**Economic Systems, Goals, and Strategies**

While economists identify **traditional, command, and market** as the three distinct economic systems, real world economies are usually “**mixed**”. They have some characteristics of all three economic systems but tend to lean toward one of the three.

|  |  |  |  |
| --- | --- | --- | --- |
| **Economic System** | **What to produce?** | **How to produce?** | **For whom to produce?** |
| **Traditional** | The economy will produce the goods and services it has produced for generations based on what the ancestors  produced. | The economy will pass the same production methods used in the past from generation to generation. | Goods and services are distributed using the methods used by past generations. |
| **Command** | The economy will produce what the government or central planner says it will produce. | The economy will produce using whatever methods the government or central planner says it will use. | The economy will distribute the goods and services to whomever the government or central planner says  should get it. |
| **Market** | Firms will produce what they believe consumers will want to buy. | Firms will produce goods and services using methods they believe will result in selling goods and services for  the most profit. | Individuals and firms in the society who are willing and able to pay the price of the good or service will obtain it. |
| **Mixed** | Many firms will produce what they believe consumers will want to buy, but government may restrict the production of certain goods or produce public goods. | Firms will try to produce goods and services using methods they believe will result in selling goods and services for the most profit, but the government may tax firm profits or mandate  production processes that minimize harm to the public. | Individuals and firms in the society who are willing and able to pay the price of the good or service will usually obtain it, but the government may restrict some people from  accessing certain goods or may decide to produce a public good  for specific people in the society. |

**Social Economic Goals**

The social economic goals are the values underlying the economic system a country chooses and act as a guiding force as individual, businesses, and governments in the economy make economic choice.

**Economic freedom** ability of consumers, producers, and workers to make their own decisions about consumption, production, and distribution of goods and services. The more individuals and businesses make these decisions, the more economic freedom exists in the economy. Market economies tend to have a great deal of economic freedom while command economies may limit economic freedom in favor of more equal distribution of wealth.

**Economic equity** refers to fairness within the economy. Market economies pursue this goal by ensuring competitive markets and protecting property rights. Command economies pursue this goal by redistributing wealth and ensuring everyone’s access to public goods.

**Economic security** protecting individuals and businesses from risk. In a market economy, individual workers and business owners protect themselves through insurance available in the private market or by saving money for the future. In command economies, the government provides security through government insurance programs, guaranteed jobs, and housing/food allowances.

**Economic growth** is increasing production of goods and services over time. This occurs through increases in factors of production or new technological innovations. Most countries measure growth through calculating the percentage change in real GDP from one period to the next. Real GDP is the total value of all final goods and services produced within a nation in a given time period adjusted for inflation. Command economies can grow rapidly when guided by a central planner. Market economies may grow more slowly, but growth tends to be more sustainable through the organic forces of supply and demand within markets.

**Economic efficiency** when factors of production are allocated to their most productive use. The most efficient economies have fully employed resources, specialize in goods and services for which they have the lowest opportunity cost, and have high levels of competition in the market. Market economies tend to be very efficient due to competition and free trade. Command economies may be less efficient since there is no competition if government owns all the productive resources, everyone has to have a job, and no profit motive drives the people to reduce the costs of production.

**Price stability** refers to an economy making sure that increases in the overall price level of goods and services in the economy is predictable and protects the purchasing power of money in the economy over time. In market economies, price levels can fluctuate with increases and decreases in the business cycle, rising significantly in expansionary times and falling drastically in times of financial crisis. Command economies are more likely to have central authorities who take action against rising or falling price levels through fiscal or monetary policy.

**Full employment** seeks to ensure that all those who are willing and able to work have the opportunity to do so. In the U.S., full employment is typically an unemployment rate between 4% and 6%. Market economies can achieve full employment during strong expansions but will often suffer high levels of unemployment during contractions. Command economies will try to ensure full employment but will often employ resources in less efficient uses and pay income much lower than that found in a market economy.

