

ECONOMIC SYSTEMS

Why does California produce food and not computers?

- Who makes that decision?

Economic System

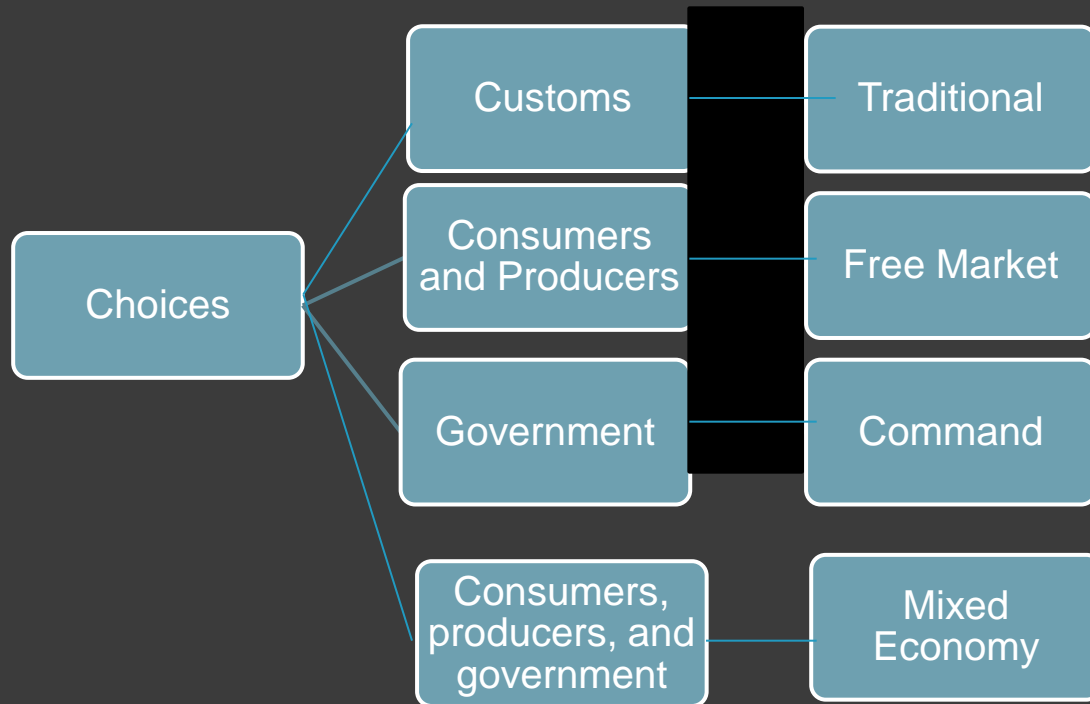
- An **Economic System** is the method used by a society to produce and distribute goods and services.
- Every society must answer three questions:
 - What goods and services should be produced?
 - How should these goods and services be produced?
 - Who consumes these goods and services?
- Societies answer the three economic questions based on their values and goals.

How do societies answer these questions?

◎ They have Economic Goals

- **Economic Efficiencies**-making the most of resources
- **Economic Freedom**-freedom from government in production and distribution
- **Economic Security and Predictability**-assurance that good and services will be available, payments will be made, a safety net will assist in case of disaster
- **Economic Equity**-fair distribution of wealth
- **Economic Growth and Innovation**-innovation leads to growth, growth leads to higher standard of living

4 Types of economies



Traditional Economies

Features:

- existence was primarily based on traditions and customs
- barter was the main form of trading
- individuals existed on a subsistence level
- the decision of what, how and for whom was determined by customs and traditions
- resources were owned or controlled by a sovereign or feudal lord.

Examples of this economic system:

- Remote tribal areas in South America, Africa and Asia



Advantages and Disadvantages?

Traditional Economy

- ◉ **Advantages:**

1. Every member of the society knows exactly what they are to do.
2. There is a strong social network.
3. Positions within society are already established.
4. Basic Economic questions are already answered by traditions and customs.
5. Life is generally stable, predictable and continuous.

Disadvantages:

1. This type of society is often very slow to change.
2. It does not take advantage of technological change.
3. There is relatively little promotion of intellectual and scientific development.
4. There is inefficient provision of goods and services.
5. There is inadequate use of skill in relation to the factors of production.
6. No upward movement of labor takes place.

Command Economies

Features:

- government controls all economic activity
- government decides what goods are produced, how much of each good to produce and how much the people should get.

Examples of this economic systems:

- The former Soviet Union (now 15 countries including Russia and Ukraine) dismantled their planned economies from 1990.
- China until the 1980s and 1990s
- Cuba until the 1990s
- North Korea – present day



Advantages and Disadvantages?

Command Economies

Advantages:

1. The welfare of all citizens is the primary goal
2. Full employment of all available resources
3. Government possess the information to be able to direct resources where they are most needed.
4. Wasteful competition is avoided
5. There is no industrial unrest such as striking, as the government controls wages
6. Greater emphasis on quality of life than on quantity produced.

