners will be unable to purchase all goods and services except through borrowing (bank credit) or savings.

However, when aggregate wages plus aggregate borrowing exceed the selling value of goods and services produced, consumers will bid up prices (inflation). The central bank will begin to restrict credit (remove money from circulation), inventories will accumulate, and production will slow, leading to employee layoffs—the classic boom-and-bust cycle.

Following Layard and Walters (1978), we assume a closed economy with two people, A and B, and two fixed factors of production: capital ($\bar{K}$) and labor ($\bar{L}$). At any point in time, community resources are fixed. We can use these factors to produce x (wheat) and y (fish). The capital allocated to producing x is K^x, and to producing y is K^y; likewise, the labor allocated to x is L^x, and to producing y is L^y. So, given the fixity of capital and labor in our closed economy, we have:

$$\bar{K} = K^x + K^y \qquad \bar{L} = L^x + L^y$$

So, the total amount of capital available is $\bar{K}$, and the total amount of labor is $\bar{L}$. The allocation of these factors of production generates outputs. Their production functions specify the maximum output the closed economy can produce. The production functions for x and y are:

[1] https://documents.worldbank.org/en/publication/documents-reports/documentdetail/099656501032511659

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$$x = x(K^x, L^x) \qquad y = \mathrm{y}(K^y, L^y)$$

Thus, society uses the limited amounts of $\bar{K}$ and $\bar{L}$ to produce wheat and fish; in a capitalist economy, their allocation across the production functions will depend on the demand from persons A and B for *x* and *y*. That is:

$$x = x^{\mathrm{A}} + x^{\mathrm{B}} \qquad y = y^{\mathrm{A}} + y^{\mathrm{B}}$$

We allocate the outputs x and y between the two citizens, A and B, according to their wealth (i.e., prices). They can demand x and y from their disposable income, accumulated savings, credit, government subsidies, or private gifts. So, without a safety net, the wealthier individual could purchase more, or all, of *x* and *y,* leaving nothing for the less wealthy (people in need).

The theory of choice posits that individuals prefer more to less, up to a point. Therefore, A and B's happiness depends on how much *x* and *y* they can afford. If they are altruistic, each will ensure the other's happiness; if they are envious or uncaring, the other's happiness is not a concern. We seldom see mass altruistic behaviors in capitalist economies; it is more prevalent in socialist economies.

Each citizen has what economists call a utility function, *U*, which represents their level of happiness or satisfaction:

$$U^{\mathrm{A}} = u^{\mathrm{A}}(x^{\mathrm{A}}, y^{\mathrm{A}}) \qquad U^{\mathrm{B}} = u^{\mathrm{B}}(x^{\mathrm{B}}, y^{\mathrm{B}})$$

In general, more of *x* and/or *y* leads to more happiness. Nonetheless, this simple example shows that every society has constraints and that an equitable distribution of resources is seldom possible under any economic system without government intervention. Equity, though, is subjective. However, we can maximize each citizen's utility, given their personal utility (or happiness) function. Likewise, governments can use redistribution schemes to improve opportunities and provide safety nets for disadvantaged and indigent citizens—for example, universal healthcare, free education, and subsidized housing.

Layard and Waters (1978) argued that the economy's configuration depends on personal judgment because citizens differ in how much they value equality versus efficiency. Equality is a contested concept in social and political thought (Arneson, 2013).

We can use mathematics to maximize the *social welfare function*, *W*:

$$\max W = W(u^{\mathrm{A}}, u^{\mathrm{B}})$$

Subject to the endowments, technology, and taste constraints, plus four (4) first-order conditions: efficiency in consumption, production, and product mix, and social justice.

A situation is efficient (Pareto-optimal) when it is impossible to make one person better off without making someone else worse off. Even when academics and policymakers design efficient economic systems, government authorities seldom apply them as intended due to human greed or inadequate administrative capacity.

