

## **SOCIAL MARKET ECONOMY: OBJECTIVES AND PRINCIPLES**

**Prepared By**

**Mahmoud Alawni      Nadia Abu Alia**

**Research Papers Series on Law and Economics**

**(9/2018)**

**Institute of Law – Birzeit university**

**SOCIAL MARKET ECONOMY: OBJECTIVES AND PRINCIPLES**  
**Research Papers Series on Law and Economics (9 / 2018)**  
**Institute of Law – Birzeit University**  
**Birzeit, 2018**

**Copyright ©, Institute of Law, Birzeit University, Palestine**

*This publication is supported by  
Konrad-Adenauer-Stiftung*



**This publication reflects the views of its author, and not necessarily those of the Institute of Law. The author is solely responsible for information used therein.**

## Table of Contents

<b>Abstract</b> .....	2
<b>I. PREFACE:</b> .....	3
<b>II. OBJECTIVES OF THE SOCIAL MARKET ECONOMY:</b> .....	4
<b>III. THE PRINCIPLES OF THE SOCIAL MARKET ECONOMY:</b> .....	6
<b>IV. ORGANIZATIONAL PRINCIPLES OF THE SOCIAL MARKET ECONOMY</b> .....	9
<b>V. THE ROLE OF THE STATE:</b> .....	10
<b>REFERENCES</b> .....	12

DRAFT

**Abstract:**

This paper shall present a summary of the basic principles and objectives of the social market economy and review the literature in the field given. More specifically, this study shall analyze the main elements of the social market economy.

This paper shall be a reference theoretical paper; its purpose is to identify the concepts and principles of the social market economy without going into the extent of the association, link and relation of these principles to the Palestinian economy. Hence, the paper shall only reflect the general framework of the objectives and principles of the social market economy.

It shall be divided into four parts: the first shall address the objectives of the social market economy. The second shall address the general principles, the third will address the organizational principles, and the fourth will analyze the role of the state.

This study does not cover the entire principles of the social market economy that each country adopts; it rather reviews the basic and general principles of the social market economy, which in return assists in the matter of adopting the system in Palestine. The study's main objective is to assist the research team in forming its empirical hypothesis on the social market economy's principles and standards, therefore is considered a reference paper.

## 1. Preface

The social market economy is defined as an organized economic system based on a competitive economy that links free enterprise to social progress, which is secured through economic achievement in the market to create and ensure prosperity for all members of society.

The social market economy is known as a social and economic concept that resulted through a long historical and political process that began between the 16<sup>th</sup> and 18<sup>th</sup> century.<sup>1</sup> This economic model is a deep normative system that is based on strong values and a set of economic rules; an envisioned system where economic growth and social sustainability are not opposed to each other, but work in harmony to create a sustainable and positive development for society as a whole.<sup>2</sup> The social market economy aims to combine the values of individual freedom, solidarity, and subsidiarity, as well as combining the efficiency of the market with equal opportunities. This model is viewed as an alternative to classical liberalism and socialism that are either based on efficiency without equitable development or equitable development without efficiency.<sup>3</sup>

Alfred Müller-Armack defined it as an ideological concept aimed at creating and strengthening relations of cooperation and coordination between various sectors of society, including the various configurations of the same class. Indeed, Müller-Armack considered the social market economy as a strategic idea that promotes real cooperation between groups of society that are different and are opposing in their aims.<sup>4</sup>

Consequently, the social market economy is not only comprised of an economic approach, but also with the philosophy of creating a society that protects and establishes the dignity, encouragement, freedom, and well-being for all individuals.<sup>5</sup>

---

<sup>1</sup> Siegfried F. Franke and David Gregosz, *The social market economy: what does it really mean?*, Konrad-Adenauer-Stiftung 2013 pg.8.

<sup>2</sup> Siegfried and David, supra note 2, pg.8.

<sup>3</sup> Ibid.

<sup>4</sup> Yamamah Ismail, *The Experience of the Social Market Economy in Syria, and its Implications for Economic and Social Reality*, Thesis, (Syria: Damascus University, 2015), pg. 9.

<sup>5</sup> European People's Party (EPP), *The Social Market Economy in a globalised world*, Congress Document adopted by the EPP Statutory Congress (Bonn, 9-10 December 2009), pg. 2.

