

Economic Systems

Essential Questions

How do different societies around the world meet their economic systems?

What are the advantages and disadvantages of each system?

Terms to know:

Economics

Economist

Economic System

Problem of Scarcity

Traditional Economic

Subsistence Agriculture

Cottage industry

Free Enterprise/Free Market/Capitalism

Profit

Supply and Demand

Commercial Industry

Command Economy

Socialist Economy

Mixed Economy

NAFTA

Maquiladoras

What is “economics”?

Economics is the study of how individuals, businesses, and nations make things, buy things, spend money and save money. People who study economics are known as **economists**.

The Problem of Scarcity



The basic problem of economics is the problem of scarcity. Something is scarce when we do not have enough of it. There are two basic ideas:

1. People usually have **unlimited wants**. There are many things each of us wants. Even if we had them all, we would still probably find new things we wanted.
2. A society can produce only a limited number of things at any one time. There is only a certain amount of goods and services. Therefore, a society **cannot fulfill everyone's wants**.

What are goods and services?



Goods: are those things that people make: for example, foods, toys, clothes, cars and houses are all considered goods. Department stores, shoe stores, bakeries, and supermarkets all sell goods to consumers.

Services: are those things that people do for others. People who provide services include electricians, teachers, plumbers, barbers, doctors and auto-mechanics.

THE FUNDAMENTAL ECONOMIC QUESTIONS

1. What should be produced?
2. How should it be produced?
3. Who should get it?

Because every society has limited resources, no society has enough goods and services to meet the unlimited needs and wants of all its

members. This problem of scarcity forces every society to answer the questions above.

The way in which society answers these three economic questions is known as its economic system. There are five major types of systems you should know:

1. Traditional
2. Capitalism/Free Market/Free Enterprise
3. Socialist
4. Command
5. Mixed

TRADITIONAL ECONOMY

- The three basic economic questions are answered according to tradition.
- Generally, people do what their ancestors did.
- Tend to be primarily agricultural.
- Usually center around the family or tribal unit.
- People usually don't choose what their position in society will be. They do what their parents did.
- Traditionally marked by **subsistence agriculture** and **cottage industry**.

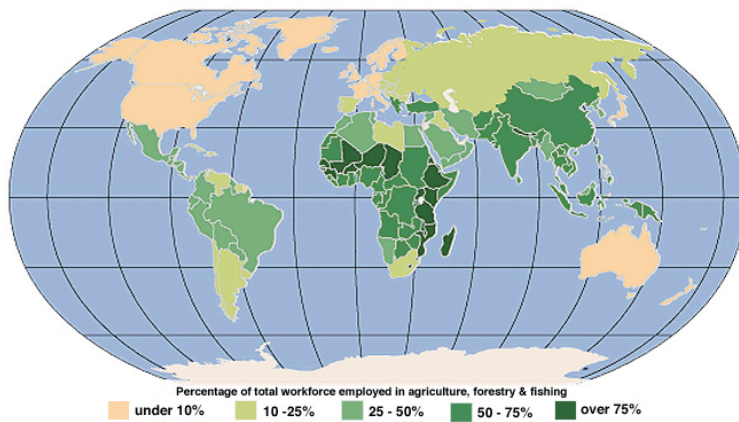


Subsistence agriculture: land usually produces only enough food to feed the farmer and his family. Almost everything grown is intended for the use of the family or the village. There is rarely a surplus, so very little is sold or traded. Economic growth is slow.

Agricultural Societies vs. Industrialized: What are some differences?

- Which would have higher literacy rates?
- Which would have higher birth rates?

- Which would stick closer to traditional beliefs and customs?
- Which would have a higher HDR?



Cottage Industries: primarily in traditional societies, where people use their spare time in their homes to weave cloth, make furniture and clothes, bead necklaces, etc.

- Very common in traditional, agriculture-based societies.
- They help farmers and families meet their financial needs.

