Chapter 2: Understanding Economics and How It Affects Business

INTRODUCTION

This Instructor's Manual has been revised to include all teaching resources offered for your course. It is organized for ease of use, so you can follow along in the classroom and use relevant materials as they are needed.

CONTENTS

Icebreaker Activity
Brief Chapter Outline, Learning Objectives, and Classroom Activities
Lecture Enhancers
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Connect Instructor's Manual

ADDITIONAL RESOURCE

For more lecture-enhancing examples and videos, visit our blog at www.introbiz.tv.

WHAT'S NEW IN THIS EDITION

Additions:

- Getting to Know Thomas Piketty, economist and author of *Capital in the 21st Century.*
- Name That Company
- Adapting to Change: The World Population is Popping
- Making Ethical Decisions: Bad Medicine for Consumers?
- Reaching Beyond Our Borders: Inflation at the Speed of Sound
- Career Exploration

Revisions:

Statistical data and examples throughout the chapter were updated to reflect current information. In addition:

- Subsection "Gross Domestic Product" was enhanced with a brief description of the underground economy.
- Subsection "Stabilizing the Economy through Fiscal Policy" was enhanced with a brief identification of entitlements.
- Figure 2.4 was redesigned.

Deletions:

- Name that Company
- Subsection "Fiscal Policy in Action during an Economic Crisis" (the key term Keynesian economic theory was moved to the subsection "Stabilizing the Economy through Fiscal Policy").
- Boxes: Making Ethical Decisions, Spotlight on Small Business, and Reaching Beyond Our Borders

ICEBREAKER ACTIVITY

Money and the Financial System

Exercise:	**Create a video.**
Learning Objectives:	2-6 Contrast fiscal policy and monetary policy, and explain how each affects the economy.
Instructor Prep Time:	10 - 20 minutes
Supplies:	N/A
Class Type:	Face-to-Face, Hybrid, and Online
Ideal Class Size:	N/A
Set-up Time:	
Face-to-Face Hybrid	In-class/hybrid 5 minutes to explain activity, hand out instructions or direct students to the posted instructions on the course platform.
Online	5 minutes to post assignment.
Student Work Time:	Allow 1 week to complete the activity.
Wrap-up Time:	
Face-to-Face Hybrid	10 - 15 minutes to show student videos and 15 minutes to discuss "take-aways".
Online	Online chat room – 1 to 2 days to post
Evaluation Suggestions:	The least controversial method is to give everyone who completes the activity a certain amount of points for example 10 points or this activity could replace a quiz grade. 2. Award the "top" 3 videos (as voted on by the class) "bonus" points.

Overview:
How to make the exercise a success

Set-up:

- This is a creative exercise to get students thinking about how pervasive money is to our culture.
- This is a fun activity that combines music, internet searches, and videos.
- You can set-up the exercise with a short history of money and common phrases (5 minutes or less) that are derived from our culture's concept of money, "Green With Envy," "Money Pit," etc. (This is optional and the activity will be successful without this discussion).
- You can create your own money/art slide show if you want an example for your students or use the attached 3 slide power point. You can in-bed a song into the slide (a list of the Top Ten Requested Money Songs is attached) to enhance the example.
- Allow the students 1 week to create their video or slide show and have them post it to the course website.
- Grading the activity:

1. The least controversial method is to give everyone who completes the activity a certain amount of points for example 10 points or this activity could replace a quiz grade.
2. Award the "top" 3 videos (as voted on by the class) "bonus" points.

Day of: Show the "top" 3 – 5 videos depending on the length and time.

Student Instructions:

- Students Steps for the activity:

1. Create a video that incorporates "Money Songs" and "art" that includes a "money/banking theme".

2. Use your imagination and have fun with this activity. There is no "right" or "wrong" videos. Be creative and remember the theme is "money, its functions, and characteristics". You will have one week to create and post the video to the course website (refer to the deadline).

3. After you post your video, watch the other students' videos and "vote"/ "like" your favorite 3 videos.

Wrap-up/"Take-aways" suggested topics:
In-person/hybrid classes: Wrap-up and discussion allot 15 minutes.

- Use this as a fun transition into the American Financial System.

Online: Instructors' and students' comments posted on the discussion page or a short "wrap-up" video (mini-lecture) of less than 20 minutes posted to the course platform.

BRIEF CHAPTER OUTLINE, LEARNING OBJECTIVES AND CLASSROOM ACTIVITIES

Chapter Opener		**Summary**	**PowerPoint Slides**
Getting to Know THOMAS PIKETTY		Thomas Piketty is an internationally renowned scholar on income inequality. Unlike many scholars, he wants to reach beyond the academic elite and wrote *Capital in the Twenty-First Century* to illustrate the last 100 years of economic activity to the whole world.	PPt 6
Name That Company		This philanthropic initiative was started by two of the wealthiest men in the world. Its purpose is to encourage the world's richest individuals and families to donate the majority of their wealth to fight poverty and support health issues and education. What is the name of this organization? (Students should read the chapter before guessing the initiative's name: The Giving Pledge)	PPt 7
LO 2-1	**Explain basic economics.**	**Key Terms:** economics macroeconomics microeconomics resource development invisible hand	

Lecture Notes:	Classroom Activities	PowerPoint Slides
I.HOW ECONOMIC CONDITIONS AFFECT BUSINESSES	**Connect Application Exercises**	
A. An economic system either promotes or hinders business activity.	**Entrepreneurship in the Dynamic Business Environment—iContact Video Case**	
B. Much of America's business success is due to an economic and social climate that allows businesses to operate freely.	see p. 47 of this manual for summary and follow-up activity.	PPt 8
1. Any change in the U.S. economic system has a major influence on the business system.		
2. Also, **GLOBAL ECONOMICS** and **WORLD POLITICS** have a major influence on U.S. business.		
C. **WHAT IS ECONOMICS?**		
1. ***ECONOMICS*** is the study of how society chooses to employ resources to produce goods and services and distribute them for consumption among various competing groups and individuals.		PPt 9
2. ***MACROECONOMICS*** is the part of economic study that looks at the operation of a nation's economy as a whole.		PPt 1-8
3. ***MICROECONOMICS*** is the part of economic study that looks at the behavior of people and organizations in particular markets.		
4. *Economics* is sometimes defined as the allocation of scarce resources.		
5. ***RESOURCE DEVELOPMENT*** is the study of how to increase resources and to create the conditions that will make better use of those resources.		
6. Businesses help economic systems by inventing		

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products and services that expand available resources *(example: mariculture, raising fish in ocean pens).*

D. **THE SECRET TO CREATING A WEALTHY ECONOMY**

1. The English economist Thomas Malthus believed that population growth would outstrip resources.
   a. In response, Thomas Carlyle called economics **"THE DISMAL SCIENCE."**
   b. **WORLD POPULATION** is currently growing more slowly than expected.
   c. But population in the **DEVELOPING WORLD** will continue to climb quickly.
2. Others believe that a large population can be a valuable resource, especially if people are educated.
3. The **SECRET TO ECONOMIC DEVELOPMENT** can be summed up in the saying *"Give a man a fish and you feed him for a day, but teach a man to fish and you feed him for a lifetime."*
4. Business owners provide **JOBS AND ECONOMIC GROWTH** for their employees as well as for themselves.
5. Economists and governments examine what makes some countries relatively rich and other countries relatively poor, then develop policies that lead to **INCREASED PROSPERITY** for everyone.

E. **ADAM SMITH AND THE CREATION OF WEALTH**

1. **ADAM SMITH** believed wealth could be created through entrepreneurship.

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critical thinking exercise 2-1

Know Your History of Economics
This online exercise is designed to help students gather information about economics from a historic perspective. (See the complete exercise on page 37 of this manual.)

bonus case 2-1

Smartphones Sweep the Nation of Myanmar

For decades, the government in Myanmar imposed strict economic isolation and control over its markets. After the government finally ended the state's monopoly over telecommunication, Myanmar's citizens were opened up to a whole new world. (See the complete case, discussion questions, and suggested answers beginning on page 42 of this manual.)