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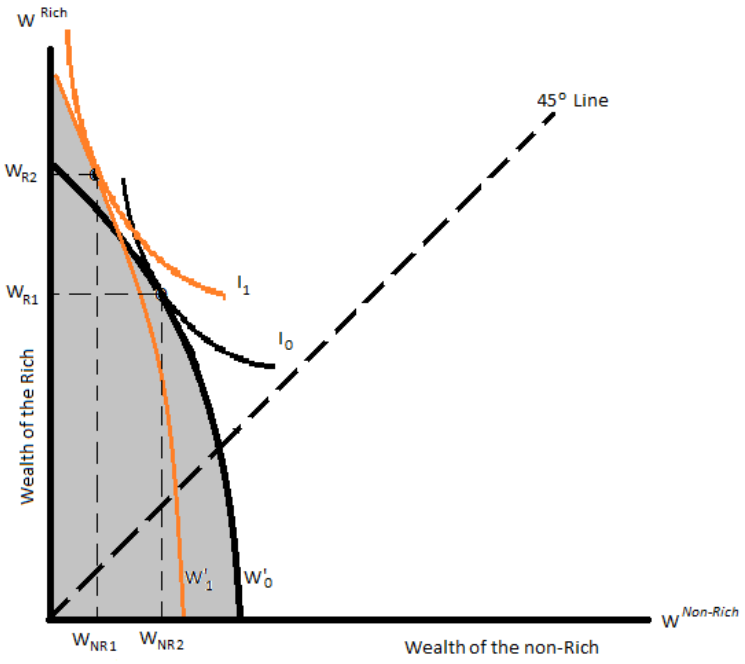


Figure 1 - Wealth Possibility Frontier

Figure 1, on the left, shows that in a closed economy, given a fixed amount of wealth, as the aggregate wealth of the rich (owners of capital) increases, the total wealth of the non-rich decreases (the pink wealth possibility frontier)—the wealth of the non-rich moves from W_{NR2} to W_{NR1}, limiting their consumption possibilities. As the non-rich consume less, inventories accumulate, and employers (capitalists) cut production and lay off workers. Recessions occur during this period, and the Federal Reserve injects money into the economy to let consumers borrow and buy goods and services from capital owners.

The COVID-19 pandemic demonstrated that consumers create jobs, not capital owners. If there is no consumption, there is no job creation; 70% of the U.S. gross domestic product is driven by personal consumption. However, in capitalist economies, government authorities bail out corporations rather than consumers.

Therefore, economic and political systems appear insignificant in achieving economic efficiency. Instead, any economic system, or combination of systems (mixed economy), with proper macroeconomic planning can approach optimality, whereas improper macroeconomic planning renders it suboptimal. China's economy performs well under a hybrid system that combines a communist authoritarian regime with a market economy.

Isidro Luna (2016) noted rising poverty rates in capitalist countries, including the United States and Europe, during the 2000s. Thus, the type of economic system does not determine a country's level of satisfaction or poverty rates.

Economic optimality, however, requires government authorities and personnel with robust administrative capacity. We rely on administrative capacity across many contexts (Misener & Doherty, 2009), and it is essential to delivering services to constituents. It entails running the machinery of a political or economic system and translating political and collective will into actions through management and implementation (Farazmand, 2009). However, many decision-makers, regardless of economic and political systems, seldom allocate employees based on their knowledge (capacity). Instead, they assign employees based on favoritism or some other physical characteristics. They select employees based on friendship, likability, homogeneity, racial and gender preferences, and so on, making optimality difficult, if not impossible, to achieve.

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Nevertheless, many efficient economic configurations exist for any given economy, and the optimum must satisfy technical conditions (Layers & Walters, 1978). Layers and Walters noted that a mixed economy and decentralized socialism could have the same formal optimality properties. In decentralized socialism, the state owns all capital and rents it out to bureaucratic enterprises, whose managers it instructs to maximize profits. Optimality is also possible under centralized socialism, though it faces information and incentive problems; nonetheless, if it uses the price system, it could overcome them (Layers & Walters).

