

ECONOMIC UNDERSTANDINGS

SS6E5. The student will analyze different economic systems.

- a. Compare how traditional, command, and market economies answer the economic questions of 1-what to produce, 2-how to produce, and 3-for whom to produce.

ANSWERING ECONOMIC QUESTIONS

Scarcity is the limited supply of something. Every country must deal with the problem of scarcity. No country has everything that its people want and need. As a result, every country develops an **economic system** to determine how to use its limited resources to answer the three basic economic questions: (1) *What* goods and services will be produced? (2) *How* will goods and services be produced? (3) *Who* will consume the goods and services? The way a society answers these questions determines its economic system.

Traditional Economy

In a **traditional economy**, the customs and habits of the past are used to decide what and how goods will be produced, distributed, and consumed. In this system, each member of the society knows early in life what his or her role in the larger group will be. Since jobs are handed down from generation to generation, there is very little change in the system over generations. In a traditional economy, people are depended upon to fulfill their traditional role. If some people are not there to do their part, the system can break down. Farming, hunting and gathering, and cattle herding are often a part of a traditional economy. There are no examples of a traditional economy in Europe.

Command Economy

In a centralized **command economy**, government planning groups make the basic economic decisions. They determine such things as which goods and services to produce, the prices, and wage rates. Individuals and corporations generally do not own businesses or farms; these are owned by the government. Workers at a business are told what to produce and how much to produce in a given time. The expectation is that everyone in the country will be able to have the goods they need when they need them. The former Soviet Union was an example of a command economy. After it collapsed in 1991, the new Russian Federation adopted a more mixed economy. However, the Russian economy is still less free than most other European countries. The government owns many of the large businesses and has many limits on private ownership.

Market Economy

In a decentralized **market economy**, decisions are guided by changes in prices that occur between individual buyers and sellers in the marketplace. Other names for market systems are **free enterprise**, **capitalism**, and **laissez-faire**. In a market economy, individuals or corporations generally own businesses and farms. Each business or farm decides what it wants to produce.

Most of Europe operates in a market economy. The United Kingdom has a market economy. It is considered one of the most **free economies** in Europe. "Free" means that businesses can operate without too many rules from the government. People are free to start a business and can do so quickly. Courts use the laws of the U.K. to protect the property rights of citizens.

- _____ 375. In the United Kingdom, who decides which goods will be produced and sold?
- A. citizens
 - B. the monarch
 - C. business owners
 - D. the prime minister
- _____ 376. Which country owns most of the large and important industries within its borders?
- A. Germany
 - B. Russia
 - C. United Kingdom
 - D. none of these
- _____ 377. Which is LEAST likely to be found in Europe?
- A. capitalism
 - B. market economy
 - C. command economy
 - D. traditional economy

Use information from the table to answer questions 380-382.

Comparing the Economies of the United Kingdom, Germany, and Russia

	United Kingdom	Germany	Russia
Who owns businesses and farms?	private citizens and corporations	private citizens and corporations	the government owns large industries such as shipping, oil and natural gas, and aerospace technology; private ownership is allowed in other areas
Who decides what to produce and how much to produce?	private citizens and corporations	private citizens and corporations; there is some regulation by the government in agriculture, energy, and telecommunications	private citizens and corporations for the most part; the government has many restrictions on businesses and controls many of the larger ones
Who decides how goods and services will be produced?	private citizens and corporations	private citizens and corporations; there is some regulation by the government in agriculture, energy, and telecommunications	private citizens and corporations for the most part; the government has many restrictions on businesses and controls many of the larger ones
Who decides distribution methods and prices for goods and services?	private citizens and corporations	private citizens and corporations; there is some regulation by the government in agriculture, energy, and telecommunications	private citizens and corporations for the most part; the government has many restrictions on businesses and controls many of the larger ones
Who decides the prices for goods and services?	buyers and sellers, based on supply and demand	private citizens and corporations; the government regulates prices of some products	private citizens and corporations; the government regulates prices of some products
How are property rights protected?	laws and a good court system protect people's property rights	laws and a good court system protect people's property rights	court system does not always protect the rights of property owners
How difficult is it to start your own business?	very easy (days)	very easy (days)	time-consuming (months)

