

# CHAPTER 26

## ★ CAPITALIST AND MIXED SYSTEMS

- What should be produced?
- How should it be produced?
- For whom should it be produced?

The four resources of an economic system are called factors of production. Land includes natural resources. Labor is human resources, or workers. Capital is the means of production, such as money

Communism is a command system in which the central government directs all major economic decisions. Socialism is a partial command system in which government agencies influence many economic decisions. Capitalism is a market system in which private business persons make the economic decisions. Capitalism is the basic economic system of the United States.

The United States has a mixed economy, or modified capitalism, because the government regulates business and labor and assumes responsibility for fiscal, monetary, and social policy.

- private ownership of the means of production
- individual initiative—anyone can become an entrepreneur
- competition among sellers
- freedom of choice for consumers
- profit—the reward an entrepreneur earns for taking the risk of producing

**★ EMERGING ECONOMIES**

Socialists believe that wealth should be distributed equally. Socialist governments use high taxes to provide citizens with lifelong benefits such as medical care. Critics claim such policies create a welfare state by making people dependent on the government.

rapid industrial growth. Other policies used by socialist governments include agricultural communes, redistribution of land, and nationalization—government control of existing industries. Centralized state planning failed to meet consumer needs in eastern Europe, which has raised doubts about the wisdom of socialism.

Some newly independent African nations chose socialism because they viewed capitalism as an extension of colonialism. Frequently they combined socialist ideas with African traditions such as communal land ownership and group decision making. Because crises weakened their economies and left them in debt, some have formed regional trade associations and have turned to free enterprise.

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**CHAPTER 26 SUMMARY CONTINUED****★ MAJOR ECONOMIES IN TRANSITION**

Beginning in 1917, the Soviet Union built the world's leading Communist system. The Communist Party closely controlled the government and made almost all economic decisions. Enterprises and farmland were state-owned and state-operated. The controlled economy led to economic stagnation. Mikhail Gorbachev, the last Communist leader, attempted economic reforms, but the Soviet economy continued to decline. In 1991 Gorbachev resigned, and several Soviet republics declared their independence, effectively ending the Soviet Union.

Since the collapse of communism, Russia has tried to continue moving toward capitalism and democracy. However, today Russia is being run much as it was under communism—and by many of the same leaders. In the last few years, under the leadership of Vladimir Putin, efforts at democratization have slowed.

The Chinese Communist government followed the model of the Soviet Union's planned economy until it found itself

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unable to compete economically in the 1970s. Since then, China's Communist leaders have begun to encourage private enterprise and the economy has started to grow rapidly. A large labor force, tax and land incentives for foreign companies, and advanced communications technologies have all assisted rapid economic development. China is attempting to move toward a market economy while maintaining an authoritative political system; however, the growing middle class, combined with increasing political corruption, present challenges to the Communist Party's continued leadership.

Trade with China has opened new markets for American goods, though competition with Chinese labor costs has driven many American manufacturers out of business. American experts worry that an economically strong China could become a dangerous political and military rival.

**★ THE GLOBAL ECONOMY**

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The major activity in the global economy is trade among nations. Nations engage in trade for several reasons: (1) to obtain goods and services they cannot produce themselves; (2) comparative advantage, or the principle that each country should produce those goods it can make more efficiently and purchase those that other nations produce more efficiently in order to increase the total world production; and (3) to create jobs.

Unrestricted trade can threaten domestic industries and the jobs of workers in those industries. As a result, national governments use several methods to restrict international trade:

- Tariffs are taxes placed on imports to increase their price in the domestic market.
- Quotas are limits on the quantities of a foreign product that may be imported.
- Non-tariff barriers (NTBs) limit or control unwanted imports by setting very strict health, safety, or other regulations that must be met before a foreign product can be offered for sale.
- Embargoes totally bar trade.

Countries may also engage in unfair trade practices such as dumping, or selling products far below their manufacturing cost in order to drive other producers out of a market.

