Types of Economies

# Starter: Recap Questions

**Instructions:** Test yourself with the below quick questions

What is the basic economic problem?

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What were the three fundamental economic choices?

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What system helps us answer these choices?

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# Presentation 1 – Free Market Economies

Complete the activities below so as to have a complete set of notes:

**Definition:** *Free Market Economy*

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**Key Notes:** *Workings*

The forces of supply and demand work together to determine what price and quantity of goods and services are traded. The Price Market Mechanism.

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*Examples*

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**Elaborate:** Elaborate on the objectives below free market stakeholders.

*Consumers: \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_*

*Producers: \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_*

*Owners of Fop: \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_*

*Government’s: \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_*

A picture containing text, person, person, suit

Description automatically generated**Elaborate:**Elaborate on the below key ideas in Classical Economics

*The Invisible Hand (Economist:\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_)*

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“It is not from the benevolence of the butcher, the brewer, or the baker, that we expect our dinner, but from their regard to their own interest. We address ourselves, not to their humanity but to their self-love, and never talk to them of our own necessities but of their advantages.”

A person wearing glasses

Description automatically generated with low confidence

*Limited Government Intervention**(Economist:\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_)*

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*Reasoning:*Too much central planning of economic activity eventually led to totalitarian rule with a one party government restricting freedom and undermining democracy.

He advocated decentralisation and decision making be left with individuals and groups of individuals e.g. businesses.

**Key Idea:** *Classical economics:*

Suggests a laissez-faire (to leave alone) approach by the government towards markets. This will provide the greatest good for the greatest number of people

**Brainstorm:** Complete two mind maps below with all the advantages and disadvantages of Free Market Economies

Advantages

Disadvantages

# Feeding America logo.svgArticle Task: Feeding America

**Instructions:**

* *Read Highlight and annotate the article*
* *Make notes to answer the questions*
* *Discuss your answers as a class*

**Article** (Source: Feeding America’: A Brilliant Example of Economics Being Successful - Adrian Spottiswoode - 15th March 2016)

*A discussion on the introduction of market forces for allocating food to food banks.*

In the USA there’s an amazing organisation called Feeding America that receives donations of 50 truckloads of food, each containing 13,000kg of provisions, every day. Its job is to distribute the food to the 215 food banks who are affiliated with it.

This used to be done via a queuing system:

* Every day the 50 food banks at the front of the queue would be given a truckload of food each - these food banks then went to the back of the queue
* The following day the next 50 in line would get food - and so on
* To avoid charges of favouritism, food banks were not given any choice to which foodstuffs they received.

***The problem***

Often, food banks were allocated either foodstuffs they didn’t want or a particular type of food they had a lot of. And they often accepted food they couldn’t get rid of or couldn’t store, which meant that the food was wasted. In one example a food bank accepted a consignment of yoghurt but had no space in its refrigeration unit, so thousands of kilograms of yoghurt spoiled and became inedible. The allocated food might also come from a location on the other side of the USA. Food banks were responsible for paying for the transportation of the consignment, so this often led to extremely high transportation costs for the charity – maybe even for a truckload they did not really need. Food banks could refuse to accept a certain truckload, but this would mean they would go to the back of the queue without having received anything.

***The solution***

Economists from the University of Chicago were asked to devise a more efficient system - and the solution they came up with used market forces and prices. Initially it was quite a hard sell to the charities – many of whom blamed similar market forces for the predicament of the users of their food banks. The solution that was eventually agreed centred upon a type of constructed currency that was called “Shares”. Food banks used their shares to place bids for food consignments in auctions, which happened twice a day. (The auctions were sealed bids, so food banks could not see what others were bidding.)

***The result***

As an economist, it gives me great pleasure to write this sentence: it seems like this solution was not just a success, but led to unintended consequences which made it even more so. Food banks are allowed to put in zero bids, meaning they might get the consignment for free, and can even make “negative bids” where they ask to be paid to accept a truckload of food nobody else wants. Smaller food banks can make joint bids where they agree to share a truckload of food if they win the auction. This has meant that every truckload of food put up for auction since the system began in 2005 has found a “buyer”. Since shares are not a real currency, and are reallocated at regular intervals, no real financial loss was incurred by any food bank - but it served as an extremely effective rationing mechanism. Some feared that larger food banks would dominate the market, but this was avoided in 2 ways.