_____ 380. In which country would it be most difficult for a person to start a business?
A. Russia
B. Germany
C. United Kingdom
D. about the same for each

_____ 381. In which countries do buyers and sellers usually come to agreement on prices in order to trade?
A. Russia and Germany
B. Russia and United Kingdom
C. Germany and United Kingdom
D. United Kingdom and United States

_____ 382. Which of these issues would make the United Kingdom a more desirable place to start a business than Russia?
A. The government in Russia owns most industries.
B. Russia's court system always protests the rights of property owners..
C. It takes less time to start a business in Russia than the United Kingdom.
D. Private citizens and corporations in the United Kingdom decide how goods will be produced.

SS6E6 The student will analyze the benefits of and barriers to voluntary trade in Europe.

- a. Compare and contrast different types of trade barriers such as tariffs, quotas, and embargos.

TRADE BARRIERS: TARIFFS, QUOTAS, AND EMBARGOS

Trade is the voluntary exchange of goods and services among people and countries. Trade and voluntary exchange occur when buyers and sellers freely and willingly engage in market transactions. When trade is voluntary, both parties benefit and are better off after the trade than they were before the trade.

Countries sometimes try to limit trade with other countries by creating **trade barriers**. The most common types of trade barriers are **tariffs** and **quotas**. A tariff is a tax on imports. A quota is a limit placed on the number of imports that may enter a country. Another kind of trade barrier is an **embargo**. An embargo is a government order stopping trade with another country. An embargo might be put into place in order to put pressure on another country.

The European Union (EU) is a large **free-trade zone**. There are no tariffs between the countries in the zone. This means that goods can be bought for a lower price. In Russia, there are tariffs on many imports. The Russian government hopes that the tariffs help Russian workers and businesses. Food imported from Germany may have a high tariff placed on it. Therefore, Russian families might choose to buy food grown by Russian farmers.

Russia produces a lot of steel. Steelmakers in the EU may worry that if too much Russian steel comes into the EU, the price of steel will go down. If the price goes down, the EU companies would have trouble making enough money to stay in business. The EU might decide to put a quota on steel imports from Russia. A quota would stop the flow of steel into EU countries, which would keep the prices stable.

- ___ 383. Which type of trade barrier involves a limit on goods brought into the country?
- A. quota
 - B. tariff
 - C. embargo
 - D. voluntary exchange
- ___ 384. In order to help Russian farmers sell more food, some people want to put a tax on the food imported from other countries. This is an example of a(n)
- A. quota.
 - B. tariff.
 - C. embargo.
 - D. voluntary exchange.
- ___ 385. Which might make an embargo against a country successful?
- A. Merchants are able to continue doing business.
 - B. People in the country are not affected by the embargo.
 - C. The country does not need to trade with other countries.
 - D. The citizens in the country suffer because of the embargo and demand a change from their government.

SS6E6 The student will analyze the benefits of and barriers to voluntary trade in Europe.

b. Explain why international trade requires a system for exchanging currencies between nations

INTERNATIONAL TRADE AND THE EXCHANGING OF CURRENCIES

Currency is the money people use to make trade easier. In the United States, we use U.S. dollars (USD or \$) to buy goods and services. When we Americans work at a job, we are paid in dollars. Most of the time, when you are in a different country, you cannot buy goods and services with currency from your own country. So what do you do? You trade it in, or exchange it! With each exchange, however, the bank charges a fee. A business that exchanges a lot of money will pay many fees.