Unlike communism, which socializes production and consumption, a socialist economy would assure its citizens a given level of income, and they would spend the income as they chose in buying commodities from the state (Taylor, 1929); that is, a socialist economy only socializes production, and not consumption (Lippincott, 1938). The argument that, under capitalism, consumers dictate what is produced is not entirely accurate. Take AI, data centers, and electric vehicles; most consumers did not demand them. Rather, entrepreneurs are attempting to impose them on consumers.

Moreover, in capitalist economies, many goods and services sell for prices far above their production costs. Additionally, in capitalist economies, government officials on both sides of the aisle often socialize taxpayer-funded research and transfer it to private ownership (Link, Oliver, Jordan, and Hayter, 2019).

Lange (1938) and Taylor (1938) assumed freedom of choice and occupation in their exposition of socialism. Thus, preferences or consumer demand also guide socialized production. In Socialism versus Capitalism, Pigou (1937) argued that a socialist economy based on economic techniques is superior to a capitalist economy.

Some economists, including von Mises (1922), have argued that public ownership of the means of production eliminates markets. Von Mises argued that capitalist society is the realization of economic democracy. However, history has documented the brutality and exploitation of capitalists worldwide, such as enslavement, stolen lands, regime changes, bombardments, and so on. Furthermore, Barone (1908), using a Walrasian general equilibrium model, proved that a socialist state yields the same results as a decentralized economy based on private property (Screpanti & Zamagni, 2005), and contemporary China has shown that these economists were incorrect. Lange (1936) also showed that socialist and capitalist economies determine prices in the same way. Thus, all economic systems must satisfy the *social welfare function,* which is the happiness of the individuals in society (Layers & Walters, 1978).

However, Western societies show a poverty of thought about the economics of socialism, even though approximately 30 percent of the world's population lives under socialism (Bergh et al., 2025). Views of socialism center on emotion rather than logic and mathematics. Lange noted that economists in capitalist societies discourage inquiry into socialist economics; yet, how can capitalist economies compete with China if they do not understand socialist or communist economies? Lastly, Western powers, such as the U.S., isolate non-Western socialist countries (Cuba, Libya, Venezuela, and others) with economic, as well as military, blockades to stifle their economies.

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In capitalist organizations and institutions, a central management board plans and sets goals to minimize costs and to ensure that the selling price covers production costs. Likewise, in socialist economies, an independent government board would do the same, planning and setting cost-minimizing goals to ensure that the selling price includes production costs. corpora

According to Lange (1936), the West's attachment to capitalism has inhibited scholars from considering socialist institutions that might more closely approximate an optimal economy. He noted that the first orthodox economist to show that the formal principles of economic theory apply to a socialist economy was Vilfredo Pareto. Lange also pointed to Pigou, who, in Socialism versus Capitalism, argued that, on economic grounds, a socialist economy is superior to a capitalist economy in most respects.

China has demonstrated beyond any doubt that different economic systems are not inferior. It is so effective that the Trump administration engaged in a failed trade war to curtail China's productive effectiveness.

In the U.S., people often conflate socialism with communism. Many U.S. citizens believe that socialist authorities dictate the products that consumers consume. However, a careful examination of Western nations with high levels of socialism, as well as communist China, shows that consumer choices prevail and that resource allocation is more cost-effective than in many capitalist economies.

In socialist economies, as in businesses and institutions, production is socialized; in communist economies, however, both production and consumption are socialized. As a result, citizens of socialist economies, such as China, dictate which commodities authorities will produce and which are in higher demand, a pattern similar to businesses in capitalist economies.

If capitalist economies, such as the U.S., had planning boards, it would be more effective in countering Chinese competition. For instance, it would know what products are causing trade deficits with the rest of the world. It could then establish cost-effective employee-owned manufacturing facilities in depressed areas to produce those products, such as in Appalachia and central cities. Likewise, it could build cost-effective housing and healthcare systems, establish effective school processes, and so on.

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