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PPt 12-13

PPt 15

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a. Rather than dividing *fixed* resources, Smith envisioned creating *more* resources so that everyone could be wealthier. b. In 1776, Smith wrote ***THE WEALTH OF NATIONS,*** in which he outlined steps for creating prosperity. 2. Smith believed that **FREEDOM** was vital to the survival of any economy. 3. Also, he believed that people will work hard if they have **INCENTIVES** for doing so. 4. Smith is considered to be the **FATHER OF MODERN ECONOMICS.** F. **HOW BUSINESSES BENEFIT THE COMMUNITY** 1. The ***INVISIBLE HAND*** is a phrase coined by Adam Smith to describe the process that turns self-directed gain into social and economic benefits for all. 2. Basically, this meant that a person working hard to make money for his or her own **PERSONAL INTEREST** would *(like an invisible hand)* also **BENEFIT OTHERS.** a. *For example, a farmer trying to make money would grow as many crops as possible.* b. This would provide jobs and needed food for others. c. If everyone worked hard in his or her own self-interest, Smith said, society as a whole would prosper.	**lecture enhancer 2-1** **A New Crop of Consumers in Africa** Africa has a growing middle class that rivals both China and India. Despite the persisting wealth disparities, more Africans have disposable incomes in which they can buy goods from others. (See the complete lecture enhancer on page 28 of this manual.)	PPt 16-17

3. Smith assumed that as people become wealthier, they would reach out to help the less fortunate, but that hasn't always happened. a. Many U.S. businesspeople are becoming concerned about social issues and their obligation to return to society some of what they've earned. b. It is important for businesses to be ethical as well as generous.			
Figures: N/A			
LO 2-2	**Explain what capitalism is and how free markets work.**	**Key Terms:** capitalism state capitalism supply demand market price perfect competition monopolistic competition oligopoly monopoly	

Lecture Notes:	Classroom Activities	PowerPoint slides:
II. UNDERSTANDING FREE MARKET CAPITALISM		
A. Following the ideas of Adam Smith, businesspeople created more wealth than ever before.		PPt 19
1. But **GREAT DISPARITIES** in wealth remained or even increased.	**bonus case 2-2**	
2. Although it is not easy, opportunities to start one's own business have always been there, especially in a free market.	**Foundations of the Capitalist System** What are the moral, ethical, and spiritual foundations of capitalism? (See the complete case, discussion questions, and suggested answers beginning on page 44 of this manual.)	
3. ***CAPITALISM*** is an economic system in which all or most of the factors of production and distribution are privately owned and operated for profit.		
a. In capitalist countries, businesspeople decide how to use their resources and how much to charge.	**lecture enhancer 2-2** **Tracking the Underground Economy** Not all incomes are reported to the IRS. Is the U.S. government losing out? (See the complete lecture enhancer on page 29 of this manual.)	
b. No country is purely capitalist, but the foundation of the U.S. is capitalism.		
c. Capitalism is also the foundation for the economics of England, Canada, Australia, and most developed nations.		
d. Some countries are practicing **STATE CAPITALISM** where the state runs some businesses instead of private owners (e.g., China).		PPt 20
4. People under free-market capitalism have **FOUR BASIC RIGHTS:**		
a. The right to **PRIVATE PROPERTY**		
b. The right to **OWN A BUSINESS** and to keep all		

of that business's profits after taxes c. The right to **FREEDOM OF COMPETITION** d. The right to **FREEDOM OF CHOICE** 5. One benefit of such rights is that people are willing to take more **RISKS** than they would otherwise. 6. President Franklin Roosevelt believed **FOUR ADDITIONAL FREEDOMS** were essential: a. Freedom of **SPEECH AND EXPRESSION** b. Freedom to **WORSHIP IN YOUR OWN WAY** c. Freedom from **WANT** d. Freedom from **FEAR**		PPt 21-22
B. **HOW FREE MARKETS WORK** 1. In a free-market system, decisions about what to produce and in what quantities are made by **THE MARKET.** 2. **CONSUMERS** send signals to **PRODUCERS** about what to make, how many, and so on through the mechanism of **PRICE.** *(Text example: T-shirts supporting favorite baseball teams.)* 3. In a free market the **PRICE** tells producers how much to produce, reducing the chances of a long-term shortage of goods.	**lecture enhancer 2-3** **The Circular Flow Model** The Circular Flow Model is used to explain how businesses and individuals interact in a free-market economy. (See the complete lecture enhancer on page 30 of this manual.)	PPt 24
C. **HOW PRICES ARE DETERMINED** 1. Prices in a free market are not determined by sellers; rather, buyers and sellers negotiating in the marketplace determine them. 2. Price is determined through the economic concepts		PPt. 26

of supply and demand.

D. **THE ECONOMIC CONCEPT OF SUPPLY**

1. ***SUPPLY*** refers to the quantity of products that manufacturers or owners are willing to sell at different prices at a specific time.
2. The amount supplied will **INCREASE** as the price **INCREASES** (**DIRECT** relationship).
3. The quantity producers are willing to **SUPPLY** at certain prices is illustrated on a **SUPPLY CURVE.**

E. **THE ECONOMIC CONCEPT OF DEMAND**

1. ***DEMAND*** refers to the quantity of products that people are willing to buy at different prices at a specific time.
2. The quantity demanded will **DECREASE** as the price **INCREASES** (**INVERSE** relationship).
3. The quantities consumers are willing to buy at certain prices are illustrated on a **DEMAND CURVE.**

F. **THE EQUILIBRIUM PRICE, OR MARKET PRICE**

1. The key factor in determining the quantity supplied and the quantity demanded is **PRICE.**
   a. At the **EQUILIBRIUM POINT**, the supply and demand curves cross**,** and the quantity demanded equals the quantity supplied.
   b. ***MARKET PRICE*** is the price determined by supply and demand.
2. In free-market economies it is the **INTERACTION** between **SUPPLY** and **DEMAND** that determines the

PPt 27

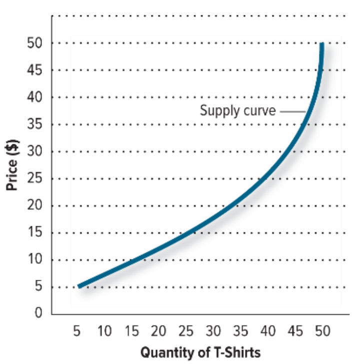
critical thinking exercise 2-2

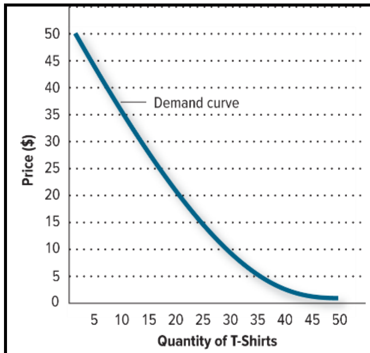
Finding the Equilibrium Point

How does the equilibrium price of a product change when forces in the economy change? (See the complete exercise on page 38 of this manual.)

market price in the long run. a. If **SURPLUSES** (too many products) develop, a signal is sent to sellers to **LOWER** the price. b. If **SHORTAGES** (not enough products) develop, a signal is sent to sellers to **INCREASE** the price. c. Eventually, supply will again equal demand. 3. In countries without a free-market system, there is no such mechanism, so there are often **SHORTAGES OR SURPLUSES.** 4. When government interferes in free markets, surpluses and shortages may develop.		
G. **COMPETITION WITHIN FREE MARKETS** 1. Competition exists in different degrees, ranging from perfect to nonexistent. 2. ***PERFECT COMPETITION*** is the degree of competition in which there are many sellers in a market and none is large enough to dictate the price of a product. a. Sellers produce products that appear to be **IDENTICAL**. b. *There are no true examples of perfect competition, but agricultural products are often used as an example.* 3. ***MONOPOLISTIC COMPETITION*** is the degree of competition in which a large number of sellers produce very similar products that buyers nevertheless perceive as different.		PPt 31

a. **PRODUCT DIFFERENTIATION**, making buyers think similar products are different, is a key to success. b. *The fast-food industry is an example.* 4. An ***OLIGOPOLY*** is a degree of competition in which just a few sellers dominate a market. a. The **INITIAL INVESTMENT** required to enter the market is usually high. b. Prices among competing firms tend to be close to the same. c. *Examples include breakfast cereal and soft drinks.* 5. A ***MONOPOLY*** is a degree of competition in which only one seller controls the total supply of a product or service, and sets the price. a. U.S. laws prohibit the creation of monopolies, but do permit **APPROVED MONOPOLIES** in markets for public utilities. b. New laws have ended the monopoly status of utilities in some areas, creating intense competition among utility companies. c. **DEREGULATION** is meant to increase competition and lower prices for consumers. H. **BENEFITS AND LIMITATIONS OF FREE MARKETS** 1. The free market allows open competition among companies. 2. Free-market capitalism provides opportunities for		PPt 32