## 2. Objectives of the Social Market Economy:

The main aim of the social market economy is to reconcile between economic efficiency and social justice, which is based on four main axes; creating competition i.e. no monopoly hit, (for monopoly leads to economic stagnation); creating equal opportunities; state intervention when market mechanisms are unable to play a sufficient role, and finally, the essence of the social market, which is state intervention in directing spending and investment in order to meet the social needs, reduce class differences and to ensure social stability, which is considered the base material for any economic start-up. Thus, the economy of the social market is mainly based on the idea of interaction between the market and the state.<sup>6</sup>

There are many requirements that, in practice, make the fundamental pillars of the social market economy. However, its most significant and important pillars are the rule of law and a democratic system that preserves the rights and interests of all different community groups. Social partnership between unions and businesses is considered to be essential for regulating the labour market and stimulating the activity of investment, setting up projects that provide a high rate of employment and for achieving social justice; all of which represent the requirements of the social market economy and its main benefit in creating sustainable economic growth that redistributes wealth to various groups of society.<sup>7</sup>

The objectives of the social market economy extend from economic growth to social justice and community care, as well as environmental protection. These objectives can be identified as follows:

---

<sup>6</sup> Hayyan Suleiman, *The Social Market Economy: between idea and application*, Syrian Association of Economic Sciences, (Damascus, 28/11/2005), pg. 3.

<sup>7</sup> Yahya Al-Mutawakil, *Social Market Economy in Yemen: Meeting the Call for Change and Achieving Human Dignity*, Sana'a University, Symposium on Economic issue at the National Dialogue Table, Sana'a, pg. 4.

### **1. Economic objectives:<sup>8</sup>**

- Financial stability, which requires a balance between expenditure and revenue, in addition, to covering the current expenditure from tax revenues to ensure price stability.
- Balance in foreign trade, which means a balance between the amount of exports and imports to achieve stability of exchange rates.
- Full employment, which reflects an optimal use of economic resources in order for unemployment not to exceed a level of 4%.
- Innovation and growth, which reflects attention to the quality of production and the pursuit of new products with modern technologies that help open markets and lead to increased economic growth.

### **2. Social objectives:<sup>9</sup>**

- Increase opportunities for education and encourage individuals to enrolling in education to ensure equal opportunities for all.
- Develop the health sector and provide appropriate medical services.
- Provision of social welfare through pension and other protection systems.
- Give attention to the behavior of the individual market participants and ethics, and motivate the individual participants in the creation of wealth.
- Achieve overall growth by giving balanced attention to political, economic and social aspects.

### **3. Environmental objectives** (achieved through the use of modern technologies that are environmentally friendly):<sup>10</sup>

- Reduce emissions of carbon dioxide.
- Increase the production and maintenance of renewable energy.
- Trash disposal.

The social market economy system has a number of characteristics, the most important of which are the following:<sup>11</sup>

---

<sup>8</sup> Yahya Al-Mutawakil, *Social Market Economy in Yemen*, pg. 11.

<sup>9</sup> Ibid.

<sup>10</sup> Yahya Al-Mutawakil, *supra* note 10, pg.11.

1. Flexibility: meaning, the possibility of increasing or reducing state intervention in economic activity according to the stages of state development, necessity and need.
2. Openness: for its ability to cope, which made this system characterized by efficiency, development, and innovation due to internal and external variables and events.

### **3. The Principles of the Social Market Economy:**

The theory of the social market economy is characterized as having the ability to accept any ideology or political thought, whilst directing its focus on rebuilding the base of the national economy and for providing an adequate minimum standard of living.

It can be concluded that the basic principles of the social market economy are:<sup>12</sup>

1. The basic principle of having an effective price system for goods and services. The policies formed should prevent actions which distort the relative prices, such as unfair price fixing by monopolies.

The principle of a price system essentially means, sending market participants indications which goods ought to be produced and in what quantity and quality. Prices indicate the methods and places where production will be most profitable.<sup>13</sup>

2. The precedence of monetary policy, which aims to stabilize the value of the local currency and achieve price stability.

Price stability is achieved by managing the policy that is related to the money and credit within the national economy. Accordingly, the state influences monetary policy through financial policy, exchange rates and foreign trade.<sup>14</sup>

---

<sup>11</sup> Ibid, pg. 10.

<sup>12</sup> Ibid, pg.3.

<sup>13</sup> Dietrich Dickertmann, Viktor Wilpert Piel, Social market economy: Principles and functioning in Rolf H. Hasse, Hermann Schneider and Klaus Weigelt (eds.), *Social Market Economy History Principles and Implementation From A to Z*, Ferdinand Schöningh 2008, pg.409.

<sup>14</sup> The Regional Program Near East/Mediterranean, *Social Market Economy in the International Work of Konrad-Adenauer-Stiftung*, (Konrad-Adenauer-Stiftung, 2008), pg. 37.

