

[The importance of a market economy](#) [1]

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[Vuk picks up on an](#) [3] important point about the Soviet economy of old. Growth in that economy was almost entirely a matter of greater inputs into the economy. This is a strategy that clearly runs out of steam when you've no more inputs to add: and run out of steam that sort of economy did. But we can take this argument further, as Paul Krugman did when examining the Japanese economy of the 80s and 90s. [Here](#) [4]

How, then, have today's advanced nations been able to achieve sustained growth in per capita income over the past 150 years? The answer is that technological advances have led to a continual increase in total factor productivity--a continual rise in national income for each unit of input. In a famous estimate, MIT Professor Robert Solow concluded that technological progress has accounted for 80 percent of the long-term rise in U.S. per capita income, with increased investment in capital explaining only the remaining 20 percent....().....But what they actually found was that Soviet growth was based on rapid--growth in inputs--end of story. The rate of efficiency growth was not only unspectacular, it was well below the rates achieved in Western economies. Indeed, by some estimates, it was virtually nonexistent.

What it boils down to is that it is the strictures of the market that lead to that greater efficiency and technological progress. William Baumol has noted the reason why: either system can create the inventions, make the new technology. But only a market based system gives the freedom to experiment with it to increase that efficiency and then, as others become more efficient, that impetus for others to adopt in order not to go bankrupt.

The most important lesson of which in modern terms is for the various greens and environmentalists. If you really do want an economy in which resource use is reduced then you really do need to have a market economy. For planned ones just aren't any good at increasing efficiency: efficiency meaning here a reduction in resource use for any given level of output.

And when I meet, if I ever do, another environmentalist like me who argues for the free market precisely because it is environmentally sound to do so I shall rejoice. Until then, looking at the greens that we do have I can only consider them with horror. Why is it that they continually argue for policies like planning so inimical to their actual desire, reduced resource use?

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