

# World Economies

## SECTION

# 3

## If YOU lived there...

You farm a small plot of land in southern India, and you have a decision to make. You can grow food for your family, or you can grow cassava, a cash crop that can be sold for profit if demand for the crop remains high.

## What choice will you make?

**BUILDING BACKGROUND** Everyone has wants. The decisions you make to satisfy your wants are economic choices. Economists say that all societies face a basic problem: people's wants are unlimited. The resources to fulfill wants, however, are limited.

## Scarcity and Resource Use

The conflict between people's unlimited wants and limited resources creates a condition called **scarcity**. Scarcity affects everybody. In fact, scarcity forces individuals, businesses, and societies to answer three basic questions: What will be produced? How will it be produced? For whom will it be produced?

## Factors of Production

To understand how societies answer these questions, economists study **factors of production, or the basic economic resources needed to produce goods and services**. The four main factors of production are land, labor, capital, and entrepreneurship. These factors have one thing in common—their supply is limited.

In economic terms, land includes all the natural resources found on or under the ground that are used to produce goods and services. Labor refers to the human time, effort, and talent needed to produce goods and services. Capital refers to the resources used to make and distribute goods and services. Tools, factories, roads, and trains are all forms of capital. Finally, entrepreneurship is the combination of vision, skill, and willingness to take risks needed to start businesses.

If a factor of production is in short supply, problems can arise. Consider this example: a farmer uses skills (labor) and



TEKS 3C, 8A, 8B, 8C, 9A, 9B, 9C, 9D,  
10A, 10B, 10C, 15E, 21B

### Main Ideas

1. Scarcity shapes how societies use factors of production.
2. There are three basic types of economic systems.
3. Contemporary societies have mixed economies.
4. The United States benefits from a free enterprise system.
5. Geographers categorize countries based on levels of economic development and range of economic activities.

### The Big Idea

Geographers understand world economies by studying factors of production, economic activities, and levels of development.

### Key Terms

scarcity, p. 117  
factors of production, p. 117  
free enterprise system, p. 121  
agricultural industries, p. 122  
manufacturing industries, p. 122  
wholesale industries, p. 122  
retail industries, p. 122  
service industries, p. 123  
developed countries, p. 123  
developing countries, p. 124



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TAKING NOTES

Use the graphic organizer online to compare economic systems.

tools (capital) to grow strawberries on a farm (land), which he or she then sells at a market (role of entrepreneur). If a drought destroys farmland, the farmer might produce fewer, if any crops. The farmer's business would be hurt. Strawberries would be scarce. Consumers and businesses would likely have to buy them at a higher price.

**The availability of resources influences economic activity. Rwanda's agricultural economy relies heavily on a large number of workers.**



**By contrast, the availability of capital resources, such as combine harvesters, helps a small number of U.S. farmers tend large fields.**



## Resources and Economies

The factors of production are not distributed equally. For this reason, countries decide what to produce based on the resources they have. For example, South Africa is rich in gold, diamonds, and mineral resources. Developing a mining industry has helped make South Africa one of the richest countries in Africa.

The availability of resources also shapes how a society produces goods and services. For example, Rwanda's economy is based on agriculture. Rwandans are rich in agricultural labor. In fact, about 90 percent of Rwandans work in agriculture. Farmers grow crops on small plots of land near their homes. In terms of capital, they have simple farming tools but few tractors and roads. By contrast, only about two percent of Americans work in agriculture. U.S. farmers rely heavily on capital. Using machinery and technology, they produce surplus crops on large farms.

## Scarcity and Trade

When a resource is relatively scarce in one place, people may trade with others to get it. This happens within a society as well as between nations. In this way, scarcity contributes to economic interdependence. It is also a driving force behind international trade.

For instance, Japan manufactures cars, which requires a great deal of steel. However, Japan lacks the iron ore needed to make steel. To obtain iron ore, Japan has formed international trading relationships with Australia and Brazil.

