Name - ____ Date - ___________________________

Honors Principals of Economics
Principles of Economics - Chapter 1 – Welcome to Economics

Please read Chapter 1 – Welcome to Economics - https://www.openstaxcollege.org/files/textbook_version/low_res_pdf/21/principles-of-economics-LR.pdf

Define the following terms –

circular flow diagram

command economy

division of labor

economics

economies of scale

exports

fiscal policy

goods

services

goods and services market

gross domestic product (GDP)

imports

labor market

macroeconomics

market economy

market
microeconomics

model

monetary policy

private enterprise

scarcity

specialization

theory

traditional economy

underground economy

Needs

Wants

Shortage

Scarcity

Allocation of Resources

Opportunity Cost and Tradeoffs

Production Possibilities curve

Marginal benefits

marginal costs

Incentives

Economic Systems

Globalization

Consumer Economics

Economics and Economists: The Basis for Controversy

Thomas R. Swartz and Frank J. Bonello

[The Introduction from the book T*aking Sides: Clashing Views on Controversial Economic Issues*, published by Dushkin/McGraw Hill, 1998]

Although more than 70 years have passed since Lord Keynes (1883-1946) penned these lines, many economists still struggle with the basic dilemma he outlined. The paradox rests in the fact that a free-market system is extremely efficient. It is purported to produce more at a lower cost than any other economic system. But in producing this wide array of low-cost goods and services, problems arise. These problems-most notably a lack of economic equity and economic stability - concern some economists.

If the problems raised and analyzed in this book were merely the product of intellectual gymnastics undertaken by egg-headed economists, we could sit back and enjoy these confrontations as theoretical exercises. The essays contained in this book, however, touch each and every one of us in tangible ways. Some focus upon macroeconomic topics, such as balancing the budget and the Federal Reserve's monetary policy. Another set of issues deals with microeconomic topics. We refer to these issues as micro problems not because they are small problems, but because they deal with small economic units, such as households, firms, or individual industries. A third set of issues deals with matters that do not fall neatly into the macroeconomic or microeconomic classifications. This set includes three issues relating to the international aspects of economic activity and two involving pollution.

The range of issues and disagreements raises a fundamental question: Why do economists disagree? One explanation is suggested by Lord Keynes's 1926 remark. How various economists will react to the strengths and weaknesses found in an economic system will depend upon how they view the relative importance of efficiency, equity, and stability. These are central terms, and we will define them in detail in the following pages. For now the important point is that some economists may view efficiency as overriding. In other cases, the same economists may be willing to sacrifice the efficiency generated by the market in order to ensure increased economic equity and/or increased economic stability.

Given the extent of conflict, controversy, and diversity, it may appear that economists rarely, if ever, agree on any economic issue. We would be most misleading if we left the reader with this impression. Economists rarely challenge the internal logic of the theoretical models that have been developed and articulated by their colleagues. Rather, they will challenge either the validity of the assumptions used in these models or the value of the ends these models seek to achieve. The challenges typically focus upon such issues as the assumption of functioning, competitive markets, and the desirability of perpetuating the existing distribution of income. In this case, those who support and those who challenge the operation of the market agree on a large number of issues. But they disagree most assuredly on a few issues that have dramatic implications.

This same phenomenon of agreeing more often than disagreeing is also true in the area of economic policy. In this area, where the public is most acutely aware of differences among economists, these differences are not generally over the kinds of changes that will be brought about by a particular policy. The differences more typically concern the timing of the change, the specific characteristics of the policy, and the size of the resulting effect or effects.

ECONOMISTS: WHAT DO THEY REPRESENT?

Newspaper, magazine, and TV commentators all use handy labels to describe certain members of the economics profession. What do the headlines mean when they refer to the Chicago School, the Keynesians, the institutional economists, or the radical economists? What do these individuals stand for? Since we too use our own labels throughout this book, we feel obliged to identify the principal groups or camps in our profession. Let us warn you that this can be a misleading venture. Some economists - perhaps most of them - defy classification. They drift from one camp to another, selecting a gem of wisdom here and another there. These are practical men and women who believe that no one camp has all the answers to all the economic problems confronting society.

