

# We will describe the role of government in a market economy.

1. In the United States of America, government has a fairly limited role in directly managing our economy. 2. Customers, businesses, investors, and other players in the economy decide on production, pricing, and distribution of goods and services. 3. Most of these decisions are made by the market forces of supply and demand. 4. This defines free market capitalism. 5. Our government has a definite role to play, but it is not to micro-manage the economy. 6. The market itself is fairly efficient at making broad economic decisions. 7. Therefore, the role of the government is largely to fill in the gaps where a market economy doesn't do a good job of providing socially desirable goods and services. 8. These roles include making the rules that all businesses must follow, providing socially desirable goods and services that are not profitable, reducing negative externalities, and managing the stability of the economy.

9. The most obvious role of government is to establish the rules and regulations that businesses must follow. 10. Enforcing contracts and property rights is essential to the function of any market economy. 11. A business has to count on the fact that any contracts signed and agreements made will be followed. 12. The enforcement of business agreements is largely through the judicial system. 13. Breaking a contract is not illegal, but instead is associated with paying for the damages that breaking the contract caused. 14. This is an important constant within business that the government enforces. 15. The government also enforces patent, copyright, and intellectual property protections. 16. These protect the creators, inventors, and owners of ideas, inventions, and creative pursuits so unscrupulous people cannot simply steal original creations and make their own. 17. Similarly, the government has an interest in preventing monopolies and trusts from breaking the system of competition that traditionally keeps prices down for customers. 18. If a business controls too much of the market, they can control competition and artificially inflate prices. 19. The government works to facilitate fair business practices and encourage healthy competition within the marketplace, not as a controller of the market, but rather as a shepherd tending and protecting markets from unethical behavior.

20. This is not to say that there is no place for the government to take a more active role in the marketplace. 21. There are some goods and services that are highly desirable to society, but are not ready sources of profit. 22. In these situations, government agencies step in to provide them. 23. The government largely pays for our roads, bridges, highways, and other transportation infrastructure. 24. These are important to the economy, but are not terribly profitable, so state and federal agencies step in and develop them as public resources. 25. Local governments create and maintain water and sewer systems, garbage collection, and local roads. 26. Many water storage and delivery programs are also run by the government to provide irrigation for farming and drinking water for large cities. 27. This active role even extends to the United States Postal Service, which was explicitly established by the Constitution. 28. The US Postal Service will deliver mail to any address, even in remote parts of the US where it isn't profitable to do so at a reasonable price. 29. Even education is a public service provided to the population. 30. Most schools, colleges, and universities in the United States are run by the individual states.

31. Another active role for government is to provide for defense and safety. 32. This includes a fairly wide variety of activities, including national defense. 33. It is, after all, difficult to run a business when your country is being invaded! 34. This also includes law enforcement, fire protection, and other safety personnel. 35. All of these government employees play a role in protecting society, and they would not do so based solely on market forces. 36. This is active participation insofar as the government is directly employing people to do these jobs. 37. The government takes on this role because protecting everyone isn't profitable.

38. Another very important role for the government is to make strict rules for what are called Negative Externalities. 39. Negative Externalities are social concerns that are not considered by the private sector because of cost. 40. This includes a variety of things that society wants but are expensive. 41. For example, air pollution coming from a factory might be a big problem for a community. 42. This might require changes to the processes the factory uses, purchasing additional equipment, moving the factory, or any number of other potentially expensive solutions. 43. Obviously, business owners would rather not make any of these expensive changes to their businesses. 44. There are no real market forces to push businesses into dealing with Negative Externalities. 45. They exist largely outside the system of supply and demand that controls much of the economy. 46. Because of this, government must step in to control things like pollution, the disposal of toxic and nuclear waste, food and drug safety, worker safety rules, and several other important rules and regulations. 47. Without such regulation, the private sector will seek to maximize profit and will, for example, dump toxic chemicals into drinking water. 48. This has happened regularly throughout history. 49. Pollution on the Cuyahoga River in Ohio was bad enough that the river itself caught fire several times!

50. The last major role of the government in most market economies is to take an active role in stabilizing the economy during economic downturns. 51. In a recession, private investment declines because there are fewer profits to invest and investing is riskier because the economy is worse. 52. This creates a negative feedback loop where investment is down because profits are down, which in turn causes profits to sink further, discouraging investment even more and so on. 53. The government's role is to step in and invest in public projects in order to make up for decreased private investment. 54. Usually, this comes in the form of building public infrastructure projects. 55. These large-scale projects and programs are there to supplement a similar role that the government plays on a more individual level. 56. The government provides unemployment insurance, supplemental food programs, and medical care for when individuals are unemployed. 57. Although these are often big news during an economic downturn, they are always in place, so when an individual loses a job, they have a safety net to provide for them while they look for a new one. 58. The government also has controls in place to manage the supply of credit and money, but we will cover monetary policy separately.

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SKILL DEVELOPMENT / GUIDED PRACTICE

Role of government	Problem with market forces	Government responsibilities and solutions
Make rules that govern business behavior		
Provide low-profit goods and services		
Provide for defense and safety		
Provide rules for Negative Externalities		
Stabilize a struggling economy		



## Write

- 1. Describe the role the government plays in regulating business practices.**

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- 2. Explain why government often takes an active role in supplying goods and services to people.**

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## Write

**3. Why must a government intervene to prevent Negative Externalities?**

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**4. Why does the government invest in public works during a recession?**

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INDEPENDENT PRACTICE