

# Comparison between a developing and developed country



The countries I choose to discuss are China representing the developing country and USA symbolizing the developed country.

economic system concerns with the production structure of a country. It also includes how to allocate the economic inputs, how to distribute the outputs between the citizens and how to consume goods and services in an economy.(NA 2007)

According to Gregory et al (2003), the economic system has four dimensions: decision-making structure, coordination mechanism, productive property rights and incentive system.

Decision making concerned with by whom the decisions are carried out, industrial councils, the government, or private owners. In US, excluding only a few national industries, many decisions are decided by the private owners, however, in China, there are a lot of state-owned enterprises which make decisions under the influence of the government.

Coordination mechanism is the way of obtaining information and how to use it to coordinate economic activity. The main forms of coordination contain planning and the market. In US, its coordination form is the market: the market is clear, and the exchange of information is highly efficient. While, China has been through a long time of planning coordination, its form, although its government claims the market, is in an interim.

Productive property rights is about who takes control of the output. In US, the ownership is protected by the constitution while in China, they are owned by the public or by all the members in the society.

Incentive system refers to the reward. There are two major base: material (compensation) and moral (social prestige). In both countries, they have both incentive systems simultaneously since either one is enough.

## 1. 2 financial system

### 1. 2. 1 financial system in US

In the US, its unit of money is dollar. Its central bank is Federal Reserve who is responsible for making decision concerning to the finance such as financial policy and the base interest rate. since Fed is independent of the government and its chairman has a term of 18 years, it may put focus in the long term. In US, there are many financial institutions such as banks, insurance companies, mutual funds, insurance companies and so on. The varied institutions designed many sorts of financial instruments circulating in the financial market in the US which make the US the most efficient financial market in the world.

### 1. 2. 2 financial system in China

In China, its unit of money is yuan. Its central bank is People's bank of China(PBC). Compared to Fed, they have a same job including issuing currency, making financial policy and so on. However, since PBC is also a part of the government, its independence is in doubt in some degree. In other words, PBC may adopt the government leaders' opinions when they make their final decision. Chinese financial system is immature and still in the progress of developing. In this way, the kinds of financial institutions in China are limited. There are no private-owned financial institutions in China

and there's legal protection that financial institutions can only be emerged but no bankruptcy. The financial instruments are also limited. Time deposit, demand deposit, and treasury bills are individual investors' primary choice. Until now, more and more people are taking part in the stock market or buying some fund.

### 1. 3 the unique feature-means used by the central to regulate the economy

In China, when PBC wants to express its monetary policy, its main tool is to change the benchmark of deposit and lending rates. If PBC wants to adopt tightening monetary policy, it will increase the benchmark rate, on the other hand, it will drop the rate when adopting expansionary monetary policy.

However, the method has its own disadvantage: its effect is so strong that it may hurt the development of the economy.

In the US, when Fed wants to regulate the economy, its first option is open market operation. If they want to adopt an expansionary monetary policy, it will buy the treasury bills from the financial market and release more money in the circulation. While, when they want to tighten the market, it will sell its bills and get money in the circulation back to the Fed. By regulation this way, the Fed is able to regulate the economy more proficiently and accurately, and this method has the smallest negative effects to the economy.

The main reason why China doesn't use open market operation very much is that its financial instruments are limited and its financial market is not mature enough to do it. The other reason is that Chinese government interferes with the central bank more compared to the US government to the Fed.

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## 2. 1 A brief introduction to IMF

IMF, short for International Monetary Fund, is the international organization aimed for supervising the global system, especially financial system. Its main targets are keeping an eye on exchange rates and balance of payments as well as aiding the developing countries financially and technically.

(Wikipedia)

This organization was conceived back to July 1944 when 45 governments held a meeting in the Mount Washington Hotel located in Bretton Woods: in this way, this financial system later was called Bretton Woods system. It was formally founded on December 27, 1945.

## 2. 2 Members of IMF

At the beginning of its foundation, it had only 29 members and its influence on the global financial system was rather limited. However, as time goes by, its affect on the global finance even economy is increasing gradually: the members it accumulated is more and more.

It is not that easily be accepted as a member of IMF. The country or state has to take several strict steps before it is able to sign the IMF's Articles of Agreement. However, that effort is worth endeavoring: every member has its own quota in it. The quota represents the status of the member in the organization since several crucial characteristics including the voting weight and allocation of SDRs are determined by the quota.