Recognizing this limitation, four major groups of economists can be identified. These groups are differentiated on the basis of two basic criteria: how they view efficiency relative to equity and stability; and what significance they attach to imperfectly competitive market structures. Before describing various views on these criteria, it is essential to understand the meaning of certain terms to be used in this description.

Efficiency, equity, and stability represent goals for an economic system. An economy is efficient when it produces those goods and services that people want without wasting scarce resources. Equity in an economic sense has several dimensions. It means that income and wealth are distributed according to accepted principles of fairness, that those who are unable to care for themselves receive adequate care, and that mainstream economic activity is open to all persons. Stability is viewed as the absence of sharp ups and downs in business activity, in prices, and in employment. In other words, stability is marked by steady increases in output, little inflation, and low unemployment.

When the term market structures is used, it refers to the number of buyers and sellers in the market and the amount of control they exercise over price. At one extreme is a perfectly competitive market where there are so many buyers and sellers that no one has any ability to influence market price. One seller or buyer obviously could have great control over price. This extreme market structure, which we call pure monopoly, and other market structures that result in some control over price are grouped under the broad label of imperfectly competitive markets. With these terms in mind, we can begin to examine the various schools of economic thought.

Free-Market Economists

One of the most visible groups of economists and perhaps the easiest group to identify and classify is *the free-market economists*. These economists believe that the market, operating freely without interferences from government or labor unions, will generate the greatest amount of well-being for the greatest number of people.

Economic efficiency is one of the priorities for free-market economists. In their well-developed models, *consumer sovereignty* - consumer demand for goods and services - guides the system by directly influencing market prices. The distribution of economic resources caused by these market prices not only results in the production of an array of goods and services that are demanded by consumers, but this production is undertaken in the most cost-effective fashion. The free-market economists claim that, at any point, some individuals must earn incomes that are substantially greater than those of other individuals. They contend that these higher incomes are a reward for greater efficiency or productivity and that this reward-induced efficiency will result in rapid economic growth that will benefit all persons in the society. They might also admit that a system driven by these freely operating markets will be subject to occasional bouts of instability (slow growth, inflation, and unemployment). They maintain, however, that government action to eliminate or reduce this periodic instability will only make matters worse. Consequently, government, according to the free-market economist, should play a minor role in the economic affairs of society.

Although the models of free-market economists are dependent upon functioning, competitive markets, the lack of such markets in the real world does not seriously jeopardize their position. First, they assert that large-size firms are necessary to achieve low per-unit costs; that is, a single large firm may be able to produce a given level of output with fewer scarce resources than a large number of small firms. Second, they suggest that the benefits associated with the free operation of markets are so great compared to government intervention that even a second-best solution of imperfectly competitive markets still yields benefits far in excess of government intervention.

These advocates of the free market have been given various labels over time. The oldest and most persistent label is *classical economists*. This is because the classical economists of the eighteenth century, particularly Adam Smith, were the first to point out the virtues of the market. In *The Wealth of Nations* (1776), Smith captured the essence of the system with the following words:

Every individual endeavors to employ his capital so that its produce may be of greatest value. He generally neither intends to promote the public interest nor knows how much he is promoting it He intends only his own security, only his own gain. And he is in this led by an invisible hand to promote an end which was no part of his intention. By pursuing his own interest he frequently promotes that of society more effectively than when he really intends to promote it.

Liberal Economists

Another significant group of economists in the United States can be classified as *liberal economists*. Liberal here refers to the willingness to intervene in the free operation of the market. These economists share with the free-market economists a great respect for the market, the liberal economist, however, does not believe that the explicit and implicit costs of a freely operating market should or can be ignored. Rather, the liberal maintains that the costs of an uncontrolled marketplace are often borne by those in society who are least capable of bearing them: the poor, the elderly, and the infirm. Additionally, liberal economists maintain that the freely operating market sometimes results in economic instability and the resultant bouts of inflation, unemployment, and slow or negative growth.