Disadvantages:

1. No freedom of choice for consumers or producers
2. System is too rigid to adjust when changes occur, can result in shortages
3. Lack of incentive for workers results in low morale and efficiency. Managers also are not motivated.
4. There are too many officials, and too much unnecessary procedure and paperwork (red-tape or bureaucracy)
5. Conflicts of interests can arise because what the country needs may not be what the people want.
6. There is wastage of manpower because large numbers of people are required for central planning.

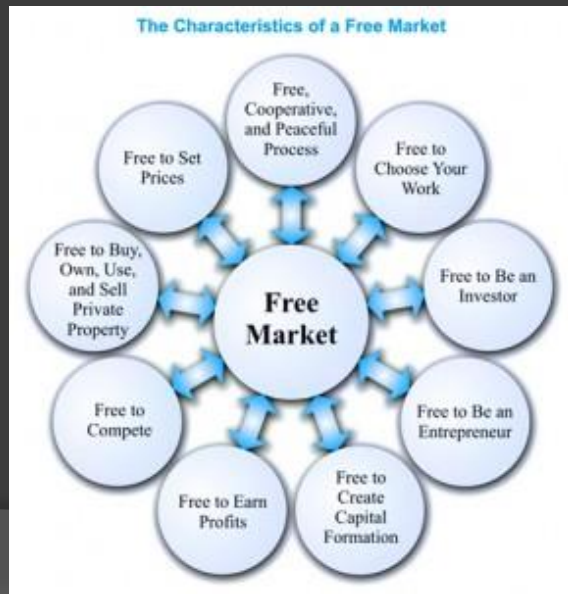
Free-Market Economy

Features:

- The government plays little role in economic activity
- Emphasis is on freedom of the individuals (consumers and producers)
- The private sector (private firms and individuals) answer the basic economic questions.
- There is consumer sovereignty.
- Profit maximization is the main goal in this economy.
- Price drives the economy

Example of Free Market:

There is no real life example of a purely free market economy, this only exists in theory.



Advantages and Disadvantages?

Free Market Economy

Advantages:

1. Manufacturers are free to produce what the consumers demand and the consumers in turn are free to spend their money as they see it fit.
2. The decision of what to produce is not controlled by government or any single individual/firm. Hence, there is greater participation in the decision-making process.
3. A large variety of goods and services are produced to satisfy the needs of consumers.
4. Prices are determined by the forces of demand and supply (the price mechanism).
5. There is freedom from government interference.
6. Efficient production is promoted since resources are allocated to their most profitable use.
7. Competition among firms improves quality, keeps prices low and spurs new technology and innovation.

Disadvantages:

1. Since the making of profits is the dominant motive of the private sector, only goods and services that yield the highest profit will be produced.
2. Since there is no government intervention in this type of system, consumer could be exploited through the charging of high prices for essential goods and services.
3. This system leads to great inequalities as the few rich get richer and the many poor get poorer.
4. There is much pollution associated with this system especially when industrialization begins to develop.
5. There tends to be an over-consumption of demerit goods such as alcohol, cigarettes and drugs

The Free-Market's Self-Regulating Nature

- In every transaction, the buyer and seller consider only their **self-interest**, or their own personal gain. Self-interest is the motivating force in the free market.
- Producers in a free market struggle for the dollars of consumers. This is known as **competition**, and is the regulating force of the free market.
- The interaction of buyers and sellers, motivated by self-interest and regulated by competition, all happens without a central plan. This phenomenon is called “the **invisible hand** of the marketplace.”

Mixed Economies

Features:

- Economic decisions are driven by price and also by the state
- The aim of the private sector is to maximize profits while the aim of the public sector is to maximize social welfare
- The public sector produces goods and services that the private sector is unable or unwilling to produce, with a bureaucratic set up like the planned economy (i.e. freeways)

Examples:

Caribbean Region

United States of America



Advantages and Disadvantages?

Mixed Economies

Advantages:

1. The state can intervene in areas of the economy through the passing of laws to protect citizens from unfair trading practices.
2. Both the government and the private sector can cooperate in offering certain services; e.g. transportation, health care.

Disadvantages:

1. Too much government regulation may dampen the free enterprise spirit.
2. Some state-owned industries are allowed to operate inefficiently, thus wasting resources.
3. Where government intervenes in the market by setting maximum and minimum prices, this may cause excess demand or supply, which may be difficult to regulate in the long-run.
4. Since the private sector helps to answer the economic questions, there can be the creation of monopolies.
5. Inequitable distribution of wealth can also arise.

Comparing Mixed Economies

- An economic system that permits the conduct of business with minimal government intervention is called **free enterprise**. The degree of government involvement in the economy varies among nations.

Continuum of Mixed Economies

Centrally planned

Free market



Source: 1999 *Index of Economic Freedom*, Bryan T. Johnson, Kim R. Holmes, and Melanie Kirkpatrick

Investigating agriculture in countries with different types of economies

- **Activity:** Research agriculture production in three countries
 - What do they produce? How much?
 - Who produces it? How many farms are there?
 - What are food prices like?
- Create a vertical poster of facts to be hung on cabinets

How does the government help and hinder the economy of American Agriculture?

- Guest speaker?
Case study
- A look at subsidies