Economic Systems Review (including Transition)

An **economic system** is the method used by a society to determine how goods and services get produced and distributed. We can gather clues to determining under which category of economic systems a particular society belongs by answering three fundamental questions about that society:

- What goods and services get produced in this society?
- How do goods and services get produced in this society?
- How does the society determine who consumes the goods and services?

In this activity, we will consider “society” to be a particular country.

As you have already studied the four economic systems include,

Free Market: an economic system in which production and distribution decisions are determined through voluntary exchange in markets

- → In theory, a free market system has no government intervention. However, since there does not exist a country with absolutely no government in control, we consider a free market economy to have very minimal government interference.
- → Free market economic systems are characterized by a large urban work force in industry and services, high GDP per capita, high literacy and life expectancy rates, low poverty rate, low fertility rate, low to average military spending, easy access to data, and developed physical infrastructure.

Centrally Planned (Command): an economic system in which production and distribution decisions are determined by a central government

- → In theory, a command economy has complete government intervention in every aspect of production and distribution decisions. However, since there does not exist a country with absolute government control, we consider a command economy to have very significant government interference.
- → Centrally planned economic systems are characterized by state-owned firms, large shortages and surplusses of consumer goods, low growth rates, low level of exports and imports, average to high poverty rate, relatively high military spending, price fixing of goods and services, and a lack of available data.

Traditional: an economic system in which production and distribution decisions are determined by long-standing rituals and customs

- → Traditional economic systems are characterized by high poverty rate, low urbanization, large agricultural workforce, low GDP per capita, high unemployment rate, undeveloped phsical infrastructure, high fertility rate, low literacy and life expectancy, and a lack of available data.

Mixed: an economic system in which production and distribution decisions are based on free market principles, but they are guided by limited government interference

- → Mixed economic systems have many of the same features of free markets, but they include a higher degree of government expenditures.

Many countries that have traditionally had centrally planned or traditional economic systems have moved into increasingly free and mixed market structures. Such economies are referred to as **transition economies**. Transition economies are characterized by several, if not all, of the following features:

- privatization of state-owned firms
- increased variation in available goods and services
- creation of laws concerning private property rights
- allowing prices to be set by market forces, rather than by government declaration
- increased business investment
- increased GDP per capita
- increased inequality of income distribution
- increased foreign trade
- establishment of a foreign exchange system for currency
- establishment of securities exchanges and privatization of banking
- establishment of non-banking financial enterprises
- initial spike in inflation, followed by long-term stabalization of low inflation rate
- increased public availability of data

In November 2000, the International Monetary Fund identified the following countries' economic systems as in transition: Albania, Armenia, Azerbaijan, Belarus, Bulgaria, Cambodia, China, Croatia, Georgia, Czech Republic, Estonia, Hungary, India, Laos, Latvia, Lithuania, Kazakhstan, Kyrgyz Republic, Republic of Macedonia, Moldova, Poland, Romania, Russia, Slovak Republic, Slovenia, Tajikistan, Turkmenistan, Ukraine, Uzbekistan and Vietnam.[i] However, since approximately a decade has passed since the publication of this report many of the countries on this list may have "completed" their transition. In addition, we may be able to identify other countries that may have begun transformation since 2000.

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[i] *Transition Economies: An IMF Perspective on Progress and Prospects*. IMF. 2000-11-03. http://www.imf.org/external/np/exr/ib/2000/110300.htm. Retrieved on August 9, 2009.