poor people to work their way out of poverty. 3. Capitalism also creates **INEQUITIES** between those who have gained wealth and those who are not able to. 4. Not all businesspeople agree on how to deal with this **INEQUITY**. 5. Greed has led some businesspeople to engage in **UNETHICAL PRACTICES** and deceive the public. 6. Some government **REGULATIONS ARE NECESSARY** to protect stockholders and vulnerable citizens.	critical thinking exercise 2-3 **Standard of Living Comparison** This exercise asks students to research key economic indicators for a capitalist country, a socialist country, and a communist country. (See the complete exercise on page 41 of this manual.)	
Figures:  	**FIGURE 2.1** **THE SUPPLY CURVE AT VARIOUS PRICES** The supply curve rises from left to right. Think it through. The higher the price of T-shirts goes (the vertical axis), the more sellers will be willing to supply. FIGURE 2.2	PPt 28 PPt 29



THE DEMAND CURVE AT VARIOUS PRICES
This is a simple demand curve showing the quantity of T-shirts demanded at different prices. The demand curve falls from left to right. It is easy to understand why. The lower the price of T-shirts, the higher the quantity demanded.

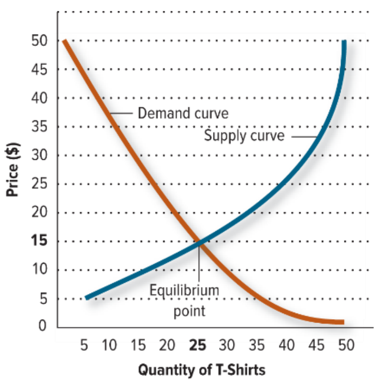


FIGURE 2.3
THE EQUILIBRIUM POINT
The place where quantity demanded and quantity supplied meet is called the equilibrium point. When we put both the supply and demand curves on the same graph, we find that they intersect at a price where the quantity supplied and the quantity demanded are equal. In the long run, the market price will tend toward the equilibrium point.

PPt 30

LO 2-3	Compare socialism and communism.	Key Terms: socialism, brain drain, communism

Lecture Notes:	Classroom Activities:	PowerPoint slides:
III. UNDERSTANDING SOCIALISM A. ***SOCIALISM*** is an economic system based on the premise that some, if not most, basic businesses should be owned by the government so that profits can be distributed		PPt 36-37

among the people. 1. Entrepreneurs can own small businesses, but their profits are **STEEPLY TAXED** to pay for social programs. 2. Advocates of socialism acknowledge the major benefits of capitalism, but believe that **WEALTH SHOULD BE MORE EVENLY DISTRIBUTED.**		
B. The **MAJOR BENEFIT** of socialism is **SOCIAL EQUALITY**. 1. Income is taken from the wealthier people and redistributed to the poorer members of the population. 2. Workers in socialist countries are given free education, free health care, free child care, and more employee benefits.		PPt 38
C. **THE NEGATIVE CONSEQUENCES OF SOCIALISM** 1. Socialism may create **EQUALITY**, but it **TAKES AWAY SOME WORK INCENTIVES**. 2. Tax rates in some nations once reached 83%. 3. Because wealthy professionals have very high tax rates, many of them leave socialist countries for countries with lower taxes. 4. The loss of the best and brightest people to other countries is called ***BRAIN DRAIN.*** 5. Socialist systems can result in **FEWER INVENTIONS AND LESS INNOVATION.**		PPt 39
IV.UNDERSTANDING COMMUNISM A. ***COMMUNISM*** is an economic and political system in		PPt 40

which the government makes almost all economic decisions and owns almost all the major factors of production. B. **PROBLEMS WITH COMMUNISM** 1. The government has no way of knowing what to produce because prices don't reflect **SUPPLY** and **DEMAND**. 2. **SHORTAGES** of many items may develop. 3. Communism doesn't inspire businesspeople to work hard, and is slowly disappearing as an alternative economic form. C. Most communist countries today are **SUFFERING SEVERE ECONOMIC DEPRESSION**, including North Korea and Cuba. 1. Some countries favor communism. 2. The trend toward free markets is growing.		
Figures: N/A		

LO 2-4	**Analyze the trend toward mixed economies.**	**Key Terms:** free-market economies command economies mixed economies

Lecture Notes:	**Classroom Activities:**	**PowerPoint slides:**
V.THE TREND TOWARD MIXED ECONOMIES		
A. There are two dominant economic systems:		PPt 42
1. **FREE-MARKET ECONOMIES**		
a. ***FREE-MARKET ECONOMIES*** are economic systems in which the market largely determines what goods and services get produced, who gets them, and how the economy grows.		
b. This system is commonly known as **CAPITALISM.**		
2. **COMMAND ECONOMIES**		
a. ***COMMAND ECONOMIES*** are economic systems in which the government largely decides what goods and services will be produced, who will get them, and how the economy will grow.		
b. These economies are known as **SOCIALISM** and **COMMUNISM**.		
B. Communist governments are disappearing and some socialist governments are cutting back social programs.		
C. No one economic system is perfect by itself.		PPt 43
1. Free-market mechanisms haven't been responsive enough to a nation's social and economic needs and haven't adequately protected the environment.		
2. Socialism and communism haven't always created enough jobs or wealth to keep economies growing fast enough.		

3. Socialist and communist countries have moved toward **CAPITALISM**.

4. So-called capitalist countries tend to move toward **SOCIALISM**.

5. No country is purely socialist or purely capitalist, rather some **MIX OF THE TWO SYSTEMS**.

6. The result has been a **BLEND** of capitalism and communism.

D. ***MIXED ECONOMIES*** are economic systems in which some allocation of resources is made by the market and some by government.

PPt 44

E. **THE U.S. HAS A MIXED ECONOMY.**

1. The role of government in many parts of the economy is a matter of some debate.

2. For instance, the government is the largest employer in the U.S.

Figures:

	CAPITALISM* (United States)	SOCIALISM (Sweden)	COMMUNISM (North Korea)	MIXED ECONOMY (Germany)
Social and Economic Goals	Private ownership of land and business. Liberty and the pursuit of happiness. Free trade. Emphasis on freedom and the profit motive for economic growth.	Public ownership of major businesses. Some private ownership of smaller businesses and shops. Government control of education, health care, utilities, mining, transportation, and media. Very high taxation. Emphasis on equality.	Public ownership of all businesses. Government-run education and health care. Emphasis on equality. Many limitations on freedom, including freedom to own businesses and to assemble to protest government actions.	Private ownership of land and business with government regulation. Government control of some institutions (e.g., mail). High taxation for defense and the common welfare. Emphasis on a balance between freedom and equality.
Motivation of Workers	Much incentive to work efficiently and hard because profits are retained by owners. Workers are rewarded for high productivity.	Capitalist incentives exist in private businesses. Government control of wages in public institutions limits incentives.	Very little incentive to work hard or to produce quality goods or services.	Incentives are similar to capitalism except in government-owned enterprises, which may have fewer incentives.
Control over Markets	Complete freedom of trade within and among nations. Some government control of markets.	Some markets are controlled by the government and some are free. Trade restrictions among nations vary and include some free-trade agreements.	Total government control over markets except for illegal transactions.	Some government control of trade within and among nations (trade protectionism).
Choices in the Market	A wide variety of goods and services is available. Almost no scarcity or oversupply exists for long because supply and demand control the market.	Variety in the marketplace varies considerably from country to country. Choice is directly related to government involvement in markets.	Very little choice among competing goods.	Similar to capitalism, but scarcity and oversupply may be caused by government involvement in the market (e.g., subsidies for farms).
Social Freedoms	Freedom of speech, press, assembly, religion, job choice, movement, and elections.	Similar to mixed economy. Governments may restrict job choice, movement among countries, and who may attend upper-level schools (i.e., college).	Very limited freedom to protest the government, practice religion, or change houses or jobs.	Some restrictions on freedoms of assembly and speech. Separation of church and state may limit religious practices in schools.

