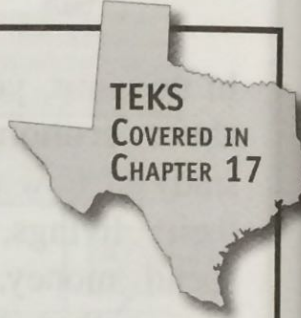


CHAPTER 17

ECONOMIC SYSTEMS

- **Economics 10** The student understands the distribution, characteristics, and interactions of the economic systems in the world.
 - **Economics 10(A)** Describe the forces that determine the distribution of goods and services in free enterprise, socialist, and communist economic systems.
 - **Economics 10(B)** Classify where specific countries fall along the economic spectrum between free enterprise and communism.
 - **Economics 10(C)** Compare the ways people satisfy their basic needs through the production of goods and services such as subsistence agriculture versus commercial agriculture or cottage industries versus commercial industries.
- **Culture 18(C)** Identify examples of cultures that maintain traditional ways, including traditional economies.



**TEKS
COVERED IN
CHAPTER 17**

In this chapter, you will learn how societies have different economic systems — traditional, free enterprise, socialist, or communist. Each of these systems goes about meeting its people's economic needs in different ways.

ESSENTIAL QUESTIONS

- How do different societies around the world meet their economic needs?
- What are the advantages and disadvantages of each economic system?

GEOGRAPHIC TERMINOLOGY IN THIS CHAPTER

- | | | |
|-----------------------|---------------------------|-------------------------|
| ■ Economics | ■ Subsistence Agriculture | ■ Supply and Demand |
| ■ Economist | ■ Cottage Industries | ■ Commercial Industries |
| ■ Economic System | ■ Free Enterprise System | ■ Communist* Economy |
| ■ Problem of Scarcity | ■ Capitalism | ■ Socialist* Economy |
| ■ Traditional Economy | ■ Profit | ■ Mixed Economy |

*A Note about Capitalization: "Communism" and "Socialism" are capitalized when they refer to a specific country or political party, but not when they refer to a general idea, such as "a communist economy."

— IMPORTANT IDEAS —

- A. **Economics** is the study of how people meet their basic needs. All societies must answer three fundamental economic questions: (1) What should be produced? (2) How should it be produced? (3) Who gets what is produced?
- B. How a society answers these three fundamental economic questions determines its type of **economic system**.
- C. In a **traditional economy**, people meet their basic needs much as their ancestors had done. Traditional economies are marked by **subsistence agriculture**, in which families grow just enough to feed themselves. Goods like textiles are produced at home in **cottage industries**.
- D. In a **free enterprise economy**, people are free to produce what they want and to buy what they want. In a free enterprise economy, prices are determined by the forces of **supply and demand**. Food is produced through **commercial agriculture** in which farmers grow food to sell to others, while goods are manufactured through **commercial industries**.
- E. In a **communist economy**, the government owns and operates all businesses. State managers develop a national plan for the production and distribution of all goods and services. Factory managers are given quotas to meet, based on the national plan.
- F. In a **socialist economy**, the government owns and operates many basic industries. Other businesses are privately owned.
- G. Specific countries can be **classified** based on the type of economy they have.

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

Economists believe that the basic problem of economics is the **problem of scarcity**. Something is scarce when we do not have enough of it. The problem of scarcity involves two basic ideas:

- ★ People usually have **unlimited wants**. There are many things each of us wants. Even if we had them all, we would most likely find new things that we wanted.
- ★ A society can produce only a **limited** number of things at any one time. There is only a certain amount of available goods and services. Therefore, a society cannot fulfill all of 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.

APPLYING WHAT YOU HAVE LEARNED

Suppose that everyone in the world were given 10 million dollars. Do you think that would end the problem of scarcity? Explain your answer.

THE FUNDAMENTAL ECONOMIC QUESTIONS

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 three fundamental economic questions:

What should be produced?

How should it be produced?

Who should get it?

TYPES OF ECONOMIC SYSTEMS

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

Traditional

Free Enterprise

Communist

Socialist

TRADITIONAL ECONOMY

In a **traditional economy**, the three basic economic questions are answered according to tradition. Generally, people do what their ancestors did. Traditional economies tend to be primarily agricultural. They usually center around the family or tribal unit. Economic decisions are made on the basis of customs and beliefs that have been handed down from one generation to the next. Individuals do not choose what their position in society will be. They are born in a small village and simply do whatever their parents did. Thus, a child's occupation is determined at birth: the child will follow the example of his or her father or mother. Resources are allocated by inheritance, and tools tend to be primitive. Major occupations in a traditional economy consist of hunting, farming, and herding cattle.