1. Shares were allocated, not just according the size of the area which a food bank covered, but also due to the proportion of people in that catchment area who need the support of that bank
2. It turned out that larger charities bid for different foodstuffs to the smaller ones. The larger food banks tended to have ample supplies of staple foods, so bid for expensive consignments like chicken breasts or peanut butter. Smaller food banks lacked staples, and because there was only limited demand for them, were able to get them at low prices or often for free

Charities have also begun to source food independently from local businesses and put it into the market. This meant that food banks earn more shares to bid with in other auctions, and it has also increased the total amount of food available - it’s estimated this has added 25% more food compared to the old system. So food banks can get food that they need and want, waste has been eradicated, excessive transportation costs have been avoided and extra food has been made available. And, perhaps most tellingly, a complaints line set-up in case any food bank thought the new system was unfair has not been contacted a single time in the ten years that the scheme has been running. Maybe we need to say it quietly and perhaps with fingers crossed, but this appears to be an example where Economics has really helped to make the world a bit of a better place.

**Questions**

Explain the market created to distribute food to foodbanks?

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How has the creation of a free market lead to an efficient outcome for the foodbanks?

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# Presentation 2 – Command Economies

Complete the activities below so as to have a complete set of notes:

**Definition:** *Command Economy*

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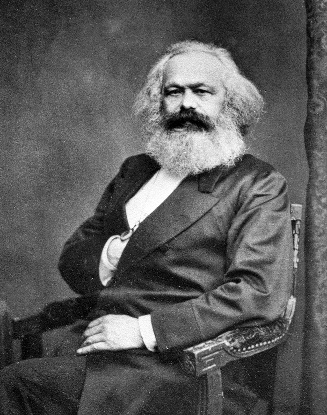
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**Key Notes:** *Workings*

The state decides what, how and for whom to produce

*Examples*

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**Elaborate:**Elaborate on the below key ideas on Command Economies

*Marxism (Economist:\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_)*

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Marx suggested that labour was underpaid by the owners of businesses which enabled them to make profits.

The inevitable inequality & exploitation that results creates a historically unavoidable class struggle

To escape, there needed to be a formation of a socialist government, eventually creating a communist utopia

‘Workers of the World, Unite! You have nothing to lose but your chains’

**Brainstorm:** Complete two mind maps below with all the advantages and disadvantages of Command Economies

Advantages

Disadvantages

# http://cdn.static-economist.com/sites/default/files/imagecache/original-size/images/2015/05/blogs/economist-explains/20150523_woc313.pngArticle Task: Cuba & America

**Instructions:**

* *Read Highlight and annotate the article*
* *Make notes to answer the key question*
* *Discuss your answers as a class*

**Article** (Source: [Why Cubans are still fleeing to America| The Economist](https://www.economist.com/the-economist-explains/2015/05/18/why-cubans-are-still-fleeing-to-america))

*The Economist explains: Why Cubans are still fleeing to America*

A CURIOUS asymmetry exists across the 90-mile (150km) Straits of Florida that divide Cuba from the United States. This month American businessmen won permission from their government to start plush new ferry services to Cuba for the first time since the United States trade embargo was imposed in 1960. Moving in the other direction are thousands of impoverished Cubans in makeshift boats and rafts, risking their lives to flee the communist island despite a five-month-old thaw in relations with America that both governments hope will bring more prosperity to Cuba. In the first quarter of the year the number of Cuban migrants arriving in America more than doubled, and 2,460 have been apprehended at sea since October. Why this gap between rhetoric and reality?

The exodus is probably being stirred by American immigration policy itself—or more precisely by the fear that it will change if rapprochement continues. As a legacy of the strident anti-communism of past American policy towards Cuba, Cuban immigrants to the United States are treated more leniently than those of other countries. If they touch dry land in America, they can automatically apply for permanent residency and, eventually, citizenship. But in order to prevent a flotilla of Cuban “boat people” (such as the Mariel boatlift of 1980), the Coast Guard returns almost all those it catches at sea to Cuba. The American authorities say there are no plans to change the policy, known colloquially as “wet foot, dry foot”. But the government of Raúl Castro blames it for encouraging illegal migration and says it should be stopped.

But in fact it is the Castro regime that bears final responsibility for the flood of migrants, because its policies—though admittedly exacerbated by the embargo—have produced the poverty and crippling lack of opportunity in Cuba that motivates many migrants in the first place. A series of reforms adopted since 2011 have allowed limited private enterprise on the island, and have sought to spur foreign investment. Yet a gap between the haves and have-nots is growing. As few as one-tenth of the labour force have their own businesses; the rest work in state-owned firms earning pitiful wages. State rations of basic staples like rice and beans add a meagre supplement to incomes, leaving remittances as the only meaningful option for households hoping to increase their earnings. Remittances from abroad are currently estimated at about $3 billion a year. Cubans who make the perilous journey to America are often on a survival mission for their families back home.

