

A Study on New Supply-Side Economics: Eliminations & Establishments

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Abstract

Review Article

A Structural reform will inevitably take place on the supply side, and pursue to improve the quality and efficiency of the entire supply system with effective system supply. Based on relevant fundamental theories, in the rethinking of mainstream economics theories after the global financial crisis, we have formed the cognitive framework of three eliminations and four establishments, namely eliminating bias, inconsistency and backwardness and establishing the framework, principles, integration and system. Analysis and cognition of supply side should be emphasized in the “basic framework” of economics. We should face up to reality and strengthen the effectiveness and pertinence of the support points in “basic theory principles and assumptions”. Market, government and non-profit organizations should play their respective roles and seek for cooperation as integration”. The institutional supply should be fully included in supply analysis to form an organic cognitive “system”.

Keywords: Structural reform, new supply-side economics; three eliminations; four establishments, financial crisis.

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INTRODUCTION

A Structural reform, theoretically speaking, must be happening in the supply side. It is in fact a solution issue of effective supply of institution, thereby to enhance the quality and effectiveness of the whole supply system. In practice, the structural reform such as its deepening in China nowadays should be supported by the proper fundamental theory of economics. Based on rethinking-related research efforts after the global financial crisis, my colleagues and I have been trying to set up a framework of New Supply-side Economics in this regard. Summing up briefly, we have got 3 eliminations and 4 establishments.

“Three eliminations”: eliminate bias, inconsistency and backwardness

After witnessing world financial crises and numerous problems in the practice in both developed and developing countries, people wonder why economists could not make accurate prediction and put forward effective explanation & feasible counter measures of these crises? How to summarize and analyze the experiences from success and failure of various economies in the process of coping with various crises using economic theories? Especially, how to consider and explain the extraordinary development and arduous transition in China? We think that we should ponder over the basic fruits of economic theories and we hold that these challenging problems frequently

mentioned all over the world can be summarized into the “Three Eliminations” of the economic theories and should be clarified in the new supply research in the following. The first is the “bias” of asymmetry of cognitive framework in the mainstream economics theories. Classical economics, neoclassical economics and Keynesian economics lay emphasis on different perspectives and make great contributions to economic analysis, but the common omission of them should not be ignored. They all assume fixed supply environment in theoretical framework and mainly focus on demand management and its in-depth analysis & relevant policies, while such kind of work for supply management are ignored and omitted. The “Washington Consensus”, which has a great influence in recent decades, is based on the theory of “perfect competition”, but there is no enough adjustment and rectification in combination with actual situation. In fact, it rejects in-depth analysis of supply side, results in obvious deficiencies in such an important research area. The supply-side school emerges under the pressure to deal with stagflation in US have made some contributions in the past decades and its contributions to innovative policies have significantly positive effects. However, there are obvious deficiencies in its theoretical system, for it is still built under the framework of “Washington Consensus” and aims to stimulate the potential and vitality of decentralized market players, while lacks in-depth understanding in