Consider for a moment the differences between free-market economists and liberal economists at the microeconomic level. Liberal economists take exception to the free market on two grounds. First, these economists find a basic problem with fairness in the marketplace. Since the market is driven by the forces of consumer spending, there are those who through no fault of their own (they may be aged, young, infirm, or physically or mentally handicapped) may not have the wherewithal to participate in the economic system. Second, the unfettered marketplace does not and cannot handle spillover effects or what are known as externalities. These are the third-party effects that may occur as a result of some action. Will a firm willingly compensate its neighbors for the pollutants it pours into the nearby lake? Will a truck driver willingly drive at the speed limit and in the process reduce the highway accident rate? Liberal economists think not. These economists are therefore willing to have the government intervene in these and other, similar cases.

The liberal economists' role in macroeconomics is more readily apparent. Ever since the failure of free-market economics during the Great Depression of the 1930s, Keynesianism (still another label for liberal economics) has become widely known. In his 1935 book, *The General Theory of Employment, Interest, and Money*, Lord John Maynard Keynes laid the basic groundwork for this school of thought. Keynes argued that the history of freely operating market economies was marked by periods of recurring recessions, sometimes very deep recessions, which we call depressions. He maintained that government intervention through its fiscal policy - government tax and spending power - could eliminate, or at least soften these sharp reductions in economic activity and as a result move the economy along a more stable growth path. Thus for the Keynesians, or liberal economists, one of the extremely objectionable aspects of a free-market economy is its inherent instability.

Liberal economists are also far more concerned about the existence of imperfections in the marketplace than are their free-market counterparts. They reject the notion that imperfect competition is an acceptable substitute for competitive markets. They may agree that the imperfectly competitive firms can achieve some savings because of their large size and efficiency, but they assert that since there is little or no competition the firms are not forced to pass these cost savings on to consumers. Thus liberal economists, who in some circles are labeled antitrusters, are willing to intervene in the market in two ways: They are prepared to allow some monopolies, such as public utilities, to exist, but they contend that these must be regulated by government; or they maintain that there is no justification for monopolies, and they are prepared to invoke the powers of antitrust legislation to break up existing monopolies and/or prevent the formation of new ones.

Mainstream Critics and Radical Reform Economists

There are two other groups of economists we must identify. One group can be called *mainstream critics*. Included in this group are individuals like Thorstein Veblen (1857-1929), with his critique of conspicuous consumption, and John Kenneth Galbraith (b. 1908), with his views on industrial structure. One reasonably cohesive subgroup of mainstream critics are the post-Keynesians. They are post-Keynesians because they believe that as the principal economic institutions have changed over time, they have remained closer to the spirit of Keynes than have the liberal economists. As some have suggested, the key aspect of Keynes as far as the post-Keynesians are concerned is his assertion that "expectations of the future are not necessarily certain." On a more practical level post-Keynesians assert, among other things, that the productivity of the economic system is not significantly affected by changes in income distribution, that the system can still be efficient without competitive markets, that conventional fiscal policies cannot control inflation, and that "incomes policies" are the means to an effective and equitable answer to the inflationary dilemma. This characterization of post-Keynesianism is drawn from Alfred S. Eichner's introduction in *A Guide to Post-Keynesian Economics* (M. E. Sharpe, 1978).

The fourth and last group can be called the *radical reform economists*. Many in this group trace their ideas back to the nineteenth-century philosopher-economist Karl Marx and his most impressive work, the three volumes of *Das Kapital*. As with the other three groups of economists, there are subgroups of radical reform economists. One subgroup, which may be labeled contemporary Marxists, is best represented by those who have published their research results over the years in the *Review of Radical Political Economics*. These economists examine issues that have been largely ignored by mainstream economists, for example, war, sexism, racism, imperialism, and civil rights. In their analyses of these issues they borrow from and refine the work of Marx. In the process, they emphasize the role of class in shaping society and the role of the economy in determining class structures. Moreover, they see a need to encourage explicitly the development of some form of democratic socialism, for only then will the greatest good for the greatest number be ensured.