Cuba needs to accelerate its economic transformation

In 2013 the Cuban government unofficially acknowledged the need for an escape valve for its citizens when, for the first time, it made it legal for any Cuban to travel abroad. It has also sought to bolster its economy by sending its highly trained (though chronically underpaid) medical staff to allies such as Venezuela, in exchange for oil. But Venezuela’s economy is in a tailspin because of weak oil prices, and neighbours such as Mexico are increasingly reluctant to offer travel visas to Cubans, lest they use the country as a transit point to America. In short, the Cuban economy is not creating new opportunities rapidly enough to satisfy struggling Cuban households. Further opening may eventually lead to a sharp reversal in flows, as Cuban ex-pats return home to participate in an investment-driven boom. Until then ambitious Cubans will place their bets on the economic powerhouse to the north.

Key Question:

Explain two reasons why Cubans are fleeing to the USA.

Reason 1

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Reason 2

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# Presentation 3 –Mixed Economies

Complete the activities below so as to have a complete set of notes:

**Definition:** *Mixed Economy*

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**Key Notes:** *Workings*

Enterprise is encouraged and markets are mostly free to answer the three fundamental choices (What, How, For Whom), but government will act to:

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*Examples*

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A person with a mustache

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**Elaborate:**Elaborate on the below key ideas on Mixed Economies

*Keynesian Economics (Economist:\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_)*

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In particular, he thought that periods of high unemployment would persist for a long time as workers are inflexible with regards to taking a pay cut.

Thus, the government has a role to control markets to ensure maximum welfare as the market won’t achieve this by itself.

**Brainstorm:** Complete two mind maps below with all the advantages and disadvantages of Free Market Economies

Advantages

Disadvantages

**Definition:** *Transition Economies*

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They undergo a set of structural transformations to develop market-based institutions. These Include:

* + Economic liberalization (prices are set by market forces rather than centrally planned),
  + The removal of trade barriers
  + State-owned enterprises and resources are increasingly privatised and restructured as businesses
  + The birth and growth of a financial sector to facilitate macroeconomic stabilization and the movement of private capital

*Examples*

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# Article Task: The Case for a Mixed Economy

**Instructions:**

* *Read, highlight and annotate this article by Paul Krugman (The Krugmeister)*
* *Make notes to answer the key question*

*Paul Krugman is a Distinguished Professor at the City University of New York Graduate Center. He won the 2008 Nobel Memorial Prize in Economic Sciences for his work on international trade and economic geography*

* *Discuss your answers as a class*

**Article (**Source: [The Case for a Mixed Economy | The New York Times](https://www.nytimes.com/2018/12/22/opinion/the-case-for-a-mixed-economy.html))

*‘Maybe not everything should be privatized’*

A mind is a terrible thing to lose, especially if the mind in question is president of the United States. But I feel like taking a break from that subject. So let’s talk about something completely different, and probably irrelevant.

I’ve had several interviews lately in which I was asked whether capitalism had reached a dead end, and needed to be replaced with something else. I’m never sure what the interviewers have in mind; neither, I suspect, do they. I don’t think they’re talking about central planning, which everyone considers discredited. And I haven’t seen even an implausible proposal for a decentralized system that doesn’t rely on price incentives and self-interest – i.e., a market economy with private property, which most people would consider capitalism.

So maybe I’m being dense or lacking in imagination, but it seems to be that the choice is still between markets and some kind of public ownership, maybe with some decentralization of control, but still more or less what we used to mean by socialism. And everyone either thinks of socialism as discredited, or pins the label on stuff – like social insurance programs – that isn’t what we used to mean by the word.

But I’ve been wondering, exactly how discredited is socialism, really? True, nobody now imagines that what the world needs is the second coming of Gosplan. But have we really established that markets are the best way to do everything? Should everything be done by the private sector? I don’t think so. In fact, there are some areas, like education, where the public sector clearly does better in most cases, and others, like health care, in which the case for private enterprise is very weak. Add such sectors up, and they’re quite big.

In other words, while Communism failed, there’s still a pretty good case for a mixed economy – and public ownership/control could be a significant, although not majority, component of that mix. My back of the envelope says that given what we know about economic performance, you could imagine running a fairly efficient economy that is only 2/3 capitalist, 1/3 publicly owned – i.e., sort-of-kind-of socialist.