the analysis of structure, institutional supply and necessary government actions perhaps for there seems no urgent need for solving “transition problems” and “economic structure problems” in the United States, but which are faced by China and other ones. Compared with demand side which have commensurable index value and is easy for model building, the indexes of supply-side are incommensurable and infinite in variety, so the problems in supply-side are much more complicated, and the variables belong to “slow ones”, with tough tasks of structural analysis and proper structural countermeasures it is difficult to build models for supply side. However, these should not be the reason why we tolerate the cognitive framework asymmetry in economic theories for a long time. The second, is the “inconsistency” between the mainstream economic theories in textbooks and the real world practices. The United States and other developed market economics carry out a series of discriminative structural countermeasures and supply policies which are critical to the overall situation, and different from the mainstream economic theories in textbooks. Although these measures are not based on the theories in textbooks, but are stressed and relied on heavily in the actual practices. For example, the United States provides “discriminative” government funding to solve the key problems in the financial crisis, which have never been mentioned and analyzed in the textbooks. At the beginning, the authority thought over whether “to save or not to save” the Lehman Brothers and decided to let the old company with 157 years of history collapse, resulted in aggravation of the crisis, therefore then, drew the lessons and later on provided a large amount of public funds for Fannie Mae, Freddie Mac, Citigroup and finally General Motors in real economy. These are typical cases of governmental discriminative treatment in supply-side operation and it has a decisive impact on the overall social and economic situation. In the anti-crises practice in China, there were also a lot of such cases. However, such kind of an important practice has not yet been included and analyzed in influential academic literature and mainstream textbooks. The third is the “backwardness” of the economic research on the supply-side problems such as governmental industrial policies and so on. For example, the well-known economic literature rarely mention the “tangible” and “visible” “industrial policies”, but the measures taken by the United States are commendable, such as Iacocca: An Autobiography in 1980s stressing that the key to American revitalization is “industrial policies”; Information Superhighway during the Clinton administration; “industrial policy” mentioned by Obama State of the Union Message, such as the “Shale Gas Revolution”, 3D printer, “Made in America Again”, discriminative immigration policies for experts, favorite government loans to emerging economies such as Musk’s electric motors and so on. These are all different from the economic theories in textbooks, aiming at dealing with the major problems in real life and focusing on supply-side efforts. The research on

economic theories should have played a practical role, but frankly speaking, it lags behind practices.

“Four establishments”: establish framework, principles, integration and system

Based on the above-mentioned “Eliminations”, we also stress on that “establishment” should be considered from a broader and innovative economic perspective in combination with practices in China and all international experience and inspiration. Firstly, analysis and cognition of supply side should be emphasized in the “basic framework” of economics. This is a proposition under the stimulation of financial crises and it should be regarded as an essential link and innovation part in the “integration of theory with practice” of scholars. The following aspects should be stressed in basic theory: the main supporting factors for the continuous development of human society should be pointed out with innovation consciousness, is the response and guidance of effective supply to demand in the long run and the decisive features of supply capability in different stages leading to the division of development periods of human society. Of course, the original engine meaning of demand in this aspect shall not be ignored, but it is in short the understanding of economists for the inducing role of effective supply to demand in the past. This relates with the new thinking of the power driving system in economy crucial power-formation mechanism should be considered in supply side. It has the universality from basic theory, and is particularly suitable to solve the prominent problems of how to complete transition and maintain sustainable development in China and other similar developing countries by emphasizing on different development stages, as well as the institutional supply problems related to the “formation of supply capability” from the perspective of the decisive role of supply capability. Moreover, by responding to and solving the problems from this perspective, it can also help the developed economics to apply theories to actual needs after the global crisis. In real life, it is essential to solve both the problem of “providing products and services to meet the consumers’ needs” in the demand side and the problems of “what to produce” and “how to produce” in the supply side, especially the problem of “how to optimize institutional supply”. The research, which closely links demand with supply, is becoming increasingly essential and important in the human development. Secondly, we should face up to reality and strengthen the effectiveness and pertinence of the support points in “basic theory principles and assumptions”. For example, in-depth research should be conducted on “imperfect competition” as a prerequisite, for this is about the actual environment of resource allocation and involves a lot of supply-side problems. Although there are a lot of theoretical results about the “perfect competition” assumed by previous economics, it is only a model of 1.0 version, which lags behind current development obviously. Now we should focus on the discussion of imperfect competition which can better