The member who has the most quota in IMF has the greatest power in IMF. United States enjoys 15.82% while other members only get around 6%, or even less. In this way, the US has always been the country which is able to block a supermajority on its own. This is also the point raised by many critics that how can IMF keep its equity among so many members.

## 2.3 the objectives of IMF

The fundamental task for the IMF stays the same as it was founded: to supply financial aid to the countries in need.

## 2.4 challenges faced by IMF

The financial crisis beginning in 2008 is so devastating that nearly every part of the world is strictly affected by it. IMF is also no exception. This crisis is also showing the world that globalization, if not controlled properly, may turn to be a disaster throughout the world and some international financial organizations, such as IMF, has to face some new challenges.

According to the statement of an official in IMF, although the global economy would hit the second bottom since 2008, the whole world still has to face four crucial challenges: the financial sustainability, employment crisis, repair of the financial organizations and global cooperation.

### 2.4.1 financial sustainability

Financial sustainability can be represented as a mutual trust between the government and its citizens on the policy. In this way, it is very critical when government is making policies in the recovery. To explicate it, let's make an

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example. When suffered from the crisis just now, the country's economy was destroyed nearly completely. In order to recover quickly, the government chooses the expansionary fiscal policy by increasing the government spending or decreasing the inflation rate. By doing this, the government wants to show the confidence that they want to encourage more investment to the citizens. The citizens, responding to the government, begin to invest more than before, since they have a faith in government. However, with the increase of investment, the government realizes that another problem is showing up: the inflation rate is rising. In order to overcome inflation, the government has to increase the interest rate, which is a signal of scotch the investment. The citizens may feel confused by the government's changing policy, and may lose faith in it. If the trust between a government and its citizens is destroyed, the recovery is totally hopeless. However, usually the government is shortsighted and its lack of financial sustainability cannot help the recovery and even lose the best opportunity, it is the IMF's responsibility to help guiding the government and make sure that they make the right decision.

#### 2. 4. 2 employment crisis

Since the financial crisis in 2008, many developed countries including USA and some major European countries are suffering from the extraordinarily high unemployment rate. Mr. Obama, the president of United States, had promised that the unemployment rate of US would drop. However, until right now, the unemployment rate of US is still above 8%, and there is more rumor that this number will fly to 10% or higher. This phenomenal is very common among the other developed countries around the world. High employment is <https://assignbuster.com/comparison-between-a-developing-and-developed-country/>

fatal to a country's stability. Without a domestic stable economy, how can people around the world make sure of the stability of the economy? While creating a stable environment for the global economy is one of the objects of IMF, how to lower the unemployment and create more job opportunities become their challenges.

#### 2. 4. 3 repair of the financial organizations

As it is well known around the world, five major investment banks disappeared in USA during the financial crisis. Affected by this, many other financial and nonfinancial organizations within and outside US were in danger of bankruptcy. Since financial organizations are the primary elements in the financial system, helping them repair from the crisis is necessary. However, despite the organizations, even some countries are facing bankruptcy themselves. Depending on the government may not be a very good choice. In this time, the job rests on the shoulder of IMF, an international financial organization, who is able to help national ones when they need it.

#### 2. 4. 4 global cooperation

With the pace of globalization, the cooperation within different countries is becoming more and more indispensable to one's own economy. The deadly financial crisis happened in 2008 was first ignited in the US, while, after a short time, this crisis was spreading around the whole world like a cancer. Until now, many parts of world are still suffering from it. From this crisis, it is widely realized that even it is caused by only one section of a country, the influence may be spreading far far way, just like the butterfly effect. Thus, in <https://assignbuster.com/comparison-between-a-developing-and-developed-country/>



order to cope with it efficiently, every country should enhance their cooperation with each. To cooperate finely, there has to be an organization to regulate their behaviors and that organization is IMF. Now, how to help each member cooperation with others effectively and safely is the final but not the easiest challenge faced by IMF.

## 2. 5 my suggestions

When facing these new challenges, I have several suggestions for the IMF.

First of all, I suggest that IMF should guide those countries who have the most serious debt problems, even by exempting from a certain amount of heavy debt. Only by doing this can help them stabilize the domestic environment within the countries.

Another suggestion from me is that IMF should appeal that every member enhances its cooperation when making policies. We must abandon the way of recovery based on hurting the other member's economy such as the protection to local product by putting more duty on the imports.

NA (2007). " economic systems," The New Encyclopedia Britannica, V. 4, p. 357.

Gregory et al(2003). Comparing Economic Systems in the Twenty-First Century.