I arrive at that number by looking at employment data. What we see right away is that even now, with all the privatization etc. that has taken place, government at various levels employs about 15 percent of the work force – roughly half in education, another big chunk in health care, and then a combination of public services and administration.

Looking at private sector employment, we find that another 15 percent of the work force is employed in education, health, and social assistance. Now, a large part of that employment is paid for by public money – think Medicare dollars spent at private hospitals. Much of the rest is paid for by private insurers, which exist in their current role only thanks to large tax subsidies and regulation.

And there’s no reason to think the private sector does these things better than the public. Private insurers don’t obviously provide a service that couldn’t be provided, probably more cheaply, by national health insurance. Private hospitals aren’t obviously either better or more efficient than public. For-profit education is actually a disaster area.

So you could imagine an economy in which the bulk of education, health, and social assistance currently in the private sector became public, with most people at least as well off as they are now.

Then there are other private activities that could plausibly be public. Utilities are heavily regulated, and in some cases are publicly owned already. Private health insurance directly employs hundreds of thousands of people, with doubtful social purpose. And I’m sure I’m missing a few others.

By and large, other areas like retail trade or manufacturing don’t seem suitable for public ownership – but even there you could see some cases. Elizabeth Warren is suggesting public manufacture of generic drugs, which isn’t at all a stupid idea.

Put all of this together, and as I said, you could see an economy working well with something like 1/3 public ownership.

Now, this wouldn’t satisfy people who hate capitalism. In fact, it wouldn’t even live up to the old slogan about government controlling the economy’s “commanding heights.” This would be more like government running the boiler in the basement. Also, I see zero chance of any of this happening in my working lifetime.

But I do think it’s worth trying to think a bit beyond our current paradigm, which says that anything you could call socialist has been an utter failure. Maybe not so much?

**Key Question**

What arguments are made here for a mixed economy over a free market one?

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# Assignment

**Short-answer questions (Section A)**

1. One advantage of a free market economy is that:

A Education and healthcare are funded from taxation and freely available to all

B Government intervention can be used to correct market failure

C Firms concentrate on producing necessities rather than luxuries

D Competition between firms can be of benefit to consumers

[1]

1. Czechoslovakia (today known as the Czech Republic) became a communist country in 1948 and central planning was introduced as a means of allocating scarce resources. Since 1993, the Czech Republic has made the transition towards a market economy, experiencing high economic growth rates compared to when it was a command economy.
   1. With reference to the statement above, explain how scarce resources are allocated in a command economy.

[2]

* 1. Which of the following statements best describes the changes to the economic system in the Czech Republic?

A Demand and supply decisions in the Czech Republic are now largely directed by government officials.

B Resource allocation in many markets is now allowed to be determined by individual consumers and producers, acting in their own self-interest and co-ordinated via the ‘invisible hand’.

C Marx predicted economic systems would switch from command economies to market economies as a progression over time.

D The public sector must now be bigger in the Czech Republic compared with when it was a communist country.

[1]

1. Both Hayek and Smith were strong advocates of letting markets determine resource allocation. Which of the following statements would be true for a pure free market economy?

A The government decides what should be produced.

B Central planners decide how much of a good should be produced, who should receive them and how they should be made.

C Prices will be determined by market forces.

D The government provides public goods.

[1]

1. Only in a pure command economy does production:

A respond to changes in prices

B change in response to the profit motive

C reflect the preferences of consumers

D respond to state directives.

[1]

**Essay questions (Section C)**

1. ‘Command economies will always be inferior to free market economies as economic systems’.

To what extent do you agree with this statement?

[25]

1. Evaluate the likely economic effects for countries, such as Poland and Russia, that have transformed their economies away from the command economy system towards a market economy.

[25]

**Question:** 1 Or 2

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| **Planning Grid: Aim = 5 paragraphs - 2 KAA points (16); 2 Eval points (9) with a conclusion** | |
| **KAA Point 1 = signpost key point** |  |
| Application |  |
| Main concept & diagram |  |
| **Eval Point 1 = relate to your earlier point & re-read the title** |  |
| Context / evidence |  |
| **KAA Point 2 = signpost key point** |  |
| Application |  |
| Main concept & diagram |  |
| **Eval Point 2 = relate to your earlier point & re-read the title** |  |
| Context / evidence |  |
| **Conclusion = judgement** |  |
| Context; what does it depend on? |  |