[https://www.kas.de/c/document\\_library/get\\_file?uuid=73a16418-6584-d5c4-8c73-522b6bffc2c8&groupId=252038](https://www.kas.de/c/document_library/get_file?uuid=73a16418-6584-d5c4-8c73-522b6bffc2c8&groupId=252038)



3. The principle of open markets, which ensures the freedom of market access to avoid monopolies and to increase competition in the market; this principle ensures that free trade is necessary in a social market economy.

The openness of a market entails the freedom of entry and exit. There must be no barriers for market participants to either market entry or exit. Indeed, every potential actor must be given an opportunity to enter the market as a new competitor, and consequently be able to withdraw from the market.<sup>15</sup>

4. The principles of private ownership and the freedom of owning means of production, which from a market perspective are the private ownership of means of production. The latter can lead to outcomes that are economically and socially satisfactory, and can be a catalyst for growth for market participants.

The functioning of a social market economy does not only include labor and knowledge but also real estate, money, pension claims, factories... etc. that are owned by individuals which have the choice of deciding what happens to these assets (sold, or given away). However, property ownership also entails the obligation that the use of property should also serve the public good; this does not only help in sustaining a family but also developing one's personality.<sup>16</sup>

5. Freedom of contract. This principle guarantees the mutual protection of all companies and increases competition.

This principle is essential for competition as market participants are able to conclude contracts free of any external restrictions. However, freedom of contract is not free from limitations. It shall not, *inter alia*, be improperly used to undermine or eliminate the order of competition, or offend common decency; otherwise such contracts will be unenforceable.<sup>17</sup>

---

<sup>15</sup> Dieter Fritz-Abmus, Open markets: Market entry, market exit in Rolf H. Hasse, Hermann Schneider and Klaus Weigelt (eds.), *Social Market Economy History Principles and Implementation From A to Z*, Ferdinand Schöningh 2008, . pg. 327.

<sup>16</sup> Konrad-Adenauer-Stiftung Regional Program Near East/ Mediterranean , *Freedom and Order for more Justice*, pg. 19.

[https://www.kas.de/c/document\\_library/get\\_file?uuid=73a16418-6584-d5c4-8c73522b6bffc2c8&groupId=252038&fbclid=IwAR2iIWZ8T0KaMg8M90INZ0QE-Iro5WETcmP9WccZ7\\_ff3vKTcHhvdHveSVQ](https://www.kas.de/c/document_library/get_file?uuid=73a16418-6584-d5c4-8c73522b6bffc2c8&groupId=252038&fbclid=IwAR2iIWZ8T0KaMg8M90INZ0QE-Iro5WETcmP9WccZ7_ff3vKTcHhvdHveSVQ)

<sup>17</sup> Ibid.

6. The principle of responsibility, which is the obligation and the responsibility of the owners of the means of production to their ownership and decisions.
7. A stable economic policy that leads to the establishment of people's confidence in the existing economic system, which is considered essential for the functioning of the market.

The main goal of the social market economy is long-term social and economic progress, relativity, with competition being the key for such a goal. Competition prompts a good market supply of goods and services. In addition, competition allows all market participants a great room for various activities and freedom of choice.

Consequently, the three general principles which form the base for any social market economy model are:<sup>18</sup>

1. **The individual spirit:** which represents liberal idealism and is expressed in private ownership and free competition, coupled with an obligation on the individual to make more effort to ensure social justice and adequate living standards.
2. **Social solidarity:** which indicates that the individual is embedded in a society that is intertwined with mutual interests. The wealthiest individuals in the society have to contribute by producing more opportunities and improve the quality of life for other individuals who cannot achieve decent standards, which can be achieved through progressive taxes or other means, in order to overcome social injustice.
3. **The principle of subsidiary:** which means that the institutional base should form the relationship between individual interests and social solidarity principles to guarantee and prioritize the individual rights. Meaning, everything that can be done by the individual shall not be done by the state. It follows that an effective role is allocated to the state in cases of, recession, natural disasters, environment protection, and innovation.

#### 4. Organizational Principles of the Social Market Economy:

---

<sup>18</sup> Yahya Al-Mutawakil, pg. 9.

