



The Free Enterprise System

Sec 5 Sec. 1 – Market-Oriented Economic Systems



What You'll Learn

- The basic principles of a free enterprise system
- The role of competition
- The importance of risk and profit
- The theory of supply and demand

Basic Principles – The free enterprise system is based on:



- Freedom of Ownership – We can own just about anything. The system encourages individuals to own businesses.



Intellectual Property Rights



- Are protected in a free enterprise system
- Patents – If you patent an invention, you alone own the rights to that item or idea.
- Trademark – A word, name, symbol, sound, or color that identifies a good or service and that cannot be used by anyone but the owner.
- Copyright – Involves anything that is authored by an individual, such as writings, music, and artwork.



- Competition – the struggle between companies for customers. Two kinds:

- Price Competition – focuses on the price



- Nonprice Competition – factors not related to price such as quality, service, location, reputation.



Monopolies

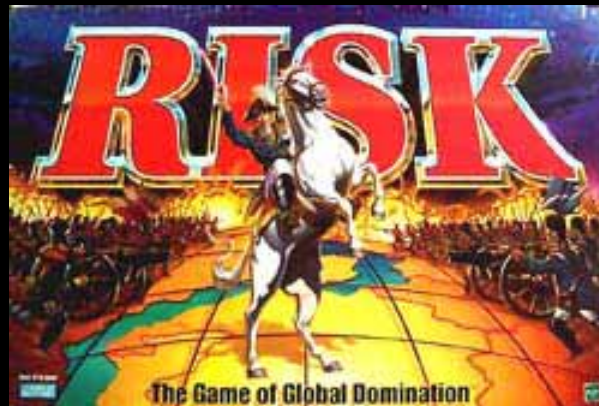


- When there is no **COMPETITION** and one firm controls the whole market.
- U.S. Government allows only a few, such as utility companies.





- Risk – The potential for loss or failure
 - As the potential for earnings gets greater, so does the risk.
 - One of every three businesses in the U.S. fails after one year.
 - Introducing new products is also risky. Up to 85 % of new products fail in the first year.





- Profit – the money earned from conducting business after all costs and expenses are paid.
 - Profit is the motivation for taking a risk.
 - Profits are high when sales are high and costs are low.



**As the
potential for
PROFIT
increases, the
RISK also
INCREASES.**



Supply and Demand

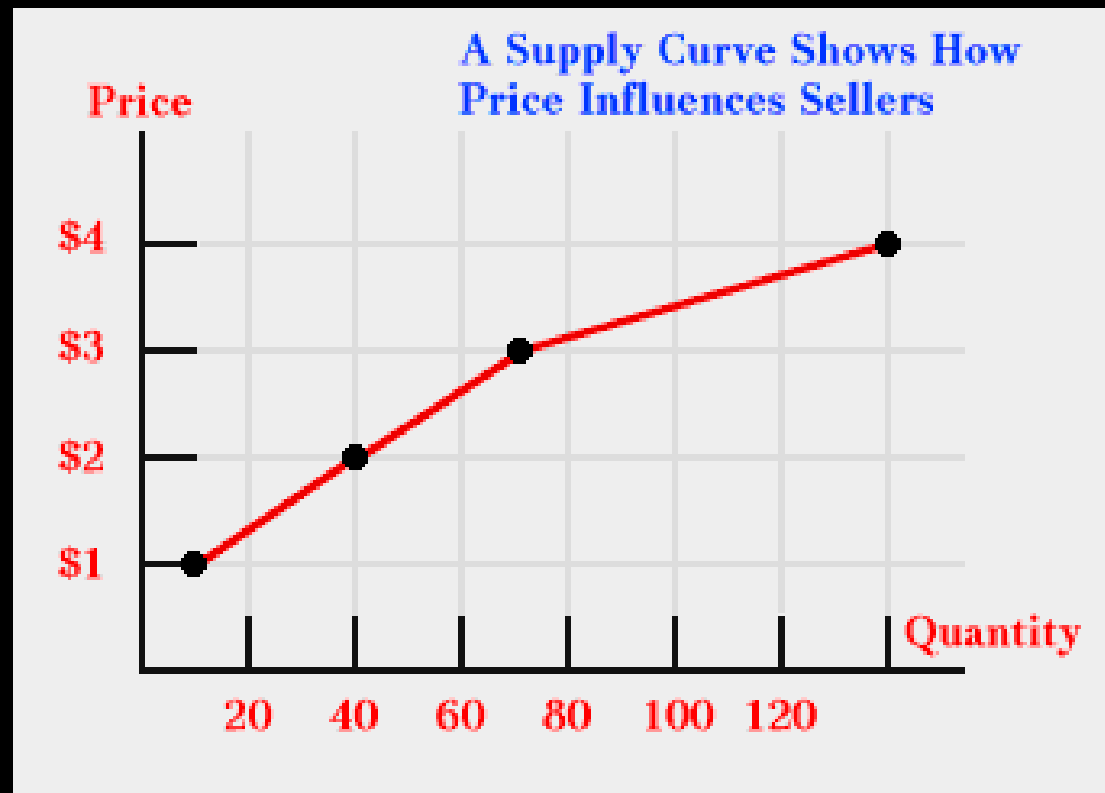


- In a market-oriented economy, supply and demand determine the prices and quantities of goods and services produced.

