In the United States economy, the government has a limited role. Most economic decisions are made by producers and consumers, not by the government. Economists, however, have identified six major functions that the government has within our market:

•Maintain Legal and Social Framework
•Maintain Competition
•Provide Public Goods and Services
•Redistribute Income
•Correct for Externalities
•Stabilize the Economy

This presentation explains those functions.

Economies cannot function without certain things that only the governments can provide.

In order for businesses to operate, there must be laws that establish such things as environmental restrictions, who has legal ownership of the company, and what are the rights of consumers. These form a level playing field for all of the businesses working in the same area. In addition to these laws, there must be courts that enforce those laws fairly.

Contracts are written or spoken agreements that are enforceable by law. Businesses and individuals have contracts to ensure that the rules are understood and followed by all parties. For example, if you sign a loan document to buy a car, you sign a contract that says how much you borrowed, what the interest rate for the loan is, and how many years you will be paying back the bank, among other things. If either you or the bank does not follow the terms of the contract, then either party can sue the other in court. The government plays the role as the regulator of contracts.

Governments are the only entities that can establish a monetary system. In the U.S., the Department of the Treasury prints all of the dollars and coins in circulation. If you look on any modern paper bill, you will see the signatures of the Treasurer and the Secretary of the Treasury on the front.

To make sure our economy grows and that consumers are treated fairly, our government creates and enforces antitrust laws and regulates monopolies.

Antitrust laws prevent businesses from collaborating to control too much of an industry or to set their own prices.

A monopoly is a large single seller or producer of goods and services. Normally, the seller is a large business or corporation. Think about your electric company or your cable company. Do they have any competitors? Since only one seller may exist in certain industries, the government closely regulates these monopolies so that you receive services at reasonable prices.

Suppose two huge airlines want to merge into one company. The government may step in using antitrust laws to ensure that these airlines do not threaten other competitors and control prices for the market. Any acquisition or merger that might possibly create a monopoly must be approved by the government.

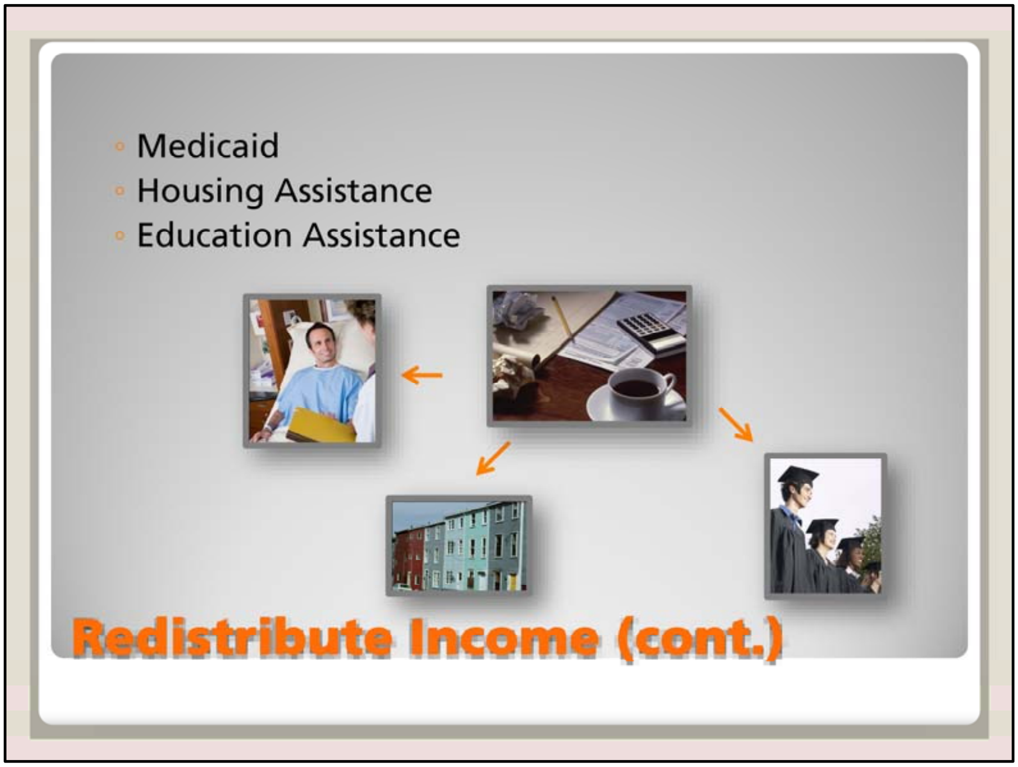
Check out this website to find companies involved in antitrust cases filed by the government. Have you ever heard of these companies?

Where do we get roads, schools, parks, and bridges? What if you couldn't drive down an interstate because you or your parents did not help pay for it? Would that be fair? Even in a free-market or capitalist economy, the government provides goods and services that businesses and individuals cannot provide for themselves.

These shared goods and services are called public goods. They are available to everyone. Taxes provide the money so the government can pay for these public goods to benefit everyone.

What does it mean to redistribute income? This is when the government transfers tax revenue from one group of people to another.

Most of the money that the U.S. Government has to spend comes from taxes on businesses and individuals. The government uses this money to fund different programs such as the military and infrastructure. Some money is distributed to specific government programs for individuals who are in need and meet certain qualifications. This is an example of redistributing income because some of the people who receive the money, especially the poorer ones, may actually receive more in services than they pay in taxes. In order to pay for these services, people with higher incomes pay more taxes. In essence, the money is being redistributed from the wealthier to the less affluent.