In concluding this section, we must warn you to use these labels with extreme care. Our categories are not hard and fast. There is much grayness around the edges and little that is black and white in these classifications. This does not mean, however, that they have no value. It is important to understand the philosophical background of the individual authors. This background does indeed color or shade their work.

SUMMARY

It is clear that there is no shortage of economic problems that demand solutions. At the same time there is no shortage of proposed solutions. In fact, the problem is often one of oversupply. The nineteen issues included in this volume will acquaint you or, more accurately, reacquaint you with some of these problems. And, of course, there are at least two proposed solutions for each of the problems. Here we hope to provide new insights regarding the alternatives available and the differences and similarities of these alternative remedies.

If this introduction has served its purpose, you will be able to identify common elements in the proposed solutions to the different problems. For example, you will be able to identify the reliance on the forces of the market advocated by free-market economists as the remedy for several economic ills. This introduction should also help you understand why there are at least two proposed solutions for every economic problem; each group of economists tends to interpret a problem from its own philosophical position and to advance a solution that is grounded in that philosophical framework.

Our intention, of course, is not to connect persons to one philosophic position or another. We hope instead to generate discussion and promote understanding. To do this, each of us must see not only a proposed solution, we must also be aware of the foundation that supports that solution. With greater understanding, meaningful progress in addressing economic problems can be achieved.

INTRODUCTION TO ECONOMICS HONORS
Hopatcong High School Summer Reading 2016 - 2017

The purpose of a course in Economics is to give students a thorough understanding of the principles of economics that apply to the functions of individual decision makers, both consumers and producers, within the economic system. It places primary emphasis on the nature and functions of product markets, and includes the study of factor markets and the role of government in promoting greater efficiency and equity in the economy.

ASSIGNMENTS

Students will be responsible for completing the following assignments over the summer. Pay attention to the due dates which can be found at the end of this document.

All assignments should be completed using GOOGLE DOCS and they should be shared with me at cderosa@hopatcongschools.org.

1.) Read Economics and Economists: The Basis for Controversy

 a. Read this introductory article before completing any of the other summer assignments.

2.) Read Issue I - Are Profits the Only Business of Business:

 a. Read the article with opposing viewpoints on the issue before completing the written assignment in the summer assignment description.

After you read the opposing viewpoints on the profits of business, complete the summary and analysis.

- Type a 1 paragraph brief summary of each of the opposing viewpoints of the issue.
- Type a 1-2 paragraph analysis stating the viewpoint you agree with – complete with explanation.
- Share this typed assignment with me (cderosa@hopatcongschools.org) with the document titled first initial.last name on google docs.

- **Due date: 1st Day Back to School - 6 September 2016**

3.) Article Summaries

 a. Follow the news on a weekly basis by reading economic articles online from any of the sources listed below. You should read at least 3 articles per week.

 The Economist
 The New York Times
 The Washington Post
 Newsweek
 Time

Bloomberg.com
Money
The Atlantic Monthly

There are additional newspaper links on my web page.

b. You should select one article per week and write a Weekly Article Analysis addressing the key economic concepts introduced in the articles. These should be completed in the following format:
   i. at least 1 page
   ii. 12 pt. font
   iii. Times New Roman
   iv. MLA style citation of article at the end of the paper

c. You are required to complete 8 total Article Analyses:
   i. 2 for June (Due July 5, 2016)
   ii. 4 for July (Due August 5, 2016)
   iii. 4 for August (Due by 6 September 2016)

Your textbook for Economics Honors is an on-line textbook. Principles of Economics is accesses as follows - https://openstax.org/details/principles-economics.

Please read Chapter 1 – Welcome to Economics and complete the attached vocabulary. Due Wednesday, 7 September 2016.