Supply



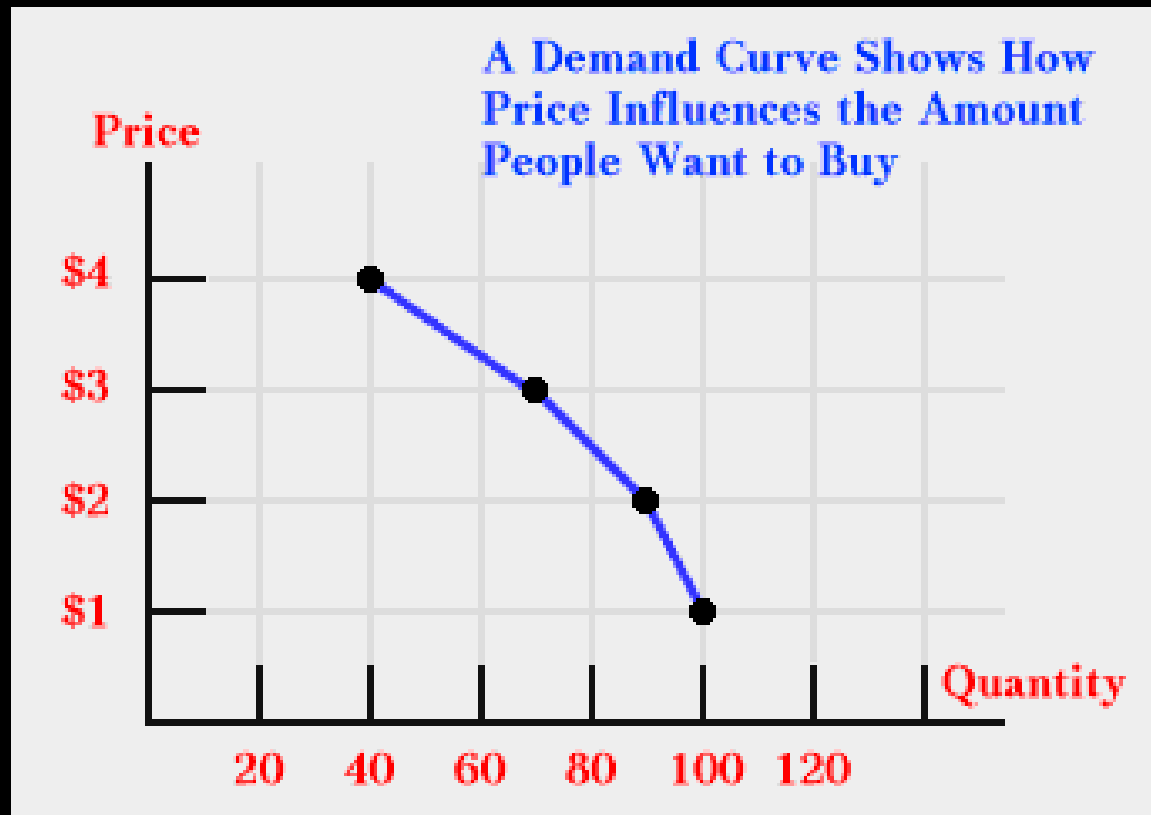
- The amount of goods producers are willing to make and sell



Demand



- The amount of goods consumers are willing to buy



Supply and Demand Theory



- Law of Supply – Price and quantity supplied move in the same direction. As prices rise, so will the quantity supplied.

Price



Quantity
Supplied

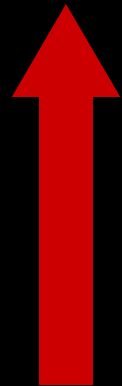


Supply and Demand Theory



- Law of Demand – Price and quantity demanded move in the opposite direction. As price increased, the quantity demanded decreases.

Price



Quantity
Demanded





- Surpluses – occur when supply exceeds demand
- Shortages – occur when demand exceeds supply
- Equilibrium – the amount being supplied is equal to the amount being demanded. Supply and demand are balanced.

FIGURE 4.8

Equilibrium