*The United States is a mixed economy based on a foundation of capitalism.

FIGURE 2.4
COMPARISONS OF KEY ECONOMIC SYSTEMS

LO 2-5	Describe the economic system of the United States, including the significance of key economic indicators (especially GDP), productivity, and the business cycle.	Key Terms: gross domestic product gross output unemployment rate inflation disinflation deflation stagflation consumer price index business cycles recession depression

Lecture Notes:	Classroom Activities:	PowerPoint slides:
VI.UNDERSTANDING THE U.S. ECONOMIC SYSTEM A. **KEY ECONOMIC INDICATORS** 1. **GROSS DOMESTIC PRODUCT (GDP)** a. ***GROSS DOMESTIC PRODUCT (GDP)*** is the total value of final goods and services produced in a country in a given year. b. Both domestic and foreign-owned companies can produce goods and services included in GDP. c. A major influence on the growth of GDP is how productive the workforce is. d. ***GROSS OUTPUT (GO)*** is a measure of total sales volume at all stages of production. e. GO is considered a better indicator of the business cycle. 2. **THE UNEMPLOYMENT RATE** a. The ***UNEMPLOYMENT RATE*** is the number of civilians at least 16 years old who are unemployed and tried to find a job within the	lecture enhancer 2-4 **How Accurate is GDP?** Many components go in to creating the GDP. However, some argue it's not entirely accurate. (See the complete lecture enhancer on page 31 of this manual.)	PPt 46-49

prior four weeks. b. There are four types of unemployment: frictional, structural, cyclical, and seasonal (as seen in **Text Figure 2.5.)** c. The U.S. tries to protect those who are unemployed because of recessions, industry shifts, and other cyclical factors. 3. **INFLATION AND PRICE INDEXES** a. **THE PRICE INDEXES** help measure the health of the economy. b. ***INFLATION*** is a general rise in the prices of goods and services over time. c. ***DISINFLATION*** is a situation in which price increases are slowing *(the inflation rate is declining).* d. ***DEFLATION*** is a situation in which prices are declining, occurring when countries produce so many goods that people cannot afford to buy them all. e. ***STAGFLATION*** is a situation when the economy is slowing, but prices keep going up anyhow. f. **CONSUMER PRICE INDEX (CPI)** i. The ***CONSUMER PRICE INDEX (CPI)*** consists of monthly statistics that measure the pace of inflation or deflation. ii. Some wages, rents, government benefits, and interest rates are based	**lecture enhancer 2-5** **Other Economic Indicators** In addition to the GDP, CPI, and unemployment indicators, there are other economic indicators that can forecast changes in the economy. (See the complete lecture enhancer on page 32 of this manual.)	PPt 53-54

on the CPI. iii. **CORE INFLATION** is the CPI minus food and energy costs. g. The ***PRODUCER PRICE INDEX (PPI)*** is an index that measures prices at the wholesale level. B. **PRODUCTIVITY IN THE UNITED STATES** 1. U.S. productivity has gone up in recent years because computers have made production faster. 2. The **HIGHER PRODUCTIVITY** is, the **LOWER COSTS** are in producing goods and services, and the lower prices can be. 3. The U.S. economy is a **SERVICE ECONOMY**—very labor-intensive—creating productivity issues. C. **PRODUCTIVITY IN THE SERVICE SECTOR** 1. Technologies may add to the quality of the services but not to the **OUTPUT PER WORKER** which is the definition of productivity. 2. New measures of productivity for the service economy are needed to measure **QUALITY** as well as **QUANTITY** of output. D. **THE BUSINESS CYCLE** 1. ***BUSINESS CYCLES*** are the periodic rises and falls that occur in economies over time. 2. Joseph Schumpeter identified **FOUR PHASES OF BUSINESS CYCLES:** a. In an **ECONOMIC BOOM,** there is strong business activity. b. A ***RECESSION*** is two or more consecutive	lecture enhancer 2-6 **Restaurants Serve Up Jobs Across the Country** The U.S. economy has been recovering for a few years now and we're seeing big gains in many industries. But growth in these sectors doesn't compare to the growth of restaurant jobs. (See the complete lecture enhancer on page 34 of this manual.)	PPt 55 PPt 57 PPt 59

quarters of decline in the GDP.

c. A ***DEPRESSION*** is a severe recession, usually accompanied by deflation.

d. A **RECOVERY** occurs when the economy stabilizes.

3. The goal of economists is to predict these fluctuations, which can be very difficult.
4. Fluctuations in the economy are **INEVITABLE**.
5. The government uses **FISCAL** and **MONETARY** policy to minimize these disruptions.

lecture enhancer 2-7

What Is a Depression?
There is a well-established definition for a recession. A depression is, well, not so easy to define. (See the complete lecture enhancer on page 35 of this manual.)

Figures:

FIGURE 2.5
U.S UNEMPLOYMENT RATE 1989-2017

PPt 50

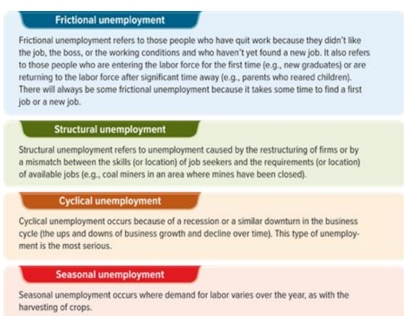


FIGURE 2.6
FOUR TYPES OF UNEMPLOYMENT

PPt 51

LO 2-6	Contrast fiscal policy and monetary policy, and explain how each affects the economy.	Key Terms: fiscal policy; Kenesian economic theory; national debt

		monetary policy

Lecture Notes:	Classroom Activities:	PowerPoint slides:
E. **STABILIZING THE ECONOMY THROUGH FISCAL POLICY** 1. ***FISCAL POLICY*** is the federal government's efforts to keep the economy stable by increasing or decreasing taxes or government spending. 2. ***KEYNESIAN ECONOMIC THEORY*** is the theory that a government policy of increasing spending and cutting taxes could stimulate the economy in a recession. 3. The first half of fiscal policy involves **TAXATION.** a. **HIGH TAX RATES** may discourage small-business ownership. b. **LOW TAX RATES** would tend to give the economy a boost. 4. The second half of fiscal policy involves **GOVERNMENT SPENDING.** a. The **NATIONAL DEFICIT** is the amount of money that the federal government spends over and above the amount it gathers in taxes. b. The ***NATIONAL DEBT*** is the sum of government deficits over time. c. The national debt of the U.S. is over **$17 TRILLION**. 5. One way to lessen the annual deficits is to **CUT GOVERNMENT SPENDING**, but there is a continuing		PPt 60-61

need for social programs and for military spending. F. **USING MONETARY POLICY TO KEEP THE ECONOMY GROWING** 1. The **FEDERAL RESERVE SYSTEM (THE FED)** is a semiprivate organization that decides how much money to put into circulation. 2. ***MONETARY POLICY*** is the management of the monetary supply and interest rates; it is controlled by the Fed. a. When the economy is booming, the Fed tends to **RAISE INTEREST RATES.** b. **LOWERING INTEREST RATES** encourages more business borrowing. c. Raising and lowering interest rates helps control the rapid ups and downs of the economy. d. After the financial crisis in 2008, the Fed kept interest rates near zero. 3. The Federal Reserve also controls the **MONEY SUPPLY**. a. The **MORE MONEY** the Fed makes available to businesspeople, the **FASTER THE ECONOMY GROWS.** b. To **SLOW THE ECONOMY**, the Fed **LOWERS** the money supply. 4. The economic goal is to keep the economy growing.		PPt 64

LECTURE ENHANCERS

lecture enhancer 2-1

A NEW CROP OF CONSUMERS IN AFRICA

While a great deal of focus has been given to burgeoning economic superpowers like India and China, Africa has a growing middle class that rivals both those countries. Thanks to open markets and greater political stability, economists estimate that Africa's middle class (those who spend $2–20 a day) makes up 34% of the continent's population. A new study shows that this 313-million-strong middle class, which has grown 60% over the last decade, is upwardly mobile and in the market for foreign goods.

