

## **ANSWERS TO END-OF-CHAPTER QUESTIONS**

- 2-1 Contrast how a market system and a command economy try to cope with economic scarcity.

A market system allows for the private ownership of resources and coordinates economic activity through market prices. Participants act in their own self-interest and seek to maximize satisfaction or profit through their own decisions regarding consumption or production. Goods and services are produced and resources are supplied by whoever is willing to do so. The result is competition and widely dispersed economic power.

The command economy is characterized by public ownership of nearly all property resources and economic decisions are made through central planning. The planning board, appointed by the government determines production goals for each enterprise. The division of output between capital and consumer goods is centrally decided based on the board's long-term priorities

- 2-2 How does self-interest help achieve society's economic goals? Why is there such a wide variety of desired goods and services in a market system? In what way are entrepreneurs and businesses at the helm of the economy but commanded by consumers?

The motive of self-interest gives direction and consistency to the economy. The primary driving force of the market system is self-interest. Entrepreneurs try to maximize their profits; property owners want the highest price for their resources; workers choose the job with the best wages, fringe benefits and working conditions. Consumers apportion their expenditures to maximize their utility, while seeking the lowest possible prices. As individuals express their free choice, the economy is directed to produce the most wanted goods at the lowest possible cost.

Each individual consumer will choose a variety of goods and services that in combination will maximize his/her satisfaction (utility). There is a wide variety because individual wants are diverse. To maximize profits, producers must respond to the desires of the individual consumer.

Although producers are free to choose what products they will produce, if the producers are to maximize profits, these good and services must be what consumers desire. Entrepreneurs can drive the economic ship where they want (at least for a while), but the ship will run aground (businesses will fail) if entrepreneurs at the helm don't listen to the consumers that command them.