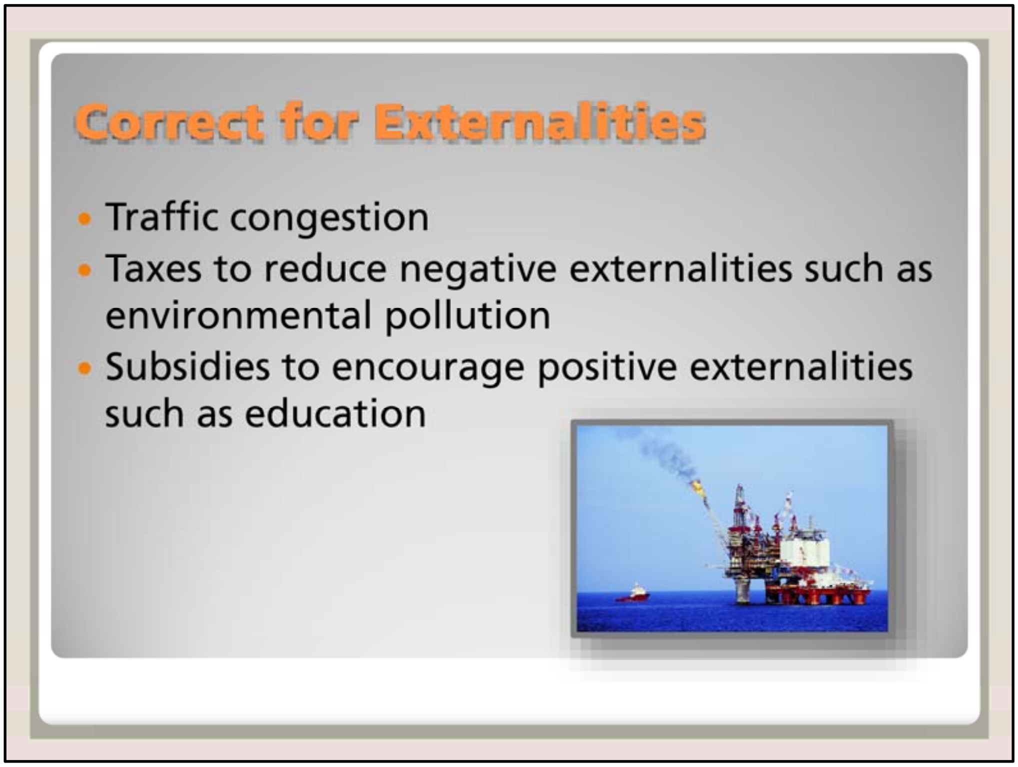


Why is it in the government's interest to redistribute income? Let's look at some example programs to find out.

Medicaid helps people pay for medical care if they don't have medical insurance and don't have enough money to pay for treatment. Since healthcare is very expensive, and sick people may have difficulty holding down jobs, the government helps pay their medical costs.

Housing Assistance – Some areas of the country have extremely high rents making it difficult for people to afford a place to live. Rather than having people live on the street, which can cause a number of other problems, the government may help people pay their rent or provide public housing.

Education Assistance – A highly-educated workforce is in the interest of the government because people who have more education are usually better able to find jobs. Because the cost of higher education is also very expensive, some people are not able to go to college even though they are capable of completing it. Since a more highly-educated workforce is better paid, and subsequently pays more taxes, the government may provide education assistance so that students who can't pay for tuition on their own may be able to afford college.



Are you thinking “what are externalities”? Basically, externalities are economic side effects or “spill-overs” that occur as a result of producing a good or service. Externalities can be positive or negative, and they affect more people than just a producer or consumer. Think about the BP oil spill that happened in the Gulf of Mexico in 2010. Did this incident affect only BP? Of course not. Let’s look at some other externalities.

Suppose a local business decides to hire individuals with disabilities. Does this create a positive or negative externality? Positive. This helps the economy because disabled individuals are learning a skill and are gainfully employed. In this case, the business also gets a reward from the government, called a subsidy, which is a payment that supports or encourages businesses for doing something special.

What about automobile pollution? Suppose the federal government requires producers of newer cars to include antipollution devices. Is this a negative or positive externality?

A growing economy is in the best interest of governments, citizens, and businesses. When recessions or downturns occur, oftentimes the government steps in and uses the tools that it has to help stabilize the economy, and help it try to grow again. What are some of these tools?

The government can put more money into hands of consumers and businesses by sending out tax rebate checks, or reducing taxes. By giving people and businesses more money to spend, the hope is they will buy more goods from producers. This doesn't always work as planned since sometimes people take the extra money and save or invest it instead.

The government can also spend more money by building roads and infrastructure. This will help the construction companies and their employees because they will have more money to spend. Again, the people and businesses may choose to save it instead. Also, the government either has to take the money from another government program, or borrow it in order to pay for the projects. This can have impacts in the future.

Lowering the interest rate, or the money people pay to borrow money, is another tool the government can use to make the economy grow. If the interest rate is lower, then it costs less to borrow money. Individuals and businesses might be more likely to take out a loan to buy things such as cars, houses, and large equipment. People may not always respond to the lower interest rate, however, so it may not have much of an effect.

Finally, the government can use all of its tools together to try and keep inflation under control. The basic concept behind inflation is that things cost more tomorrow than they do today. If inflation is high, the price of things goes up quickly. A relatively low, stable rate of inflation makes it easier for businesses and individuals to make plans.

Think about the economy in 2008-2010. What has the government done to help stabilize the economy? Have they tried to produce more government jobs to decrease unemployment? Have they lowered taxes for individuals to put more money in their pockets? Have they been successful?