Imagine an olive farm in Greece. The olive grower pays his workers in euros. He buys fertilizer and pesticide in euros. He pays for water and machinery in euros. When the olives are ripe, a store in Russia wants to buy them. The Russian storeowner has **rubles** (the Russian currency) to spend. In order to make the trade, the Russian storeowner exchanges his rubles for euros. The bank where he makes the trade charges a fee. The olive grower gets money for the olives in euros. The Russian gets the olives. Everyone is happy!

More than half of the EU countries use the euro today. This makes trade among the EU countries easier because they do not have to exchange currency. It also makes trade less expensive because people don't have to pay banks a fee to exchange their currency.

____ **386. What is the currency people use in much of the EU called?**

- A. euro
- B. ruble
- C. dollar
- D. pound

____ **387. What is the currency of Russia?**

- A. euro
- B. ruble
- C. dollar
- D. pound

____ **388. What is a problem with exchanging currency?**

- A. People make more money by trading currency.
- B. Most people want to use American dollars to trade.
- C. Banks do not like to exchange their money for other currencies.
- D. It costs more to do business because banks charge fees for exchanges.

SS6E7 The student will describe factors that influence economic growth and examine their presence or absence in Europe.

- a. Explain the relationship between investment in human capital (education and training) and gross domestic product (GDP).

HUMAN CAPITAL AND THE GROSS DOMESTIC PRODUCT

The **Gross Domestic Product (GDP)** of a country is the total value of all the goods and services produced in a country in one year. The GDP is one way to tell how rich or how poor a country is. The GDP can be used to tell if the economy of a country is getting better or getting worse. Raising the GDP of the country can mean a higher **standard of living** (economic level) for the people in the country. To increase the GDP, countries must invest in **human capital**. This resource includes the education, training, skills, and health of the workers in a business or country.

Russia, Germany, and the United Kingdom have made large investments in human capital. The **literacy rate** of each country is nearly 100 percent. The workforce is very well trained and educated. This has helped the standard of living in these countries improve over time.

Russia has the most poverty of the three countries. The Russian government is spending large amounts of money to train workers and to educate youth so that they will have more opportunities to be successful in the economy. In the former Soviet Union, everyone was assigned a job. Today, in Russia, workers must show they are skilled and valuable to the business in order to keep their jobs.

- _____ 389. Which is an example of investing in human capital?
- A. cash
 - B. factories
 - C. highways
 - D. education
- _____ 390. A country that does not invest in human capital will have problems because
- A. there will be no money to pay its workers.
 - B. workers will learn on their own the skills they need.
 - C. businesses will not pay the taxes to pay for good schools.
 - D. workers who are not educated, skilled, and healthy are less productive.
- _____ 391. What is human capital?
- A. a country's standard of living
 - B. the cash a business has to spend
 - C. investment in the workers of a business or country
 - D. the buildings, equipment, and property owned by a business

SS6E7 The student will describe factors that influence economic growth and examine their presence or absence in Europe.

b. Explain the relationship between investment in capital (factories, machinery, and technology) and gross domestic product (GDP).

CAPITAL INVESTMENTS AND THE GROSS DOMESTIC PRODUCT

To raise the Gross Domestic Product (GDP), countries must invest in *physical capital*. Physical capital is the factories, machines, technologies, buildings, and property needed by businesses to operate. If a business is to be successful, it cannot let its equipment break down or have its buildings fall apart. New technology can help a business produce more goods for a lower price.

The former Soviet Union did not do a good job of investing in physical capital. Highways and buildings are in need of repair. Factory equipment and technology are out of date. These conditions are keeping workers from being as productive as workers in the EU. Today, the Russian Federation has the job of helping companies overcome this problem. To solve the problem, the government has a plan to invest \$1 trillion over the next few years in capital improvements.

- _____ 392. Which is an example of investing in physical capital by a company?
- A. constructing a new factory
 - B. keeping old delivery trucks
 - C. training workers to do their jobs better
 - D. keeping old computers in order to save money
- _____ 393. The Soviet Union did not invest in capital improvements, so Russian workers today
- A. do not want to increase their standard of living.
 - B. are not as productive as workers in other countries.
 - C. work in brand new factories and are very productive.
 - D. have shut down their factories until new ones are built.

