Chapter 2: Economic Systems
Section 1
Objectives

1. Identify the three key economic questions that all societies must answer.

2. Analyze the societal values that determine how a country answers the three economic questions.

3. Define the characteristics of a traditional economy.
Key Terms

• **economic system**: the structure of methods and principles that a society uses to produce and distribute goods and services

• **factor payment**: the income people receive in return for supplying factors of production

• **profit**: the amount of money a business receives in excess of expenses

• **safety net**: a set of government programs that protect people who face unfavorable economic conditions
Key Terms, cont.

- **standard of living**: level of economic prosperity
- **innovation**: the process of bringing new methods, products, or ideas into use
- **traditional economy**: an economic system that relies on habit, custom, or ritual to decide the three key economic questions
Introduction

• What goals and values affect how a society answers the key economic questions?
  – Each society is guided by its economic system, which affects the way in which it does business within the society itself and with other societies.
  – A society’s values, such as freedom or tradition, guide the type of economic system that society will have.
Three Economic Questions

• As a result of scarce resources, societies must answer three key economic questions:
  – What goods and services should be produced?
  – How should these goods and services be produced?
  – Who consumes these goods and services?

• How a society answers these three questions defines the type of economic system that society has.
Questions 1 and 2

• What goods and services should be produced?
  – Each society must decide what to produce in order to satisfy the needs and wants of its people.
  – Because resources are limited, each decision that a society makes about what to produce comes at an opportunity cost.

• How should goods and services be produced?
  – As a society decides how to produce its goods and services, it must consider how best to use its land, labor, and capital.
Combining Factor Resources

**Hand Tools**

1 acre of land + 56 worker-hours + capital = 15 bushels of wheat

**Modern Mechanical Equipment**

1 acre of land + 2.9 worker-hours + capital = 40 bushels of wheat
Question 3

• Who consumes goods and services?

  – This question is largely determined by how societies distribute income.
  – Through factor payments, including profits, societies can determine who will be the consumers of the goods and services produced.
Economic Efficiency

• Societies answer the three economic questions based on the importance they attach to various economic goals.

• Because resources are always scarce, societies try to maximize what they can produce using the resources they have.
  – If a society can accurately assess what to produce, it increases economic efficiency.
Economic Freedom and Security

• Some societies limit the economic freedoms of its people.
  – In the United States, Americans face some limitations but, in general, we enjoy a large amount of economic freedom.

• Economic systems also strive to achieve a certain degree of economic security.
  – Ideally, economic systems seek to reassure people that goods and services will be available when needed and they can count on receiving expected payments on time.
Economic Equity

• Economic equity is another economic goal that is defined differently in different societies. Each society must decide how to divide its economic pie.

• Checkpoint: What are two examples of economic goals?
Economic Growth

- A society also strives for economic growth. A nation’s economy must grow so it can provide jobs for the new people joining the workforce.
  - A nation strives to improve its standards of living.
  - Innovation plays a huge role in economic success as well.
Economic Goals in Conflict

• There are some additional economic goals for certain societies, including environmental protection, full employment, and protecting national industries.

• All societies must prioritize their economic goals, or arrange them in order of importance. Each choice comes with some kind of trade-off.
Traditional Economies

• The oldest and simplest economic system is known as a traditional economy.

  – Traditional economies rely on habit, custom, or ritual and revolve around the family. There is little room for innovation or change.
• Traditional economies are usually found in communities that tend to stay small and close.

– Often these societies work to support the entire community, rather than just themselves or their immediate families.
Traditional Economies, cont.

- Societies with traditional economies are successful if they meet their own needs.
  - In many cases, these communities lack modern conveniences and have a relatively low standard of living.
Review

• Now that you have learned about the goals and values that affect how a society answers the key economic questions, go back and answer the Chapter Essential Question.
  – How does a society decide who gets what goods and services?