After World War II, the major economic nations created trading blocs, or groups of nations that trade without barriers such as tariffs. The General Agreement on Tariffs and Trade (GATT), an effort to reduce trade barriers, has been signed by over 100 nations since it was first enacted in 1947. In 1994 GATT was replaced by a regulatory body known as the World

Trade Organization (WTO), which hears complaints brought to it by member countries and has the authority to penalize nations that violate the GATT treaty. The European Union (EU), currently made up of 15 European nations, is the world's most important economic group; the EU achieved monetary integration with the adoption of the euro in 2002. The North American Free Trade Agreement (NAFTA) is an agreement to reduce and eventually end most trade restrictions between the United States, Canada, and Mexico.

Nations must decide on the best approach to trade policy:

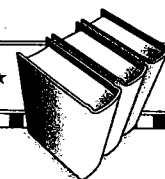
- A pure free-trade policy would mean that businesses in different nations could buy and sell goods with no tariffs or other limitations of any kind.
- The United States advocates a fair trade policy, which means supporting an orderly world market that does not give an unfair advantage to countries that use unfair business practices.
- With a managed trade policy, governments intervene in trade agreements in order to achieve a specific results.
- Protectionism is the policy of using trade barriers to protect domestic industries from foreign competition and to prevent unrestricted trade.

Globalization has brought the American consumer new and more varied products at lower prices. However, the American worker must now compete with a wider labor pool, and economic and political decisions are now much more complicated.



## Guided Reading Activity 26-1

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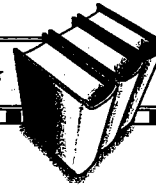
### Capitalist and Mixed Systems

**★DIRECTIONS** Use the information in your textbook to choose the word or phrase that completes each sentence correctly.

1. A condition that exists because society does not have all the resources to produce needed goods is called \_\_\_\_\_.
2. Habit and custom dictate the rules for all economic activity in a \_\_\_\_\_ economy.
3. Government agencies determine people's needs and direct resources to meet them in a \_\_\_\_\_ economy.
4. When buyers and sellers determine what, how, and for whom goods and services are produced, the economy is called a \_\_\_\_\_ economy.
5. Resources used to produce goods and services are called \_\_\_\_\_.
6. An entrepreneur is a person who \_\_\_\_\_.
7. A command system in which the central government directs major decisions is \_\_\_\_\_.
8. A partial command system in which the government influences many economic decisions is called \_\_\_\_\_.
9. A system in which consumers and private owners make the decisions in free markets is called \_\_\_\_\_.
10. Most countries in the world today have a \_\_\_\_\_ economic system.
11. Another name for a capitalist system is a \_\_\_\_\_ system.
12. Capitalist economies depend on the right of \_\_\_\_\_ of property and control of economic resources.
13. A situation in which there are several sellers of a product or service and no single seller can have control over its market price is known as \_\_\_\_\_.
14. An industry dominated by only one seller, resulting in no competition, is a \_\_\_\_\_.
15. A situation in which a few large firms dominate an industry is a(n) \_\_\_\_\_.
16. The difference between the amount of money used to operate a business and the amount of money the business takes in is called \_\_\_\_\_.
17. An economic system that combines private ownership with the government's role in fiscal and monetary policy is \_\_\_\_\_.



# Guided Reading Activity 26-2



## Emerging Economies

**★DIRECTIONS** Use the information in your textbook to list the pros and cons of economic choices facing developing nations.

	Advantages	Disadvantages
1. Capitalist free markets		
2. Socialist central planning		

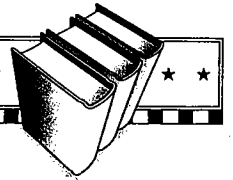
**★DIRECTIONS** Use the information in your textbook to identify the following items.