As such, the aforementioned principles generally indicate that individual rights and economic freedoms are the conditions under which justice and social solidarity are implemented. The social market economy aims to balance the principles of the free market and social responsibility in order to make them an integrated political economic and social program. As the confidence of liberalism's supply and demand factors in the management of the market economy has diminished, the need to establish mechanisms that guarantee social protection as well as free markets has emerged. Thus, the social market economy is considered to be a combination of political and economic factors that go beyond the liberal thought in a market mechanism to a more socially moral concept in social development theories.<sup>19</sup>

The social market economy is based on the following organizational principles:<sup>20</sup>

- Competition policy which aims to reduce and eliminate the permanent control of monopolies.
- The policy of redistributing income and correcting its imbalances by market intervention and an effective tax system to ensure that social needs are taken into account.
- The prices must reflect the costs and serve a fair distribution and an equitable division of scarce resources through organizing it.
- Regulate external effects and compensate for market failure.
- Compensation and social security.

Consequently, the organizational principles of the social market economy are based on the following main elements:<sup>21</sup>

- Balanced focus on economic and social objectives.
- Focus on human rights.
- The balance between productivity, goals and social.
- Regulated state intervention in the economy.
- Expansion of social security.

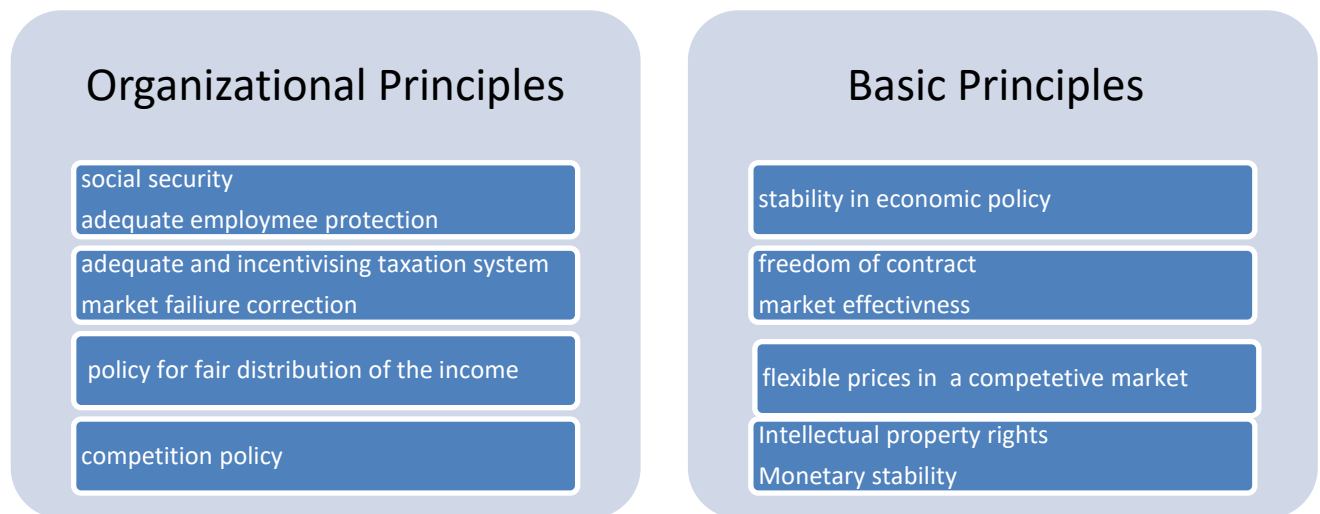
---

<sup>19</sup> Yahya Al-Mutawakil, 9.

<sup>20</sup> Yamamah Ismail, *The Experience of the Social Market Economy in Syria*, pg. 16.

<sup>21</sup> *Ibid*, pg.11.

The boxes below state the basic and organizational principles of the social market economy:<sup>22</sup>



## 5. The Role of the State:

It has been recognized by the architects of the social market economy that the only sufficient framework conditions are created by the state,<sup>23</sup> through implementing the social market principles by creating certain economic and institutional qualifications, legal framework and legal security to create the ideas and model of the social market economy.<sup>24</sup> Market actors can behave irrationally or solely focus on short-term gains and thereby put the market at risk. Therefore, the government needs to take action and create adequate framework conditions by setting rules against discrimination, unfair competition, and excessive risk-taking.

Accordingly, this is achieved by counterbalancing special interests and the limits on state intervention, which in return will help in creating a safeguarded free competitive market based on a constitutional level.<sup>25</sup>

Thus, In order to establish the social market economy system, the state has to assure “social welfare” this is created by creating a mechanism that insures competition as to harmonize the profit maximization motive with the common good, also by establishing full-employment policy that also assures promotion policy as to protect employers from the downturns of the business cycle. In addition the state must encourage social thrift by combining the respect of the principles of the social market economy with the policy of bridging the gap in income in order to avoid great differences in incomes and wealth by supporting inexpensive housing

<sup>22</sup> Yamamah Ismail, *The Experience of the Social Market Economy in Syria*, pg. 16.