However, this isn't to say that Africa is prosperous. Sixty-one percent of Africa's 1 billion people continue to live on less than $2 a day. Vast wealth disparities persist as well. The net worth of 100,000 of the continent's richest citizens accounts for 60% of its gross domestic product. A further 180 million people can afford to spend only $2 to $4 a day, making them vulnerable to economic shifts that could knock them out of the middle class. Even those firmly entrenched in the new consumer class are far from rich, with daily spending budgets between $4 and $20.

To many, the fact that a significant portion of Africa's population has disposable income at all is cause for celebration. In fact, some analysts credit this new breed of consumer for buffering Africa against much of the global financial crisis. Also with jobs on the rise, rural Africans are flocking to cities. The U.S. ambassador to South Africa even claims that Africa is now nearly as urbanized as China. Again, all this newfound growth must be viewed alongside current stories of tragedies against citizens in Uganda and Nigeria as well as the violent repressions in Libya. Still, one can only hope that much of the violence and chaos that has defined Africa for decades is now in the past, leaving the future open for more political freedom and economic growth.

lecture enhancer 2-2

TRACKING THE UNDERGROUND ECONOMY

A peculiar statistic has been puzzling economists ever since the economy began its recovery. Retail sales have climbed steadily over the last four years despite the fact that gains in reported income have stalled. So if people still aren't getting paid more, where is this disposable cash flow coming from? According to some, one need not look further than the underground economy.

Then again, the sum total of unreported U.S. income isn't a thing you can easily track on a graph. All untaxed cash transactions are considered part of the underground economy, including everything from drug deals to yard sales. Although a definite amount is impossible to determine, most economists value America's shadow economy at $2 trillion annually. That accounts for as much as 19 percent of total income, resulting in a yearly tax gap that tops out at $500 billion. Experts fear that disparity will only grow larger as more and more people become dependent on under-the-table transactions to supplement their earnings.

Kevin Kalmes, for instance, was out of work for two years when she received a foreclosure notice on her home. She began to sell items from her basement to raise cash and eventually made enough money to save the house. Rather than shutter her ad-hoc second-hand shop, though, Kalmes kept her rummage sale going full-time without permits. Kalmes' story represents just one among thousands in which people had to devise their own ways to make money legally in this still shaky economy. Over the long-term experts hope that the current stimulus driven by untaxed cash and enjoyed by retailers will lead to job creation. Ideally, that would mean fewer people would have to toil in the shadow economy in order to make their living. Still, there's a chance that companies could remain reluctant to hire, driving even more people to seek out cash through tax-free means. If this turns out to be the case, then the U.S. government may stand to lose an increasing share of vital tax revenue.

lecture enhancer 2-3

THE CIRCULAR FLOW MODEL

(**PPT 2-XX** presents this simplified Circular Flow Model.)
Economists often use *models* to explain economic principles. A model is like a map of a concept. A *road map* shows you the major highways and waterways, not every tree. An *economic model* presents an economic concept as a bare-bones “map,” containing only the major elements. Thus, a model does not contain all the detail and complexity of the concept, just the simplified major elements.

One such economic model is the Circular Flow Model, a simplified presentation of the basic transactions in a free-market economy. The two major elements are **consumers** (presented in the model as *households*) and the **businesses** that create goods and services.

Each of the factors of production mentioned in the text has a price. To use *land*, a business must make rent or mortgage payments (simplified as *rent*). *Labor* must be paid salary or *wages*. The buildings, equipment, production lines, and so on (*capital*) are financed by paying *interest*. Finally, the entrepreneur expects to earn a *profit* from using his or her *entrepreneurship*. However, this resource payment is not guaranteed. If costs exceed income, the business may suffer a *loss*. (Some newer versions of this model include *knowledge* as a factor of production; older versions usually don’t.)

Businesses demand resources in order to produce products and services. In a capitalist economy, the households own the factors of production and must be compensated. This income flows back into the households. The prices of resources are set by the interaction of supply and demand.

The goods and services that households demand are created by business. The consumers in these households use the income from their factors of production to purchase goods and services.

Thus, business activity flows in a circle, which is illustrated by the Circular Flow Model. The market for resources (top arrows) is known as the *resource market*. The bottom flow is referred to as the *product market.*

This is a simplified model of pure capitalism, and it ignores a major player—government. Purchases of goods and services by all levels of government amount to about 20% of the nation’s gross domestic product. More sophisticated models include the government’s role in diverting resource payments as taxes and spending on government programs, which creates a more realistic representation of a mixed economy.

lecture enhancer 2-4

HOW ACCURATE IS THE GDP?

In today's modern economy, statistics are supreme. GDP, unemployment and interest rates all play dominant roles in the allocation of the government's budget. No spending bill can hope to pass into law without a battery of statistics and figures charting how such legislation will benefit the country. But just how accurately do those numbers reflect the world we live in?

Take GDP, for instance. The famous figure has only been reliably collected in the U.S. since the 1930s and didn't become the primary indicator of the nation's economic health until 1991. Yet despite such a short history, economists and legislators treat GDPs of any stripe with devotion. For instance, global financial markets recently went into uproar when China reported its GDP at 7.7 percent rather than the expected 8 percent. That missing 0.3 percent may seem negligible, but it was enough to ruffle the feathers of analysts across the world who now had to readjust their projections. But if the accuracy of the U.S.'s GDP is merely suspect, China's is outright unreliable. Only gathered for less than 20 years, the Chinese GDP fails to account for many key factors, such as the political pressure of its five-year plans or the enormous private loan industry.

Other figures present similar problems. In trade stat terms, every time an iPhone leaves a Chinese factory and lands on American shores, $200 is added to our trade deficit with China. In reality, though, the components of that same iPhone have been produced all over the world, not just China. A more accurate figure would take all those other manufacturers into account and ascribe value accordingly. Instead, current guidelines grant sole credit to the country where the product is "assembled." Ultimately, statistical hiccups like this demonstrate just how much the world has changed since these figures became prominent. Decades ago, it was safe to assume that a product was fully assembled in one place. That is simply not the case today as complex supply chains send items crisscrossing around the world. So while statistics like these no doubt provide relevant information, the conclusions they reach are perhaps not so concrete as to justify basing entire economies around their slight shifts in value.

lecture enhancer 2-5

OTHER ECONOMIC INDICATORS

In addition to the key economic indicators mentioned in the text—CPI, GDP, unemployment rate—other indicators measure different segments of the economy. Below are some of the more important ones.

KEY ECONOMIC INDICATORS

Prime Interest Rate	Lowest interest rate that banks charge preferred borrowers on short-term loans
Housing Starts	Tracks how many new single-family homes or buildings were constructed during the month and can detect trends in the economy looking forward
Durable Goods Orders	New orders for goods that last more than three years
Balance of Trade	Total value of a country's exports minus the total value of its imports, over a specific period of time
Inflation Rate	Percentage increase in prices of goods or services over a period of time
Consumer Confidence Index	Measures the degree of consumer confidence in the economy, and can indicate an upcoming increase or decrease in economic activity

THE "BEIGE BOOK"

Many economists use the Federal Reserve Board "Beige Book" to detect trends in the economy. The correct name for the report is "Summary of Commentary on Current Economic Conditions by Federal Reserve District." Each Federal Reserve Bank gathers information on current economic conditions in its district. The Beige Book summarizes this information by district and sector and is a gauge on the strength of the economy.

TIMING OF THE INDICATORS

Economic indicators can further be classified by the timing of the indicator.

Some indicators are **lagging**, meaning that they don't change direction until a few quarters *after* the economy does. An example is the unemployment rate. Unemployment tends to increase for two or three quarters after the economy starts to improve.

Coincident indicators move *at the same time* as the economy does. The gross domestic product measures the economy's output as it occurs.

Leading economic indicators are indicators that change *before* the economy changes. Stock market returns are a leading indicator, as the stock market usually begins to fall before the economy declines and they improve before the economy begins to pull out of a recession. Housing starts and the consumer confidence index are other leading economic indicators.

lecture enhancer 2-6

RESTAURANTS SERVE UP JOBS ACROSS THE COUNTRY

The U.S. economy has managed to add thousands of jobs so far this year thanks to big gains in industries like construction and health care. But even these substantial sectors can't compare to the robust growth of the restaurant industry, which has gained nearly 200,000 new jobs in 2017 alone. And unlike manufacturing or construction work, these jobs aren't localized to a few lucky cities scattered across the nation. Instead, nearly every American metropolis has seen a boom in restaurant positions in recent years.