**Economic sustainability** usually refers to the goal of individual countries to maintain an upward trend of real Gross Domestic Product growth in the long-run. In market economies, sustainability is a goal if firms believe it is in the firm’s self-interest to pursue sustainability. In command economies, the government or central planner will determine the type of sustainability to pursue.

**Allocation Strategies**

* **Price:** This refers to allowing the forces of supply and demand to determine a market price. This allocation strategy allows rationing of a resource based on who can afford the price set by the market. The more desirable and relatively scarce the item, generally, the higher the price. This method is efficient because one can easily tell whether he or she can obtain the good, service, or factor of production based on his or her willingness and ability to pay the price. However, this method will exclude people from markets if they lack the money to pay the price.

**United States Example:** If one would like to obtain a banana, one must pay the price per pound indicated by the grocery store. If one has no money, one gets no banana.

* **Authority:** This strategy is based on the decisions of a power person or group of people who make most of the decisions about who gets to obtain a good, service, or factor of production. This allocation strategy allows for quick action because a person or a group of people in power can make and implement the decisions quickly.

**United States Example:** Elected representatives have the authority to pass legislation requiring workers to pay a tax on the income they earn.

* **Force:** When allocating by force, goods, services, and factors of production are given or taken away under using threats. In countries where the government makes and carries out decisions by force, economic changes can happen quickly because the government decides how to distribute all items and enforces the decision through military/police power.

**United States Example:** When the United States had a military draft during the Vietnam War, the United States arrested those who did not report for military duty.

**Lottery:** also known as random selection, gives everyone who wants the good, service, or factor of production equal odds of obtaining it. This strategy can be inefficient because it may allocate the resource to a purpose or person who does not need it or who will not put it to a productive use. If the government randomly selects individuals to receive farmland, the land may go to someone who has no knowledge of farming techniques and the land resource may be underutilized.

**United States Example:** conscripted military service, force was not the only allocation strategy employed. The lottery held in 1940 - Secretary of War chose a number from a bowl. Nationally, 6,175 men held the number. All of them had to report to their local draft board for military service.

* **First Come, First Served:** allows people to receive a good, service, or factor of production if they get to it first or are one of the people close enough to the front of the line to before there are none remaining. This can be an inefficient strategy since the time spent waiting in a physical or virtual line took time away from more productive activities.

**United States Example:** At one time, a teenager who wanted to take the driver’s license road test had to arrive early and get in line for the opportunity to take the test. The aspiring driver might wait in line all day for the test.

* **Majority Rule:** This strategy occurs when a group of people who have control over a good, service, or factor of production vote to decide how it will be distributed. In the best case, the vote will have a significant majority in favor of the decision and the decision will be in society’s best interest. However, if the majority has a small margin, many people may be unhappy with the decision. If the majority is corrupt or makes the decision based on favoritism or fear, the good, service, or factor of production allocation may not be efficient.

**United States Example:** National, state, and local governments sometimes vote to establish public parks and greenspace. In some cases, there are citizens who would rather the land be used for commercial production. When the majority of elected representatives vote for the public land use, those who favor private ownership of the land are unable to access the factor of production.

* **Personal Characteristic:** This allocation strategy allows resources to be distributed based on need or merit. Ideally, the person who gets the good, service, or factor of production is the one who will put it to the best use. However, personal characteristics can be barriers to keep certain individuals from receiving the allocation.

**Related Terms & Concepts**

**Private ownership** refers to the ability of individuals and businesses in an economy to buy, sell, and hold property as they wish without fear government interference or seizure. The profit motive incentivizes entrepreneurs to take the risk of starting a business.

**Profit** is the amount of revenue (price times quantity sold) received by a business minus the costs of operating the business. If the revenue is greater than the cost of operation, the business will make a profit. This potential reward for the entrepreneur drives them to start businesses.

**Consumer sovereignty** determines the goods and services an economy produces because businesses will only produce those products that consumers are willing to buy.

**Competition** refers the characteristics and behavior firms in a market or industry.

**Government Regulation** refers to the extent to which a central authority has control over the production and consumption decisions in an economy. The chart below provides a comparison of these principles under each economic system.