<sup>23</sup> European People’s Party, *The Social Market Economy in a globalised world*, pg. 3.

<sup>24</sup> Konrad-Adenauer-Stiftung Regional Program Near East/ Mediterranean , *Freedom and Order for more Justice*, pg. 17

<sup>25</sup> Yamamah Ismail, pg. 16.

construction, progressive taxation, child and family benefits for those in need and guaranteeing minimum wages.<sup>26</sup>

However, these rules must be implemented without distorting the market economy as a whole. Thus, in essence, the order of the economy must be guaranteed by the state without directly interfering in the economic process. Moreover, in a free market price system, competition and cooperation between consumers and free entrepreneurs creates a new discovery process that is able to incorporate more decentralized and spontaneous knowledge than central planning by political authorities. Entrepreneurial forces are therefore turned into powerful tools that are able to increase the wealth of all nations. As such, this is achieved when the state acts as a rule-maker and a referee as opposed to being omnipresent.<sup>27</sup>

Essentially, if Palestine wants to adopt the social market economy, these are the main elements that constitute this model. Consequently, there shall be papers that will analyze the current Palestinian system, and evaluate whether, and how, the social market economy system can be implemented in Palestine.

---

<sup>26</sup> Zbigniew Klimiuk, *The Concept of the Social Market Economy and Economic Policy as the Foundations of Economic Growth in the Federal Republic of Germany, After World War II*, *Roczniki Ekonomii i Zarządzania* 1 (2016), pg.11.

<sup>27</sup> European People's Party, *The Social Market Economy in a globalized world*, pg. 3.

## References:

### English:

- Dieter Fritz-Aßmus, “Open markets: Market entry, market exit” in Rolf H. Hasse, Hermann Schneider and Klaus Weigelt (eds.), *Social Market Economy History Principles and Implementation From A to Z*, (Ferdinand Schöningh 2008).
- European People’s Party (EPP), *The Social Market Economy in a globalised world*, Congress Document adopted by the EPP Statutory Congress (Bonn, 9-10 December 2009).
- Franke, Siegfried F., and David Gregosz. *The Social Market Economy: What Does it Really Mean?* (KAS, 2013).
- Hasse, Rolf, and Klaus Weigelt, eds. *Social Market Economy: History, Principles and Implementation: from A to Z*. (Konrad-Adenauer-Stiftung, 2002).
- The Regional Program Near East/Mediterranean, *Social Market Economy in the International Work of Konrad-Adenauer-Stiftung*, (Konrad-Adenauer-Stiftung, 2008).
- Zbigniew Klimiuk, *The Concept of the Social Market Economy and Economic Policy as the Foundations of Economic Growth in the Federal Republic of Germany, After World War II*, *Roczniki Ekonomii i Zarządzania* 1 (2016)
- Konrad-Adenauer-Stiftung Regional Program Near East/ Mediterranean , *Freedom and Order for more Justice*,  
<[https://www.kas.de/c/document\\_library/get\\_file?uuid=73a16418-6584-d5c4-8c73522b6bffc2c8&groupId=252038&fbclid=IwAR2iIWZ8T0KaMg8M90INZ0QE-Iro5WETcmP9WccZ7\\_ff3vKTcHhvdHveSVQ](https://www.kas.de/c/document_library/get_file?uuid=73a16418-6584-d5c4-8c73522b6bffc2c8&groupId=252038&fbclid=IwAR2iIWZ8T0KaMg8M90INZ0QE-Iro5WETcmP9WccZ7_ff3vKTcHhvdHveSVQ)>

### Arabic:

- Hayyan Suleiman, *The Social Market Economy: between idea and application*, Syrian Association of Economic Sciences, (Damascus, 28/11/2005).
- Yahya Al-Mutawakil, *Social Market Economy in Yemen: Meeting the Call for Change and Achieving Human Dignity*, Sana'a University, Symposium on Economic issue at the National Dialogue Table, Sana'a.
- Yamamah Ismail, *The Experience of the Social Market Economy in Syria, and its Implications for Economic and Social Reality*, Thesis, (Syria: Damascus University, 2015).



## **Research Papers Series on Law and Economics**

**Within the framework of its research project on law and economics, the Institute of Law at Birzeit University focuses – during the first year - on studying social market economy principles and values, examines comparative experiences and conducts theoretical comparisons. Moreover, papers produced examine to what extent relevant Palestinian legal frameworks are compatible with the principles and values of social market economy.**