In Cleveland, restaurants are responsible for more than a third of all new jobs added since 2015. That figure is the same in New Orleans and goes back all the way to 2010. In fact, this trend has been gaining steam for years in culinary-centric cities like San Francisco, Nashville and the Texas capitol of Austin, which leads the nation in percent-growth of restaurant jobs. Smaller metro areas like Little Rock and the military hub of Virginia Beach have enjoyed this expansion of eateries as well. Experts see the nationwide restaurant boom as a consequence of America's three-decade long shift from a manufacturing to a service-based economy. By 2020, restaurants will employ more people than factories.

The country's changing eating habits have also fueled this food service surge. In the 1950s only 25 percent of the average American's food budget went towards eating in restaurants. Today, people spend 50 percent of their budgets on dining out. This has provided an unprecedented boost for the restaurant industry, which has seen four of its five best years for growth occur since 2011. Although this is undoubtedly good news for business owners, some analysts worry that workers won't see many benefits from the boom. After all, a typical restaurant employee earns $12.50 per hour while private sector workers bring in an average of $22 an hour. So even though restaurants can provide plenty of work, there's no guarantee that those jobs will be able to provide a steady living for low-level employees.

lecture enhancer 2-7

WHAT IS A DEPRESSION?

Last decade, with the stock market falling, banks failing, and unemployment soaring, many people wondered if the U.S. economy was suffering not from a recession, but from a much worse condition, a depression. Economists say that a depression is, well, nobody really has a formal description for a depression. A depression is when things are really, really bad.

While recessions are easy to define, there are no firm rules for what makes a depression. Everyone at least seems to agree there hasn't been one since the epic hardship of the 1930s. According to economist Peter Morici, a business professor at the University of Maryland, you'll know you've been in a recession when you see it behind you. "It's not going to be acknowledged until years go by."

No one disputes the definition of a recession, and the Great Recession surely qualified. Recessions have two handy definitions—two straight quarters of economic contraction, or when the National Bureau of Economic Research makes the call.

Declaring a depression is much trickier.

- By one definition, it is a downturn of three years or more with a 10% drop in economic output and unemployment above 10%.
- Another definition says a depression is a sustained recession during which the populace has to dispose of tangible assets to pay for everyday living.
- Morici says a depression is a recession that "does not self-correct" because of fundamental structural problems in the economy, such as broken banks or a huge trade deficit.
- Or maybe a depression is whatever corporate America says it is.

The Great Depression still maintains top ranking. Unemployment peaked at more than 25%. From 1929 to 1933, the economy shrank 27%. The stock market lost 90% of its value from boom to bust. The Great Recession came nowhere near those figures. And government policy makers argue that safeguards in place today weren't there in the 1930s: deposit insurance, unemployment insurance, and an ability by government to hurl trillions of dollars at the problem.

Before the 1930s, any serious economic downturn was called a depression or a *panic*. The term *recession* didn’t come into common use until *depression* became burdened by memories of the 1930s. When the economy collapsed again in 1937, people didn’t want to call that a new depression, and that’s when the term *recession* was first used. According to Millsaps College professor Robert McElvaine, “People also use ‘downward blip.’ Former Fed Chairman, Alan Greenspan, once called it a ‘sideways waffle’.”

CRITICAL THINKING EXERCISES

critical thinking exercise 2-1

KNOW YOUR HISTORY OF ECONOMICS

Go online and look up the following economists: Adam Smith, Jeremy Bentham, David Ricardo, and T. R. Malthus. Choose one of these economists and answer the following questions that describe their contributions to the field of economics.

1. Describe the personality of your chosen economist.

2. What major contributions did this chosen economist contribute to the field of economics regarding:

    a. Microeconomics

    b. Macroeconomics

3. How does the works of your chosen economist have any relevance to our economy today?

4. How did your chosen economist further the field of economic study?

critical thinking exercise 2-2

FINDING THE EQUILIBRIUM POINT

In 2018, Epic Electronics sold 350,000 digital video recorders (DVRs). Based on the company's analysis of the DVR market, the company believed that $160 was the equilibrium price based on the following supply and demand schedules.

2018 Price	Amount Supplied	Amount Demanded
$120	290,000	390,000
140	320,000	370,000
160	350,000	350,000
180	380,000	330,000
200	410,000	310,000
220	440,000	290,000

As the price of gas rises, consumers start driving less and going out less frequently for entertainment. With more people staying at home, DVR usages increased. In 2019 Epic's executives revised their estimate of the amount of product demanded. At each of the above price points, it estimates that consumers will purchase (demand) 50,000 more DVRs. For instance, at $140, now 420,000 DVRs will be sold. The price–amount supplied relationship remains the same.

1. Describe what has happened to the supply and demand curves for Epic Electronics' DVRs in 2018.

2. What is the new equilibrium price?

3. How many DVRs will be produced at the new equilibrium price?

4. Epic Electronics revised its estimate of the amount of product demanded for 2019 as described above. In 2020 a new technology became available enabling DVRs to fully partner with smartphones. Users can access any and all of their recorded programming from their wireless devices. Epic's competitors are selling this new DVR, called SuperDVR, for $150. What will happen to the supply and demand curves for Epic's DVRs now?

notes on critical thinking exercise 2-2

1. ***Describe what has happened to the supply and demand curves for Epic Electronics' DVRs in 2018.***
Supply remained unchanged. Demand shifted right, showing the increased quantity demanded at every price.

2. ***What is the new equilibrium price?***
The quantity demanded and quantity supplied are now identical at $180, a higher price. At that price the quantity supplied remains stable at 380,000. However, the quantity demanded at that price is increased by 50,000 to 380,000. The equilibrium price will now be $180.

2018 Price	Amount Supplied	Amount Demanded
$120	290,000	440,000
140	320,000	420,000
160	350,000	400,000
180	***380,000***	***380,000***
200	410,000	360,000
220	440,000	350,000

3. ***How many DVRs will be produced at the new equilibrium price?***
At $180, 380,000 DVRs will be produced.

4. ***Epic Electronics revised its estimate of the amount of product demanded for 2019 as described above. In 2020 a new technology became available enabling DVRs to fully partner with smartphones. Users can access any and all of their recorded programming from their wireless devices. Epic's competitors are selling this new DVR, called SuperDVR, for $150. What will happen to the supply and demand curves for Epic's DVRs now?***

With a more advanced DVR available from competitors, demand for Knight DVRs will decrease at the same price. The demand curve shifts to the left, and the equilibrium price falls.

critical thinking exercise 2-3

STANDARD OF LIVING COMPARISION

Is the standard of living different in capitalist, socialist, and communist economies? Which economic system provides the highest standard of living? One way of answering these questions is by comparing economic data you might find in the library or on the Internet. (*Hint:* Try the CIA World Factbook page.) Choose one capitalist country, one socialist country, and one communist country. Use the following chart to record your findings.

	CAPITALIST COUNTRY	SOCIALIST COUNTRY	COMMUNIST COUNTRY
Country Chosen			
Gross Domestic Product			
Consumer Prices			
Unemployment Rate			
Average Income			
Average Education			

BONUS CASES

bonus case 2-1

SMARTPHONES SWEEP THE NATION OF MYANMAR

Much focus is usually centered on China when it comes to technological developments in business. But China is far from the only Asian nation to undergo drastic changes thanks to the rise of smartphones. From India to Indonesia, mobile technology has altered the ways that both consumers and businesspeople go about their lives. Still, perhaps no other place on the continent has been as fundamentally changed by smartphones as the country of Myanmar.

Up until six years ago, the citizens of this Texas-sized nation suffered under the brutal rule of a military dictatorship. The government imposed strict economic isolation and kept tight control over markets. As the country emerged from this decades-long ordeal, smartphones were beginning to catch on with millions of consumers across Asia. In Myanmar, though, only a wealthy elite could afford mobile devices. For instance, a SIM card for a cellphone cost as much as $2,000 on the black market. As a result, Myanmar had fewer mobile phones than any other country besides North Korea.