CAPITALISM/FREE MARKET/FREE ENTERPRISE ECONOMY



New York Stock Exchange

- People own their own goods and property.
- Some people invest their money in different ways of doing things (businesses, real estate, land)
- People are able to make a **profit**-what remains after the costs of running the business are paid.
- People are free to produce whatever they wish and buy whatever they can afford.
- The three basic questions are answered by the interplay between consumers (buyers) and producers (sellers).

How are prices determined?

Supply and Demand

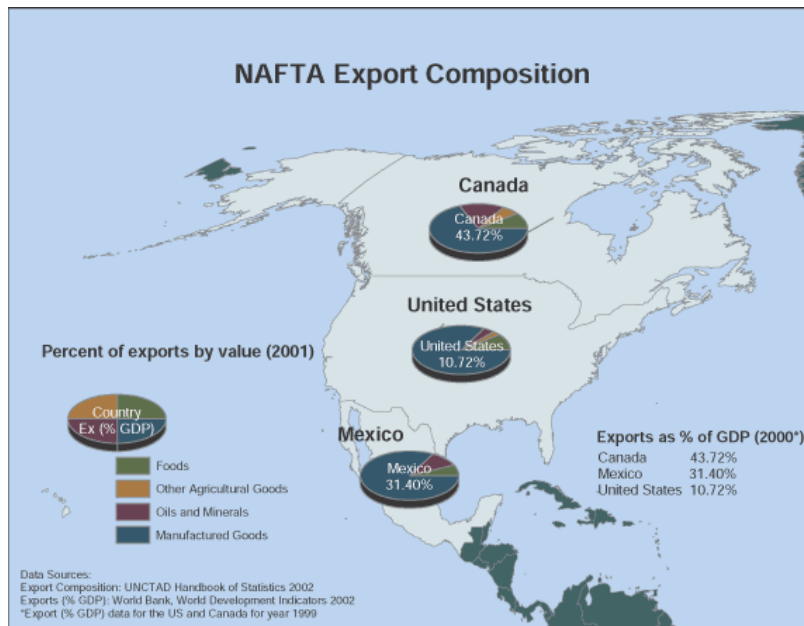
- Supply: how much of a good producers are willing to make and sell.
- Demand: how much of a good consumers are willing to buy.

Low Demand and Large Supply: Prices go: _____

High Demand and Short Supply: Prices go: _____

- An economy based on free enterprise will limit inefficient producers and limit the production of unwanted goods.
- What is the role of government in a free enterprise system?
- Limited government interference, but it still plays a vital role.
- Acts as an umpire
 - Providing and enforcing a set of common rules
 - Maintains a monetary system
 - Provides for the nation's defense
 - Protects people's rights to own property
 - Sometimes people look to governments to break up or regulate companies that have obtained so much power that they could defy market forces

NAFTA (North American Free Trade Agreement)



What is it?

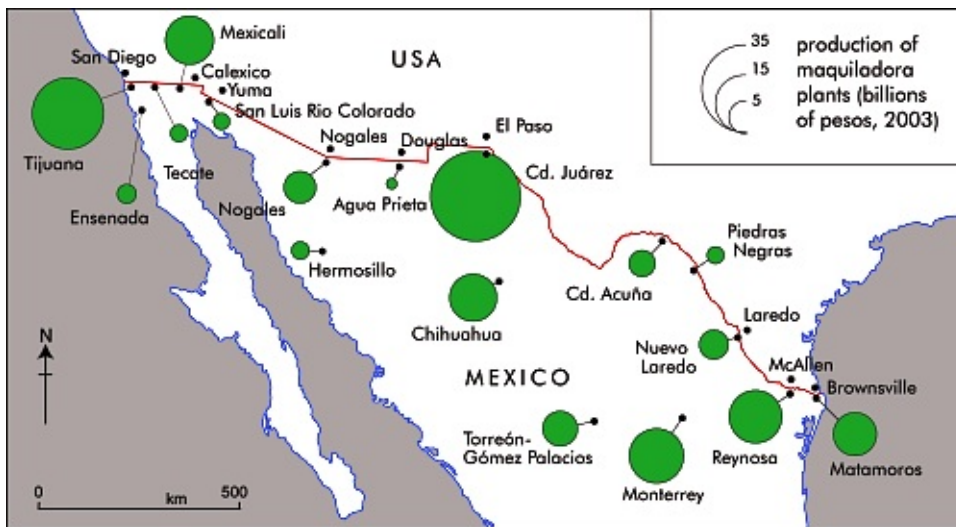
- An economic treaty between Mexico, North America and Canada
- Established in January of 1994
- Designed to increase trade between the three nations by reducing restrictions on commerce, and reducing or eliminating tariffs or import quotas.