**READING CHECK Analyzing** How does availability of the factors of production affect a society's economy?

## Economic Systems

An economic system is the way in which a society organizes the production and distribution of goods and services. Economic systems can be divided into three types: traditional, market, and command.

In a traditional economy, the work that people do is based on long-established customs. People in these groups hunt, fish, and tend animals and crops. Often, the focus of work is survival. The good of the group is more important than individual desires. In earlier times, all societies had traditional economies.

Today traditional economies are rare and under pressure to change. Still, you can find this system in many places. For example, the Aymara people of the South American Andes and the Inuit people in northern Canada have traditional economies.

In a command economy, the government controls the economy. Command economies decide what goods and services to produce, how and how much to produce, and how goods and services are distributed. It also sets wages and prices. Some

economists refer to command economies as centrally planned economies.

The most common economic system used today is a market economy. A market economy is based on private ownership, free trade, and competition. Individuals and businesses are free to buy and sell what they wish with little interference from government. Prices are determined by the supply of and demand for goods.

**READING CHECK** Summarizing What are the three basic types of economic systems?

## Modern Economies

Few if any pure economic systems exist today. Most countries have mixed economies that combine elements of traditional, market, and command economic systems. The most common types of mixed economies are communist, capitalist, and socialist.

### Communist Economies

Modern economies tend to emphasize features of one system over others. For

**Traditional** The Inuit of Canada use fishing techniques passed down over many generations.

**Command** Food was scarce and expensive in this store in the former Soviet Union, a command economy.

**Market** Advertisements, like these billboards in New York City, are a common sight in a market economy.



example, communist economies are closest to the command model. In a communist economy the government owns all the factors of production. There is no private ownership of property and little or no political freedom.

How do communist nations decide what, how, and for whom to produce? In countries such as North Korea and Cuba, the government collectivized, or took ownership, of the factors of production. Then government workers called central planners make long-term plans. They make all decisions about the production, price, and distribution of goods and services. They may even decide what types of work people are able to do.

### Capitalist Economies

By contrast, capitalist economies emphasize features of market systems. In capitalist economies, individuals and businesses own the factors of production. They play a major role in answering the basic economic questions and no central government authority tells them what to do. Consumers buy goods and services that they like best. Their choices push producers to make better products at lower prices.

The economies of the United States, Canada, and Taiwan are capitalist. In these countries, government plays an important

but limited role in the economy. For example, in the United States, government agencies enforce health and safety standards. These actions benefit U.S. workers and consumers but affect business planning in complicated ways. Regulations can increase the cost of running a business. On the other hand, the government spends money that it collects in taxes on services that support economic development, such as education, roads, and social welfare programs. Businesses save money by not having to pay for these services themselves.

### Socialist Economies

The third type of economy falls between communism and capitalism. In socialist economies, the government controls some of the basic factors of production. In most cases, that control is limited to industries and services that are central to a nation's well being, such as electrical utilities, communications networks, and healthcare. Other industries are privately controlled.

Today, many nations with elements of a socialist economy, such as Sweden and India, have democratic governments. Still, central planners make decisions about government-owned industries. They also make decisions about other sectors, such as healthcare, to ensure that everyone has access to services.

Comparing Economic Systems			
	Communism	Socialism	Free Enterprise
Who owns resources?	Government	Government owns basic resources; the rest are privately owned	Individuals and businesses
Who distributes resources?	Government decides how resources are used	Government regulates basic resources; market allocates privately owned resources	Market allocates resources
What role does government play?	Government makes all economic decisions	Government makes decisions in the basic industries	Government has a limited role, acting mostly to ensure market forces are free to work

## Trends Since the Fall of Communism

The record of collective, or communist, non-free market economies, is poor. From the 1940s until the 1990s, between one quarter and one third of the world's people lived under communist regimes. The former Soviet Union and several of its Eastern European neighbors, China and much of Southeast Asia, Cuba, and North Korea all had centrally planned economies.