Then in 2013 the government finally ended the state's monopoly over the telecommunications industry. Although the door was now open for outside investors, officials required that any potential providers had to create networks that could cover the entire country, not just cities. By 2014 three telecommunications companies had invested billions to construct cellular towers all across Myanmar. Today, more than 90 percent of the nation's 54 million people have access to a mobile device. SIM cards now cost $1.50 rather than $2,000. Plus, people can purchase a smartphone for less than $20 and make domestic calls for about 2 cents per minute. This amazing transformation has had a major effect on a country where only 5 percent of citizens have a bank account. New apps like the domestically produced Wave Money allow people to manage their finances online rather than depend largely on cash. Only time will tell how other Myanmar-made apps and technological services will alter the nation.

discussion questions for bonus case 2-1

1. How did free enterprise change Myanmar's economy after years of strict government control?
2. Do you think the rise of mobile phones in Myanmar will cause more citizens to get bank accounts?

notes on discussion questions for bonus case 2-1

1. ***How did free enterprise change Myanmar's economy after years of strict government control?***
   Under strict government control, the only way a person could obtain a mobile device or SIM card would be on the black market. This was far too costly for the average citizen. By 2014, three telecommunications companies invested billions in Myanmar. Now, more than 90% of the nation have access to mobile devices at affordable prices.

2. ***Do you think the rise of mobile phones in Myanmar will cause more citizens to get bank accounts?***
   Answers will vary.

bonus case 2-2

FOUNDATIONS OF THE CAPITALIST SYSTEM

Throughout the history of capitalism there has been one persistent criticism: The whole system seems to be based on selfishness—the more one works, the more one prospers. If a person is unable to work, the system seems to have no answer to his or her problems. Furthermore, there does not seem to be any moral or spiritual foundation to the system. Where do businesses get their values? What about concepts such as sharing, helping neighbors, and protecting the environment?

It is important to make a distinction between plain capitalism and democratic capitalism. Democratic capitalism is a system based on three components: (1) free enterprise—that is, freedom to own your own businesses and farms and freedom to keep the profits; (2) a freely elected government that has internal checks and balances; and (3) moral, ethical, and spiritual values that are part of the very fabric of the country and the business system. Plain capitalism is a system where there is free enterprise, but no freely elected government and no foundation of moral, ethical, and spiritual values. There are several "capitalist" countries headed by right-wing dictators that do not have democratic capitalism and do not have the relative prosperity and social justice that we have in the United States.

Let's explore democratic capitalism in more detail so that you can understand how the system works. One of the most important elements of democratic capitalism is its moral and spiritual base. When the United States was being settled, there was so much religious debate and rivalry among religions that people were tortured and killed for their beliefs. When it came time to establish a free and separate United States, however, the founding fathers were adamant about freedom of religion. They were very religious people themselves.

Thomas Jefferson was proud of his religious heritage and his fight for religious freedom in the United States He asked that his epitaph read: "Author of the Declaration of Independence, of the Statute of Virginia for Religious Freedom, and Father of the University of Virginia." Jefferson felt that freedom of religion was one of his most important contributions. He felt it was as important as being president of the United States.

Democratic capitalism cannot work effectively and fairly without all three components. With all three, the democratic capitalist system can become the fairest and most equitable economic system in the world. Not everyone agrees on the role of government in the democratic system and on how much of the total gross national product the government should control. (Recent history indicates that somewhere between 20% and 25% of GDP gives the government the funds it needs to create more social justice and more equitable distribution of wealth.) A freely elected government is important to democratic capitalism because if the people feel that the system is not fair, they can elect new politicians to change the rules.

discussion questions for bonus case 2-2

1. Do you see any evidence that the moral, ethical, and spiritual foundation of the American democratic capitalist system is eroding? How does that affect the ability of capitalist proponents to promote capitalism in other countries such as China and India?

2. Why is it so necessary to have a freely elected government for democratic capitalism to create a prosperous and fair economy?

3. Go through the three components of democratic capitalism and picture an economy without each one. What happens to freedom, fairness, and moral and ethical behavior? Which part of the system seems weakest today? What can be done about it?

notes on discussion questions for bonus case 2-2

1. ***Do you see any evidence that the moral, ethical, and spiritual foundation of the American democratic capitalist system is eroding? How does that affect the ability of capitalist proponents to promote capitalism in other countries such as China and India?***
   When one of the authors was in elementary school, the codes of what was moral forbid him to see *The Moon Is Blue* because the movie used the word *virgin* in it. Now movies include more adult language and more violence and sexual content. In fact, many such movies are now available in prime time on TV. There does seem to be an erosion of moral and ethical behavior in business, witness the Merck, Enron, WorldCom, Tyco, and Martha Stewart scandals. It could be a function of more media reporting of such behavior, but the impression is clear—moral decay is spreading.
   When other countries see moral decay in capitalist countries, they are hesitant to adopt capitalism. They do not want the immorality, the crime, and the music that they see as corrupting of the spiritual values of their countries.

2. ***Why is it so necessary to have a freely elected government for democratic capitalism to create a prosperous and fair economy?***
   Because any kind of dictatorship hinders the operation of free markets, or at least tends to do so. Free choice in the market is based on a value system that includes free choice in it, including free choice of leaders.

3. ***Go through the three components of democratic capitalism and picture an economy without each one. What happens to freedom, fairness, and moral and ethical behavior? Which part of the system seems weakest today? What can be done about it?***
   Without free enterprise, shortages develop and the whole economy tends to slow. Poverty, hunger and starvation often result. Without a freely elected government, the arbitrary allocation of resources can lead to the same problems as an absence of free markets. But what is needed in any economy is a moral and ethical base. Without that base, the market mechanism falters.

CONNECT INSTRUCTOR'S MANUAL

Helpful Suggestions Regarding Assignment Policies: Connect gives instructors a wide array of flexibility in making assignments and creating grading policies. Instructors may choose to:

- assign as many assignments as he/she deems appropriate
- determine point values for each question/exercise individually
- make available multiple attempts per assignment with options of accepting the highest score or averaging all the attempts together
- deduct points for late submissions of assignments (percentage deduction per hour/day/week/etc.) or create hard deadlines
- show feedback on exercises/questions immediately or at the time of his/her preference
- create new assignments or questions from scratch, such as web-linked assignments, LearnSmart study modules, writing assignments, blog assignments, discussion board assignments, or upload questions from a pool

Recommendations: Here are some recommendations you might want to consider if you are using Connect for the first time.

- Assigning Application Exercises: consider assigning only 1 or 2 exercises per chapter.
- Assigning LearnSmart: You might also want to assign less than an entire chapter segment of LearnSmart in Connect. The system allows you to do this by dragging the toggle lever left or right to increase or decrease the time of the activity. You can also reduce the time based on which learning objectives you select and deselect for the chapter.
- The entire LearnSmart module is available to your student at all times; however, assigning 30 minutes or so will prompt students to try it. You are required to select a due date for LearnSmart. However, this will not prevent the student from LearnSmart access; it is designed to show you that the student has taken the LearnSmart assignment. LearnSmart is an adaptive study tool designed for students. It can also show you where students are struggling to understand specific concepts.
- The student's LearnSmart score in the Connect reports is based on their mastery of the material at the time the assignment is due. Mastery is an evaluation of the number of learning objectives they completed via performance on answering questions.
- Students may, and are encouraged, to continue to use LearnSmart throughout the semester. After the assignment due date, they can continue to access LearnSmart. Continued use of LearnSmart will not affect their LearnSmart assignment results in the Connect reports, but has shown to improve test scores by as much as a full letter grade.

Time-Saving Hints:

- Instructors may want to give students unlimited or multiple attempts on the first few assignments so the students have a chance to learn and navigate the system before selecting the option for one attempt only.
- The value of each question should probably be relatively low, since multiple questions are usually assigned for each chapter. A good rule of thumb would be to make “Quiz Questions” worth 1 point each and “exercises” worth 5–10 points each since these require more time and thought.
- Feedback given to students is time flexible. Selecting feedback to be displayed after the assignment due date helps to limit students from giving the correct answers to other students while the exercise is still available.

