Name ______________________ Date ______________ Class ______________

Economics and History Activity 3

The Role of Government

Suppose you invent a mechanism that will improve ship navigation in fog. Now suppose you show it to a big shipbuilding company, it steals your idea, and then increases its business significantly because its ships now have this wonderful device for safely navigating in fog. You do not see a dime of profit. What would you do? You would likely look to the government for assistance. Why? One of the government's roles in our economy is to enforce contracts and protect property rights.

THE GOVERNMENT AND THE ECONOMY

In 1776 economist Adam Smith described a system in which government has little to do with a nation's economic activity. He said that individuals left on their own would work for their own self-interest. In doing so, they would be guided to use resources efficiently and thus achieve the maximum good for society. However, in some instances the government does become involved in the U.S. free market economy. The chart below states five ways in which government might intervene in the economy.

EFFICIENCY AND COMPETITION

In economics, **efficiency** is maximum productivity that meets society's goals. Market efficiency is created through competition. **Competition** means that producers are rivals with other producers for profits; workers are rivals with other workers for wages; and buyers are rivals with other buyers for goods and services. These rivalries create efficiency. For example, producers who charge more than their rivals will not get buyers, so competition holds down the prices of goods and services and makes them affordable to more people.

COMPETITION AND MONOPOLIES

As noted in number 5 on the chart, the government may intervene in the economy to promote competition and, thus, efficiency. A **market failure** occurs when a problem in the market causes inefficiency. Monopolies cause market failure because they reduce competition. The late 1800s and early 1900s in America saw the creation of many monopolies, called trusts. Some of the common practices these trusts used to unfairly crush competition were:

Five Government Roles in the Economy

1. Enforcing Law	The government enforces contracts and property rights.
2. Ensuring Economic Stability	The government tries to stabilize the economy through fiscal and monetary policies to shield citizens from inflation, unemployment, and recession.
3. Redistributing Income	The government redistributes income. For example, it uses tax revenues to support those unable to help themselves.
4. Providing Public Goods	The government provides certain important public services that the market cannot provide, such as national defense or systems of courts and schools.
5. Regulating Economic Activity	The government intervenes in the economy by passing workplace and product safety standards and by promoting competition.

Name ____________________ Date ____________________ Class ____________________

UNIT 3

Economics and History Activity 3 (continued)

- Withdrawing their business from suppliers and retailers who did business with other rival companies
- Forcing smaller businesses out by temporarily lowering prices and then raising them after the smaller businesses failed
- Stealing inventions

Government first responded against monopolies with the Sherman Anti-Trust Act of 1890. This law established the principle that restraint or monopolization of trade or commerce is illegal. In 1914 the Clayton Act strengthened the Sherman Act. In the same year, the government established the Federal Trade Commission (FTC). The FTC is a watchdog agency that can investigate companies engaging in interstate commerce.

MONOPOLIES TODAY

Two court decisions ruled that Microsoft was a monopoly because it unfairly restricted the creativity and competition of an open market. The courts ruled that Microsoft practiced unfair competition against Netscape, an Internet browser. Microsoft insisted on including its Internet Explorer browser with its Windows operating system. The courts ruled this practice a restraint of trade. According to the courts, Microsoft was using the advantage of its huge share of the software market to unfairly compete in the Internet browser market.

The Federal Trade Commission, established in 1914, has the power to bring court cases against private businesses engaging in unfair trade practices.

APPLYING ECONOMICS TO HISTORY

Directions: Use the information you have read and the information in the chart to answer the following questions on a separate sheet of paper.

RECALLING INFORMATION

1. Why do monopolies make the market inefficient?
2. Name two unfair business practices of the trusts.
3. What unfair business practice caused the courts to rule Microsoft a monopoly?
4. What is competition supposed to create in the market?
5. What are the five categories of government intervention in a free market?
6. What effect does competition have on the prices at which sellers offer their goods and services?

CRITICAL THINKING

7. **Synthesizing Knowledge** When the government provides a check to support someone who is unable to work, the money is an example of a *transfer payment*. What role is government playing when it facilitates the transfer payment?
8. **Making Inferences** You have learned about some of the effects that competition has on the prices at which producers sell their goods and services. How does competition affect the wages that employers pay?