The failure of these economies is due largely to the shortcomings of communism. Often, central planners had too many decisions to make and too little understanding of local conditions. With wages set, workers had little incentive to work hard. Communism's greatest failing, however, was the suffering that it caused. Shortages of food and goods were common. Millions of people died building huge collective farms in China and the Soviet Union. Millions more were imprisoned for criticizing government policies.

With the collapse of communism in the early 1990s, most communist countries adopted some form of market economy. Even the five communist countries that are left—China, Cuba, Laos, North Korea, and Vietnam—have adopted some features of market economies.

**READING CHECK** **Comparing** How are socialist economies similar to both communist and capitalist economies?

## The Free Enterprise System

U.S. capitalism is sometimes called the **free enterprise system**. Under this system, Americans enjoy a number of freedoms. They are free to exchange goods and services and choose careers. They are also free to own and operate enterprises, or businesses, with little government intervention.



At age eight, Madison Robinson started a business selling flip-flops that she designed.

Let's take a look at one American who took advantage of these freedoms. In 2006 Eight-year-old Madison Robinson from Galveston, Texas, had an idea to sell light-up flip-flops for kids. With financing from friends and family, she started her own company, Fish Flops. By 2013 Fish Flops had over \$1 million in sales, enough profit to cover Robinson's college tuition.

The ability to make a profit is one of the chief advantages of the free enterprise system. In this system, profit can reward hard work and innovation. The desire to make a profit also encourages competition, forcing producers to offer higher-quality products at lower prices. Another advantage is that people often have greater freedoms in societies with free enterprise systems. They can own property, make economic decisions, and participate in open elections.

Maintaining a functioning free enterprise system requires people to act in a morally responsible and ethical way. Businesses and individuals must obey laws, be truthful, and avoid behaviors harmful to others. Government regulations must be effective and fairly enforced.

## FOCUS ON READING

What are the clue words in this sequence of events?

Unethical behavior can lead to business failure and a loss of trust in the system. For example, if company officials begin to lie about a business's financial condition, then investors can lose thousands, even billions of dollars. Finally, the company itself could go bankrupt.

**READING CHECK** **Summarizing** How does the ability to make a profit help the economy?

## Economic Activities and Development

Every nation's economy includes a variety of economic activities. Economic activities are the ways in which people make a living. Some people farm, others manufacture goods, and still others provide services. Geographers categorize these economic activities into four levels of industry.

### Levels of Industry

The first level is called primary industry. People working at this level harvest

products from the earth. **Agricultural industries** are primary activities that focus on growing crops and raising livestock. Fishing and mining are also primary activities. Raw materials such as grain, cattle, seafood, and coal are all products of primary activities.

At the next level, secondary industry, people use natural resources and raw materials to make products to sell. **In manufacturing industries**, people and businesses manufacture, or make, finished products from raw materials. For example, a furniture maker could use wood to make a table or a chair.

In the third level, or tertiary industry, people provide goods and services to customers. Workers at this level may sell goods and products from primary and secondary industries. Some work in **wholesale industries**, businesses that sell to businesses. They help move goods from manufacturer to market. Others work in **retail industries**, businesses that sell

## Economic Activity

### Primary Industry

Primary industries use natural resources to make money. This farmer sells milk from dairy cows to earn a living.



### Secondary Industry

Secondary economic activities use raw materials to produce or manufacture something new. In this case, the milk from dairy cows is used to make cheese.



### Tertiary Industry

Tertiary economic activities provide goods and services to people and businesses. This grocer selling cheese in a market is involved in a tertiary activity.



### Quaternary Industry

Quaternary industries process and distribute information. Skilled workers research and gather information. Here, inspectors examine and test the quality of cheese.



directly to final consumers. For example, a furniture wholesaler buys tables from a manufacturer. Then the wholesaler sells the tables to a retail store, such as a department store, that sells directly to consumers.

Still other tertiary workers, like health care workers and mechanics, work in **service industries, businesses that provide services rather than goods.** Teachers, store clerks, and doctors are all tertiary workers.