- Though it was designed to benefit its member countries, it has been the subject of much controversy since its inception.

Criticisms of NAFTA

1. Labor unions blame the decline of U.S. manufacturing jobs on **outsourcing** to Mexico and Canada

a. Maquiladoras



- A Maquiladora is a factory in Mexico run by a foreign company and exporting its products to the country of that company.
2. Agricultural reforms caused many Mexican farmers to lose their jobs
 - a. As methods of production changed
 - b. And the industry faced more competition from U.S. imports
 3. Debate over environmental regulations

Production Methods

1. Commercial Agriculture: farmers produce for cash, and distribution to wholesalers and retailers like supermarkets.

Large scale makes production much cheaper

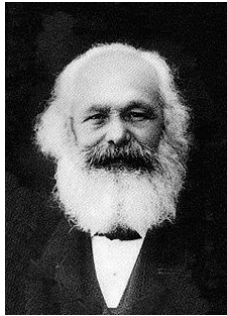
2. Commercial Industries: goods are manufactured in factories for sale throughout the country and overseas.

Examples of Free Market Economies:

- USA
- Great Britain
- France
- Chile
- Canada
- Japan
- Germany
- Singapore

COMMAND ECONOMY

Based on Communist government model.



Karl Marx (1818-1883), believed that business owners (he called capitalists) used their wealth to take advantage of workers. Predicted conditions would grow worse and eventually workers would rise up and overthrow their rulers in a violent revolution.

In theory, there are no social classes on a communist system:

- Cooperation is supposed to replace competition
- Everyone's needs are met

Production Methods

- ALL economic decisions are made by the government
- The leaders decide what, how, and for whom goods and services will be produced
- In theory, production decisions are made for the good of society as a whole
- Governments develop national plans, often for five-year periods that specify which goods each factory will make
- There is NO such thing as private property.

Examples

At one time, there were many. However, these systems were unable to keep up with production in the free enterprise systems:

- Soviet Union (15 member states)
- China
- North Korea
- Vietnam
- Cuba

Today

- North Korea
- Vietnam
- Cuba
- China (Keeping its communist political system, but rapidly moving towards a free market economy. Therefore, it is considered a “Mixed Economy”)

SOCIALISM

- Like command economies, most important businesses producing goods (mines, factories, businesses) are owned by the government, rather than by individuals.
 - Railroads
 - Airlines
 - Hospitals
 - Banks
 - Utility companies
 - Mining or oil companies
 - Other major industries
- Unlike command economies, socialists encourage private ownership of small businesses

Began in the 1800s as a political movement in response to the injustices and exploitations of workers in Europe.

- Many had to work long hours in unsafe conditions for low wages
- People saw the government as the best protector of the workers

Main features of socialism (theories)

1. Government should use its power to bring an end to poverty by taking control of the major resources of the nation and providing public services.

2. Many, but not all, economic decisions are made by the government.

Examples:

Sweden and Israel model their economies on the ideas of socialism

After WWII, most Western European countries became socialist, but in the 1980s and 90s sold off their public ownership of major industries in a wave of “privatization.”

India was socialist from its independence in 1947, but is now moving toward free enterprise.

MIXED ECONOMIES

- In the real world, no economy totally follows one economic system.
- Most countries have economies that blend features of each.
- Countries can be classified on a spectrum from free enterprise to command based on how actively the government intervenes in the economy.