A traditional economy relies heavily on customs and traditions of the past.

MAIN FEATURES OF A TRADITIONAL ECONOMY

Economic Decisions. Custom and tradition determine what should be produced, how it should be produced, and for whom.

Production. The production of goods is based on custom and time-honored methods. New ideas are discouraged. Change and growth proceed very slowly.

Private Property. Often there is no private property: things are owned by the family or village in common.

Trade. Goods and services are produced to meet the needs of the members of the family or tribe. Since they are produced and consumed locally, there is very little trade with outsiders.

PRODUCTION METHODS

Traditional economies are generally marked by **subsistence agriculture** and **cottage industries**.

Subsistence Agriculture. In traditional economies, the land usually produces only enough crops to feed the farmer and his family. Almost everything grown is intended for use by the family or village. There is rarely a surplus, so very little is sold or traded. Economic growth is quite slow. In most of Africa, Asia, and many parts of Latin America, a large percentage of people are primarily involved with feeding themselves from their own land and livestock.

Cottage Industries. In traditional societies, people use their spare time in their home to weave cloth, make furniture and clothes, and to produce other goods by hand. These “cottage industries” are quite common in traditional societies where a large portion of the population is engaged in agriculture. Cottage industries help farmers and their families meet their needs, and may give them extra income during the winter months when there is little work on the farm. Typically, cottage industries involve the entire family working together.



A woman bleaches yarn in a cottage industry.

Examples

Throughout history, most economies have been traditional ones. Today, traditional economies are still found in many rural, non-industrial areas. Traditional economies exist among the Bushmen of the Kalahari Desert of South Africa, the Berber tribesmen of Algeria, and the villages in South Asia.

FREE ENTERPRISE SYSTEM

Free enterprise (also known as *capitalism* or the *free market system*) is an economic system in which people own their own goods and property. Some people invest their money in different ways of producing things (*factories, machines, and land*) or in distributing goods so that they may gain a **profit** — what remains after the costs of running the business are paid. In a free enterprise system, people are free to produce whatever they wish and to buy whatever they can afford. The three basic economic questions are answered by the interplay between consumers (*buyers*) and producers (*sellers*).

HOW PRICES ARE DETERMINED

Prices in a free enterprise system are established by the interaction of supply and demand.

Supply refers to how much of a good producers are willing to make and sell. **Demand** refers to how much of a good consumers are willing to buy. As the diagram shows, when the demand for a good is high, the price goes up. If the supply is high but demand is low, the price goes down. If a producer charges too much for an item, other producers will sell the item at a lower price and outsell that producer.

THE INTERACTION OF SUPPLY AND DEMAND



This interaction between supply and demand is the force behind how resources are allocated. In a free enterprise economy, supply and demand led to the distribution of resources in the most efficient way possible. In this way, an economy based on free enterprise will eliminate inefficient producers and limit the production of unwanted goods.

THE ROLE OF GOVERNMENT

There is limited government interference in the economy in a free enterprise system. However, government still plays a vital role. Government acts as an umpire, providing and enforcing a set of common rules, maintaining a monetary system, providing for the nation's defense, and protecting people's right to own property. In a free enterprise system, people sometimes look to government to break up or regulate companies that have obtained so much power that they could defy market forces.

MAIN FEATURES OF FREE ENTERPRISE SYSTEM

Private Property. People have a right to own private property (*personal possessions, factories, farms, businesses*) and to use this property as they see fit with limited governmental interference.

Free Enterprise. People are free to take part in any business, buy any product, or sell any legal product. Businesses are also free to do anything they wish in order to attract customers — such as lower prices, provide better quality goods, advertise, etc.

Profit Motive. The ability to make profits is what drives people to risk their money in starting a new business.

Supply and Demand. The interaction of supply and demand determines prices in a free market economy. When demand is high, the price goes up. If the supply is high but demand is low, the price goes down.

PRODUCTION METHODS

Unlike traditional economies, free enterprise economies generally have **commercial agriculture** and **commercial industries**. Farmers grow food not just for themselves, but in order to sell it to others for cash. In commercial agriculture, crop production is intended for distribution to wholesalers and retailers, such as supermarkets and grocery stores. Large-scale commercial agriculture makes production cheaper. Farmers can use tractors and other equipment over large tracts of land. In commercial industries, goods are manufactured in factories for sale throughout the country or overseas.

Examples

The free enterprise system exists in such nations as the United States, Great Britain, France, Chile, Canada, Japan, Germany, and Singapore.