Connect: Chapter 2 – Table of Contents

Application Exercises:

Free-Market Competition	Click and Drag
Key Economic Indicators	Click and Drag
Supply and Demand	Click and Drag
Opportunity International	Video Case
Economic Systems	iSeeit! Video Case
Supply and Demand	iSeeit! Video Case

Language Toolkit:

Language Toolkit 02a	Click and Drag
Language Toolkit 02b	Click and Drag
Language Toolkit 02c	Click and Drag

Chapter Learning Goals:

Learning Goal 02-01: Explain basic economics.
Learning Goal 02-02: Explain what capitalism is and how free markets work.
Learning Goal 02-03: Compare socialism and communism.
Learning Goal 02-04: Analyze the trend toward mixed economies.
Learning Goal 02-05: Describe the economic system of the United States, including the significance of key economic indicators (especially GDP), productivity, and the business cycle.
Learning Goal 02-06: Contrast fiscal policy and monetary policy, and explain how each affects the economy.

Free-Market Competition

Activity Summary: This activity involves terms and concepts related to capitalism and the free-market system. Students will be presented with descriptions of various industries, and they must determine whether to place the industry in the category of perfect competition, monopolistic competition, oligopolistic competition, or monopoly. Topics include free-market system, capitalism, competition in capitalism, and government regulation.

Concept Review (Learning Goals, Difficulty, Blooms, and AACSB)

Learning Goals:

<u>Learning Goal 02-02</u>: Explain what capitalism is and how free markets work.

Difficulty Level: 3 = Hard

Blooms: Understand

AACSB: Knowledge Application

Follow-Up Activity: Instructors could discuss the causes of the competitive pressures each industry faces, such as high entry barriers, high levels of competitive rivalry, the bargaining power of supplies and buyers inside that industry, and government regulatory presence. Students could be asked to create a larger list of individual companies that fall into one of the four main categories: perfect competition, monopolistic competition, oligopolistic competition, and monopoly. Instructors could also engage students in a debate or assignment involving how the free-market system differs from socialism and communism. Students could be asked to write their opinions of why each system has advantages and disadvantages.

Key Economic Indicators

Activity Summary: This activity involves terms and concepts related to the three key economic indicators used in the United States: GDP, unemployment rates (seasonal, structural, frictional, and cyclical), and price indices (Consumer Price Index and Producer Price Index). Students are presented with an individual's life situation, and then must determine to which category this situation relates. Topics include GDP, unemployment rates (seasonal, structural, frictional, and cyclical), price indices (Consumer Price Index and Producer Price Index), and inflation.

Concept Review (Learning Goals, Difficulty, Blooms, and AACSB)

Learning Goals:

Learning Goal 02-05: Describe the economic system of the United States, including the significance of key economic indicators (especially GDP), productivity, and the business cycle.
Difficulty: 3 = Hard
Blooms: Understand
AACSB: Knowledge Application

Follow-Up Activity: Instructors could ask students to find the GDPs and unemployment rates of various countries, and then categorize or rank this information based on the economic system that each country most adheres to (capitalism, socialism, or communism). By analyzing this small data sample, students would begin to form an understanding of the advantages and disadvantages of each economic system. Students could also describe the types of unemployment (seasonal, structural, frictional, and cyclical) in order to understand why each one happens. This would bring to light changes in the business cycle and trends in the general environment of a business.

Supply and Demand

Activity Summary: This activity involves creating a supply and demand graph by labeling the axis, lines, and intersection points. Students will be given definitions of key vocabulary words and then will be asked to drag and drop each word to its appropriate place on the graph. Topics include supply, demand, supply curve, demand curve, equilibrium point, price, and quantity axis.

Concept Review (Learning Goals, Difficulty, Blooms, and AACSB)
Learning Goals:
Learning Goal 02-01: Explain basic economics.
Difficulty: 2 = Medium
Blooms: Understand
AACSB: Analytical Thinking

Follow-Up Activity: Instructors could ask the students to determine what causes an upward or downward shift in supply and demand. Students could also analyze the price of several familiar products to understand why the price has changed in the past few years. Instructors could have students list other scenarios that alter pure capitalism negotiations that exist in a mixed economy or a socialism economy (embargoes, taxes, tariffs, etc.).

Opportunity International

Activity Summary: This video case features the micro-lending organization Opportunity International. This organization provides small loans for individuals who want to start a business in developing countries. It highlights the Invisible Hand Theory, and it describes how the ideas of Adam Smith are confirmed when an economy increases as a result of individuals being free to economically prosper. The video pauses periodically to ask the student questions throughout the activity. Topics include capitalism, socialism, communism, Adam Smith, Invisible Hand Theory, entrepreneurship, lending, risk, capital, and factors of production.

Concept Review (Learning Goals, Difficulty, Blooms, and AACSB)

Learning Goals:
Learning Goal 02-01: Explain basic economics.
Learning Goal 02-02: Explain what capitalism is and how free markets work.
Difficulty: 2 = Medium
Blooms: Remember
AACSB: Knowledge Application

Follow-Up Activity: Instructors could have students research other micro-lending organizations, and then ask students to list the various business ventures that have been created with these small financial loans. Students could also be asked to describe different ways that a person could obtain money to start businesses outside of the micro-lending realm. This would lead to a conversation about capitalism versus socialism and communism.

Economic Systems

Activity Summary: This iSeeit! short video describes how one’s economic life would be under the three major economic systems of the world: capitalism, socialism, and communism.

Concept Review (Learning Goals, Difficulty, Blooms, and AACSB)

Learning Goals:
Learning Goal 02-02: Explain what capitalism is and how free markets work.
Learning Goal 02-03: Compare socialism and communism.
Learning Goal 02-06: Contrast fiscal policy and monetary policy, and explain how each affects the economy.

Difficulty: 1= Easy
Blooms: Understand
AACSB: Reflective Thinking

Follow-Up Activity: These short videos are designed to help students understand specific terms and concepts that are often key to understanding the overarching subject. Instructors could use these short videos as quick ways to launch into the subject matter at the beginning of a chapter or unit.

Supply and Demand

Activity Summary: This iSeeit! short video describes the concept of supply and demand in a capitalistic economy by using the example of jeans.

Concept Review (Learning Goals, Difficulty, Blooms, and AACSB)
Learning Goals:
Learning Goal 02-01: Explain basic economics.
Learning Goal 02-02: Explain what capitalism is and how free markets work.
Learning Goal 02-03: Compare socialism and communism.
Difficulty: 1 = Easy
Blooms: Understand
AACSB: Reflective Thinking

Follow-Up Activity: These short videos are designed to help students understand specific terms and concepts that are often key to understanding the overarching subject. Instructors could use these short videos as quick ways to launch into the subject matter at the beginning of a chapter or unit.

Language Toolkit 02a

Activity Summary: This is a vocabulary matching assignment. Students are asked to correctly match a list of selected key terms from the chapter to their appropriate definitions.

Concept Review (Learning Goals, Difficulty, Blooms, and AACSB)

Learning Goals:

Learning Goal 02-01: Explain basic economics.

Learning Goal 02-06: Contrast fiscal policy and monetary policy, and explain how each affects the economy.

Difficulty: 1 = Easy

Blooms: Understand

AACSB: Reflecting Thinking

Follow-Up Activity: Instructors could ask students to explain the definition of these terms in greater detail or explain how terms relate to a specific business.

Language Toolkit 02b

Activity Summary: This is a vocabulary matching assignment. Students are asked to correctly match a list of selected key terms from the chapter to their appropriate definitions.

Concept Review (Learning Goals, Difficulty, Blooms, and AACSB)

Learning Goals:

Learning Goal 02-01: Explain basic economics.

Learning Goal 02-06: Contrast fiscal policy and monetary policy, and explain how each affects the economy.

Difficulty: 1 = Easy

Blooms: Understand

AACSB: Reflecting Thinking

Follow-Up Activity: Instructors could ask students to explain the definition of these terms in greater detail or explain how terms relate to a specific business.

Language Toolkit 02c

Activity Summary: This is a vocabulary matching assignment. Students are asked to correctly match a list of selected key terms from the chapter to their appropriate definitions.

Concept Review (Learning Goals, Difficulty, Blooms, and AACSB)

Learning Goals:

Learning Goal 02-01: Explain basic economics.

Learning Goal 02-06: Contrast fiscal policy and monetary policy, and explain how each affects the economy.

Difficulty: 1 = Easy

Blooms: Understand

AACSB: Reflecting Thinking

Follow-Up Activity: Instructors could ask students to explain the definition of these terms in greater detail or explain how terms relate to a specific business.