- developing nations: \_\_\_\_\_
- newly developed nations: \_\_\_\_\_
- welfare state: \_\_\_\_\_
- centralized planning: \_\_\_\_\_
- nationalization: \_\_\_\_\_



# Guided Reading Activity 26-3

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## Major Economies in Transition

**★DIRECTIONS** Use the information in your textbook to complete this table describing the problems with, changes in, and future of the Russian and Chinese economies.

	PROBLEMS	CHANGES	FUTURE
Russia/USSR			
	PROBLEMS	CHANGES	FUTURE
China			

**★DIRECTIONS** Use the information in your textbook to match the items in Column A with their descriptions in Column B. Write the correct letter in the space provided.

### Column A

- \_\_\_\_\_ 1. gross national product
- \_\_\_\_\_ 2. state farms
- \_\_\_\_\_ 3. collective farms
- \_\_\_\_\_ 4. Soviet central planning
- \_\_\_\_\_ 5. Mikhail Gorbachev
- \_\_\_\_\_ 6. Vladimir Putin
- \_\_\_\_\_ 7. China
- \_\_\_\_\_ 8. KGB
- \_\_\_\_\_ 9. planned economy
- \_\_\_\_\_ 10. Chinese Communist Party

### Column B

- A.** booming market economy
- B.** president of Russia who prescribed "strengthening of the state" to cure economic ills
- C.** Chinese economy after World War II until the 1970s
- D.** the sum of a nation's goods and services
- E.** maintains control of Chinese government
- F.** farms that were owned by the Soviet government and run like factories, with the workers being paid wages
- G.** Soviet secret police
- H.** Soviet president who tried to improve the economy through economic reforms
- I.** created major problems in Soviet factories and farms
- J.** system in which the Soviet government owned farmland and rented it to the families who would raise food products



# Guided Reading Activity 26-4







## The Global Economy

**★DIRECTIONS** Use the information in your textbook to identify the following items.

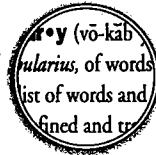
1. comparative advantage: \_\_\_\_\_
2. tariff: \_\_\_\_\_
3. quota: \_\_\_\_\_
4. trading bloc: \_\_\_\_\_
5. two leading regional economic blocs: \_\_\_\_\_
6. European Union: \_\_\_\_\_
7. "euro": \_\_\_\_\_
8. protectionism: \_\_\_\_\_
9. dumping: \_\_\_\_\_
10. non-tariff barriers: \_\_\_\_\_

**★DIRECTIONS** Use the information in your textbook to complete this diagram. Briefly explain each alternative in the answer box below each heading.

TRADE ALTERNATIVES FOR THE UNITED STATES			
Free Trade	Fair Trade	Managed Trade	Protectionism
			



# Vocabulary Activity 26



## Development of Economic Systems

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**DIRECTIONS** → Select the term that matches each definition below. Write the correct term in the space provided.

factors of production	traditional economy	developing nations
scarcity	quotas	newly developed nations
market economy	command economy	tariffs
profit	entrepreneur	revitalization

1. A person who takes a risk to produce goods and services in search of profit \_\_\_\_\_
2. The sum of all the nation's goods and services \_\_\_\_\_
3. A system in which a central authority makes most economic decisions \_\_\_\_\_
4. Taxes placed on imports to increase their price in the domestic market \_\_\_\_\_
5. The amount of money a business earns minus the amount used to operate it \_\_\_\_\_
6. A condition that exists because society does not have all the resources to produce all the goods and services that everyone wants. \_\_\_\_\_
7. States with little or no industry \_\_\_\_\_
8. The resources which economies must have to produce goods or services \_\_\_\_\_
9. Limits on the quantities of a product that may be imported \_\_\_\_\_
10. A system in which habit and custom dictate the rules for all economic activity, determining what, how, and for whom goods and services are produced \_\_\_\_\_
11. States that have had significant or rapid industrial growth in recent years \_\_\_\_\_
12. A system that allows buyers and sellers acting in their individual interests to determine what, how, and for whom goods and services are produced \_\_\_\_\_

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**DIRECTIONS** → Use each of the following terms correctly in a complete sentence. Write the sentences on a separate sheet of paper.

nationalization	monopoly	mixed economy	welfare state
trading blocs	state farm	collective farm	comparative advantage

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# Reteaching Activity



## Development of Economic Systems

### DIRECTIONS

Each main idea is related to the topic given. Complete the chart by writing the letter of the item that supports each main idea.