SS6E7 The student will describe factors that influence economic growth and examine their presence or absence in Europe.

c. Describe the role of natural resources in a country's economy.

THE ROLE OF NATURAL RESOURCES IN A COUNTRY'S ECONOMY

A country has different kinds of resources that can help its people produce goods and services. Human resources are the education and skills that people have to produce goods and services. Capital resources are the things like machines and equipment that people need to produce goods and services. Natural resources, "gifts of nature," include forests such as those in southern Germany. They include fertile soil, such as the farms of the United Kingdom. Water is another natural resource. Russians use their water resources by damming rivers and creating hydroelectric power.

Natural resources are important to countries. Without natural resources of their own, countries must import the natural resources that they need. This adds to the cost of goods and services. A country is better off if it can use its own natural resources to supply the needs of its people. It can also use the natural resources to create goods that can be traded to other countries. If a country has many natural resources, it can trade these to other countries for goods and services it needs.

In Europe, many countries have used up much of their nonrenewable natural resources. They have had to find other ways to make their economies work. For example, coal was once a plentiful resource in the United Kingdom. Today, most of the supply has been used. Russia is a major exporter of oil and natural gas. Money from these resources has helped many Russians become wealthy. However, these resources will not last forever. Russia must find ways to not only use these resources but also develop other ones.

- _____ **394. Which is an example of a natural resource?**
- A. forests
 - B. highways
 - C. education
 - D. automobiles
- _____ **395. Which natural resources have helped the Russian economy in the twenty-first century?**
- A. oil and natural gas
 - B. highways and factories
 - C. machines and equipment
 - D. education and health care
- _____ **396. Why is a country better off if it does not have to import natural resources?**
- A. Other countries may need the resources.
 - B. Buying from other countries costs more money.
 - C. People in other countries don't want to sell their natural resources.
 - D. Businesses have a hard time using the natural resources that are located nearby.

SS6E7 The student will describe factors that influence economic growth and examine their presence or absence in Europe.

d. Describe the role of entrepreneurship.

THE ROLE OF ENTREPRENEURSHIP

The person who provides the money to start and own a business is called an **entrepreneur**. Entrepreneurs risk their own money and time because they believe their business ideas will make a profit. They must organize their businesses well for those businesses to be successful. Entrepreneurs bring together natural, human, and capital resources to produce goods or services to be provided by their businesses.

In Europe, Russia is a country that has many entrepreneurs. Laws have made it easier than it used to be to own a business. Russia's natural resources and skilled labor make it a good place to have a business. In the twenty-first century, many entrepreneurs in Russia are getting rich. Russia is one of the top five countries in the number of billionaires. Still, doing business in Russia is difficult. Entrepreneurs say that the government needs to do a better job of protecting private property. The courts need to be stronger to protect businesses. It can take months for an entrepreneur to get the proper permissions to start a business.

Entrepreneurs play an important role in the economy of a country. As they work to make their businesses profitable, entrepreneurs hire more workers, giving more people jobs. The tax money that comes from their businesses helps the government. Goods and services entrepreneurs produce encourage trade within a country. This provides more jobs and more money for the economy. Entrepreneurs trading with other countries bring in goods and services that are not already available.

397. Which is an example of an entrepreneur?

- A. people who operate a hospital
- B. a person who runs a government-owned coal mine
- C. roofers who work for a business owned by an individual
- D. a person who uses her money to start a business selling cell phones

398. What is a problem faced by entrepreneurs in Russia?

- A. No one has money.
- B. There are no skilled workers.
- C. Courts don't protect property rights.
- D. There is a lack of natural resources, such as gas and oil.

399. Which is a way that entrepreneurs help increase a country's GDP?

- A. writing laws to protect personal property
- B. creating businesses that give people jobs
- C. providing the ideas to start and expand businesses
- D. working to increase the amount of goods and services bought by a country