**BASIC ECONOMIC DECISIONS**

No two economies are organized in exactly the same way, but all have to solve three fundamental problems:

**1. What should be produced in the economy?**

What quantities of food, mobile phones or banking services should be produced by the economy? How many trees need to be felled to meet the demand for pulp for newspapers and magazines? Should we spend extra money on national defence or should more resources be devoted to health care and education?

**2. How should production be organised?**

Should a firm use labour or machinery to produce their goods? How many workers should be employed? Should production take place in London or Bangkok or in the UK or Malaysia? Should Mazda plc buy its components from Thailand or Indonesian suppliers? These are all examples of important production decisions.

**3. For whom should production take place?**

Should everybody be entitled to an identical share of production, or should some receive more than others? We know that the distribution of income and wealth in China and every other economy is not equal. There are large-scale inequalities in people's living standards.

**There are Three main types of economic system**

**FREE MARKET ECONOMIES**

A free market economy is one where economic decisions are made through the free market mechanism. The forces of market demand and supply, without any government intervention, determine how resources are allocated. This is known as the working of the price mechanism. The basics of this are covered in the theories of demand and supply later on.

* What to produce is decided upon by the profitability for a particular product.
* When demand for a product is high, the price rises and this raises the profitability of selling in the market
* High prices and high profits provide the signal for firms to expand production.
* Supply from producers responds to consumer wants and needs expressed through the price mechanism
* The consumer is said to be sovereign - their "economic votes" determine how resources are allocated

**COMMAND ECONOMIES**

A command economy is one where all key economic decisions are made by the government (or state). The government decides what to produce, how it is to be produced and how it is to be allocated to consumers. This involves a great deal of economy planning by the state. The price mechanism has no active role in a pure command economy since market prices are rarely used. By state planning, goods and services can be produced to satisfy the needs of all the citizens of a country, not just those who have the money to pay for goods. Over the last decade, many former planned economy have attempted to bring market forces into their economy.

**MIXED ECONOMIES**

A mixed economy is a mixture of a pure free-enterprise market economy and a command economy. Nearly every country in the world operates a mixed economy although the "mix" can change. There is a private sector and a public sector in the economy. In recent years many command economies have become mixed economies. Examples include China . These economies are often referred to as Transitional Economies as they are moving towards a freer market system, and becoming a mixed economy.

The amount of state intervention differs in all economies. For example Sweden has a great deal of Government intervention, whilst the USA has far less. The mix depends often on the political party in power at the time. Left wing governments tend to intervene in the market economy far more than right wing governments who leave the allocation of resources mainly to the market mechanism. Eg health care provision often differs in many countries