ECONOMIC DECISIONS AFFECT CITIZENS AND THE GLOBAL ECONOMY			
Main Idea	Main Idea	Main Idea	Main Idea
Capitalism is the basic economic system of many industrialized nations.	As developing nations move toward industrialization, they deal with economic problems in a variety of ways.	Many nations today are attempting to make the transition from a command economy to a market economy.	The global economy makes nations interdependent.
Supporting Details	Supporting Details	Supporting Details	Supporting Details

- A. Russia's attempt to transform its economy is limited by bureaucrats unwilling to relinquish power and a long-standing tradition of totalitarian rule.
- B. A free enterprise system has five characteristics, including private ownership, individual initiative, competition, freedom of choice, and profit or loss.
- C. Nations engage in international trade to obtain goods and services they cannot produce, to increase total world production, and to create jobs.
- D. While some developing nations have instituted capitalist economies, many others have chosen socialism.
- E. GATT, NAFTA, and the EU reduce barriers to trade and encourage regional economic cooperation.
- F. Soviet farm workers had little incentive to work hard on vast state-run farms, and inefficiency was widespread.
- G. The United States government plays an important role in regulating business, agriculture, labor, and fiscal and monetary policy.
- H. Governments may try centralized planning or nationalization to achieve rapid growth and raise the standard of living for large masses of poor people.
- I. By the late 1970s, China found itself unable to compete with the market-based economies of neighboring countries.
- J. In Japan, Singapore, Taiwan, and South Korea the government works closely with private businesses to limit foreign competition in the domestic market.
- K. Four major types of trade policy are free trade, fair trade, managed trade, and protectionism.
- L. Israel and some African nations incorporate communal agriculture into their economies.



# CHAPTER SUMMARY Activity



## Development of Economic Systems

**★DIRECTIONS** Match each term in Column A with the statement that best applies to it in Column B. Write the correct letters in the spaces provided.

### COLUMN A

- \_\_\_\_\_ 1. command economy
- \_\_\_\_\_ 2. factors of production
- \_\_\_\_\_ 3. capitalism
- \_\_\_\_\_ 4. developing nations
- \_\_\_\_\_ 5. newly developed nations
- \_\_\_\_\_ 6. nationalization
- \_\_\_\_\_ 7. quotas
- \_\_\_\_\_ 8. gross national product
- \_\_\_\_\_ 9. comparative advantage
- \_\_\_\_\_ 10. regional trading blocs

### COLUMN B

- A.** Private ownership, individual initiative, competition, freedom of choice, and profit characterize this economic system.
- B.** The socialist policy in which the government takes control of existing industries.
- C.** The theory which holds that each country should produce those goods it can make more efficiently and import others.
- D.** The central government decides what, how, and for whom goods are produced.
- E.** This is the annual sum of a nation's goods and services.
- F.** Groups of nations that trade without barriers such as tariffs.
- G.** These resources of an economic system include land, labor, capital, and entrepreneurs.
- H.** States that recently have experienced significant industrial growth.
- I.** These are limits on the quantities of a foreign product that may be imported.
- J.** States that have little or no industry.

**Organizing Information** Write each item from the list below under the appropriate heading.

ECONOMIC SYSTEMS	
Command Economy	Market Economy

- profit
- nationalization
- state farms
- centralized planning
- competition
- private ownership
- equal distribution of wealth
- individual initiative

**Critical Thinking** Answer the following question on a separate sheet of paper.

11. How do consumers everywhere benefit from the elimination of tariffs and import quotas?