The fourth level of economic activity, quaternary industry, involves the research and distribution of information. People making a living at this level work with information rather than goods and often have specialized knowledge and skills. Architects, librarians, and scientists all work in quaternary industries.

### Economic Indicators

Economic systems and activities affect a country's economic development, or the level of economic growth and quality of life. Geographers group countries into two

basic categories: developed countries and developing countries. To decide if a country is developed or developing, geographers use economic indicators, or measures of a country's wealth.

One indicator, gross domestic product (GDP), is the value of all goods and services produced within a country in a single year. Another indicator is a country's per capita GDP, or the total GDP divided by the number of people in a country. As you can see in the chart, per capita GDP allows us to compare incomes among countries. Other indicators include literacy and life expectancy and the overall level of industrialization. We also look at the types of industries a country has and at its level of health care and education.

### Developed and Developing Countries

Many of the world's wealthiest and most powerful nations are **developed countries, countries with strong economies and a**

#### A Developed and a Developing Country

Australia	Afghanistan
Per Capita GDP (U.S. \$): \$43,300	Per Capita GDP (U.S. \$): \$1,100
Life Expectancy at Birth: 82	Life Expectancy at Birth: 50.1
Literacy Rate: 99%	Literacy Rate: 28%
Physicians Per 10,000 People: 39	Physicians Per 10,000 People: 2



**Contrasting** How does the quality of life in Afghanistan differ from that in Australia?

**high quality of life.** Developed countries like Germany and the United States have a high per capita GDP and high levels of industrialization. Their health care and education systems are among the best in the world.

The world's poorer nations are known as **developing countries, countries with less productive economies and a lower quality of life.** Almost two-thirds of the world's people live in developing countries. These countries have a lower per capita GDP than developed countries. Most of their citizens work in farming or other primary industries. Although these countries typically have large cities, much of their population still lives in rural areas. People in developing countries usually have less access to health care and technology. Guatemala, Nigeria, and Afghanistan are all developing countries.

Often, a country's economic activities reflect its economic development.

In the poorest developing countries, the vast majority of people work in primary industries, such as farming. As a country becomes more developed, fewer people work in primary industries. In the mid-1800s about two thirds of U.S. workers worked in primary activities. Today, 80 percent work in tertiary industries, including wholesale, retail, and service industries. Only three percent of Americans work in primary industries.

**READING CHECK Analyzing** How does GDP differ in developed and developing countries?

**SUMMARY AND PREVIEW** In this section you learned about the economic activities, systems, and levels of development that characterize societies today. In the next chapter you will learn about citizenship in various countries.

## Section 3 Assessment



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ONLINE QUIZ

### Reviewing Ideas, Terms, and Places

- a. Describe** What are the **factors of production**?

**b. Predict** What problems might a homebuilder face if one of the factors of production, such as land or labor, was in short supply?

**c. Explain** Identify and explain an example of how the relative scarcity of resources might impact economic interdependence within a country.
- a. Compare** Who makes the economic decisions in a traditional economy? Compare this with market and command economies.

**b. Evaluate** What explains the record of collective, non-free market economies in the world today?
- a. Identify** What are the advantages of the **free enterprise system**?

**b. Analyze** How can unethical and immoral behavior hurt the free enterprise system?
- a. Define** Describe and give examples of **agricultural, wholesale, retail, manufacturing, and service industries.**

- b. Explain** What are **developed** and **developing countries**? Include examples of economic indicators in your answer.
- c. Analyze** How might economic factors affect the use of technology in a developing country?

### Critical Thinking

- 5. Comparing** Use your notes to complete a chart like the one below comparing economic systems. For each system, list how some societies organize the production and distribution of goods and services.

Free Enterprise	Socialist	Communist

### FOCUS ON WRITING

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- 6. Describing Economic Systems** Use your notes on economic systems to write your article. Be sure to include definitions of different economic systems as well as details on the United States and Rwanda.