

What is an Economic System?

An economic system is the combination of the various agencies and entities that provide the economic structure that defines the social community. These agencies are joined by lines of trade and exchange goods. Many different objectives may be seen as desirable for an economy, like efficiency, growth, liberty, and equality. An economic system may involve production, allocation of economic inputs, distribution of economic outputs, landlords and land availability, households (earnings and expenditure consumption of goods and services in an economy), financial institutions, firms, and the government.

Alternatively, an economic system is the set of principles by which problems of economics are addressed, such as the economic problem of scarcity through allocation of finite productive resources.

The scarcity problem, for example, requires answers to basic questions, such as:

- What to produce?
- How to produce it?
- Who gets what is produced?

Types of Economic Systems

Examples of contemporary economic systems include:

- Planned systems
- Free market systems
- Mixed economies

Today the world largely operates under a global economic system based on the free market mode of production.

Planned Systems

In a planned system, the government exerts control over the allocation and distribution of all or some goods and services. The system with the highest level of government control is communism.

In theory, a communist economy is one in which the government owns all or most enterprises. Central planning by the government dictates which goods or services are produced, how they are produced, and who will receive them. In practice, pure communism is practically nonexistent today, and only a few countries (notably North Korea and Cuba) operate under rigid, centrally planned economic systems.

Under socialism, industries that provide essential services, such as utilities, banking, and health care, may be government owned. Other businesses are owned privately. Central planning allocates the goods and services produced by government-run industries and tries to ensure that the resulting wealth is distributed equally. In contrast, privately owned companies are operated for the purpose of making a profit for their owners. In general, workers in socialist economies work fewer hours, have longer vacations, and receive more health, education, and child-care benefits than do workers in capitalist economies. To offset the high cost of public services, taxes are generally steep. Examples of socialist countries include Sweden and France.

Free Market System

The economic system in which most businesses are owned and operated by individuals is the free market system, also known as "capitalism. "

In a free market, competition dictates how goods and services will be allocated. Business is conducted with only limited government involvement. The economies of the United States and other countries, such as Japan, are based on capitalism.

In a capitalist economic system:

- Production is carried out to maximize private profit.
- Decisions regarding investment and the use of the means of production are determined by competing business owners in the marketplace.
- Production takes place within the process of capital accumulation.
- The means of production are owned primarily by private enterprises and decisions regarding production and investment determined by private owners in capital markets.

Capitalist systems range from laissez-faire, with minimal government regulation and state enterprise, to regulated and social market systems, with the stated aim of ensuring social justice and a more equitable distribution of wealth or ameliorating market failures.

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