reflect the real environment of resource allocation and cover all kinds of monopolies and other issues, so as to upgrade and extend model to 2.0 version and gain an insight into reality. Demand analysis mainly deals with the problems of total volume with homogeneous, unitary and commensurable indexes, while the supply analysis is more complicated, for it needs to deal with structural problems, system problems and it has no unitary and incommensurable indexes. It also involves government-market core problems. So it is bound to bring obvious challenges and extraordinary difficulties in the model extension. However, this is the major problem which can't be avoided in the innovation and development of economics. More medium-and-long term problems and "slow variable" problems will inevitably become difficult supply-side problems to be studied. As for the structural problems which are considered can be solved naturally in "General Equilibrium" or "Anti-Cycle" regulation, there is only a few words about it in the previous economic research, but we think that it can be upgraded to a series of imperfect natural evolution process based on the imperfect competition theory and deeply studied in combination with supply-side positive factors. Thirdly, we think market, government and nonprofit organizations should play their respective roles and seek for cooperation as "an integration". This is fundamentally the objective requirement for optimization of resource allocation. On the premise of clearly acknowledging the decisive role of the overall market, we should also discuss the labor division, cooperation and interaction of various subjects in optimizing resource allocation, namely market, government and "the third sector" (including nongovernmental organizations, volunteers, public interest groups, etc.). The selection and features of different subjects in labor division, cooperation and interaction are different by stages and fields. The evolution of concepts for labor division among these subjects from the "failure", "replacement" and eventually "cooperation" based on "Public-Private Partnership" (PPP) reflects that the diverse subjects relation in human society show the new features and tendency along with economic development and civilization progress. Fourthly, the institutional supply should be fully included in supply analysis to form an organic cognitive "system". According to the new supply economics, the research on supply-side economics should be conducted from the perspectives both of "goods and materials" and "human"; the research on supply problems of various elements, and the research on institutional supply problems, should be well combined; the research results of development economics, institutional economics, transition economics, behavioral economics and other concepts need to be integrated in one system. It is particularly necessary to respond to transition economics and China's actual needs through the "establishment" of system. The core concept thus formed is that more attention should be paid to the "rational supply

management" in the process of establishing theories and linking theory with practice. In order to solve the challenging historical task of modernization in China, we must pay special attention to the extraordinary long-term process of "catch-up and surpassing", in supply-side which focus on innovation of system & mechanism, and structural optimization. Moreover, it is necessary to integrate all positive research achievements of economics and other relevant subjects into one scientific system with the broadest view; the analysis of productive force factors in "goods and materials", and the analysis of productive relations and institutional factors in "human", should be organically combined in the supply-side, so as to help us to "know the world and change the world". Both "productive forces determine the productive relations" and "the productive relations also influence and improve productive forces" are objective rules to abide by; as for China in transition, in order to seize a profound understanding of the former, the government needs to understand, respect and revere the market and keep economic development as the central task; in order to have a profound understanding of the latter, the government should carry on market-oriented reform, give full room to the decisive role of the market in resource allocation while play a active and proper role for structural adjustment. In the meantime, it is necessary to deal with the challenging problem of "how to achieve better functioning of the government" and improve the quality and efficiency of the entire supply system in the economic development through the structural reform. In addition to the above-mentioned "Eliminations" and "Establishments" in the study of new supply economics, it is necessary to have an understanding of demand side. Since there are sufficient theoretical results of "demand management" in the economic field, it is hoped that more understanding of supply side should be added to improve the symmetry of cognitive framework. According to the reality in China, economists and scholars will certainly lay logical emphasis on the concept of "taking reform as the central task" and implement reform, transform the system in the new era of "all-round reform" in supply side. This is a "key measure" to effectively resolve the contradictions, "stagflation", "Middle Income Trap", "Tacitus Trap", "Welfare Trap" and other risks, and cater to China's urgent needs for transition and sustainable, healthy development, so as to gain the "biggest bonus" for realizing "China Dream" of modernization. We have put forward a theoretical model for supply side factors analysis in an economic journal in English, and hope to promote the research further.

CONCLUSION

Based on the economic rethinking after the global financial crises, it is necessary to study and establish the cognitive framework of new supply-side economics so as to make the theories reflect and lead the practice much better by its function. The relevant

“elimination” and “establishment” supporting this framework refers to at least “three eliminations” and “four establishments” in this paper. This is an important perspective that economic theoretical innovation cannot avoid when it comes to the times.

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