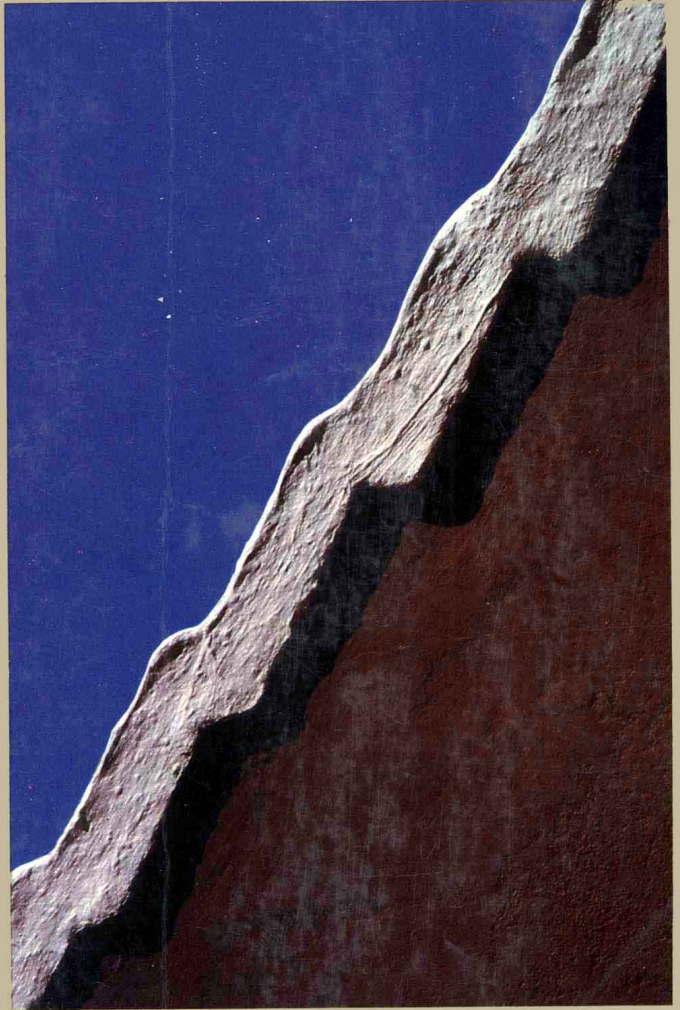


Second Edition



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Leftwich*

A Basic Framework for Economics



BUSINESS PUBLICATIONS, INC.
Plano, Texas 75075

1984 • Second edition

A BASIC FRAMEWORK FOR ECONOMICS

Cover photo by L. Dennis, The Image Bank.

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ISBN 0-256-03068-5

Library of Congress Catalog Card No. 83-71732

Printed in the United States of America

1 2 3 4 5 6 7 8 9 0 V 1 0 9 8 7 6 5 4

This textbook is accompanied by a Student Workbook/Study Guide, published by Business Publications, Inc. and available through your college bookstore. The Study Guide is designed to enhance your learning experience in this course by offering additional supplementary material and review questions for self-examination or extra credit work. If the bookstore does not have the Study Guide in stock, please ask your bookstore manager to order a copy for you.

Preface

The present revision contains a new chapter on international trade, adds applications of principles to real-world issues in each chapter, and is intended to provide improved exposition throughout the book. As before, the book streamlines, but does not water down, macroeconomics and microeconomics for beginning students, providing an alternative to the encyclopedic texts now on the market. The book has been developed from many years of teaching economic principles. I have consistently attempted to eliminate principles and materials that are unnecessary for a beginning student and to emphasize those basic to a student's understanding of the current economic world.

Since late 1980 it has been my privilege to do a number of short radio broadcasts and newspaper columns on a variety of economic topics of current interest. From these I have selected one for each chapter to help bring the world of theory and the real world closer together in the students' minds. Economic events have changed rapidly over the last several years, providing unique opportunities to illustrate the applications and uses of economic principles under various states of inflation, recession, and unemployment. The date at which each piece was broadcast is provided so that it can be considered in the context of the economic scene at that particular point in time.

There are several possible uses for the book. It can serve for the theory-oriented part of a two-semester or two-quarter sequence in which half the sequence is devoted to issues and the other half to theory. Or supplemented with issues-oriented textbooks, it can be used for the entire principles sequence. It should be useful for any separate one-semester principles course. It can also provide the requisite economic background for MBA students from other disciplines who have had no training in economics.

I am grateful to many who have contributed ideas and suggestions for improvements. These include Paula A. Smith, Oklahoma State University; Larry G. Cox, Southwest Missouri State University; Bruce N. Joseph, University of Central Florida; and Larry L. Sander, California State University–Sacramento. Ms. Gaye Trivitt provided her usual excellent secretarial service.

Richard H. Leftwich

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part
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*Introduction:
Starting from ground zero*

A BASIC FRAMEWORK FOR ECONOMICS

We start from scratch in Part 1. Although some students using this book have been exposed to basic economics before, others have not, and it is desirable that we all have a common foundation on which to build. In the first chapter, we review what the discipline of economics is about. In the second chapter, we review demand, supply, and price determination fundamentals. With this foundation securely in place, we construct the basic framework of economic analysis—macroeconomics in Part 2 and microeconomics in Part 3.

SCARCITY AND ECONOMIC ACTIVITY

Wants

Resources

Techniques

Production possibilities

So what is economic activity?

ECONOMIC SYSTEMS

The functions of an economic system

What to produce

Organization of production

Distribution of the product

Alternative economic systems

Private enterprise

Socialism

Mixed systems

A FRAMEWORK FOR ECONOMIC ANALYSIS

FROM THE MEDIA:

THERE AIN'T NO SUCH THING AS A FREE LUNCH

SUMMARY

CHECKLIST OF ECONOMIC CONCEPTS

Wants
Labor resources
Capital resources
Techniques
Production possibilities curve
Alternative costs
Economic activity
Economic system
Private enterprise system
Socialistic system
Private sector
Public sector
Macroeconomics
Microeconomics
Principles
Theories
Positive economics
Normative economics

**What is economics
about?**

The U.S. economy is in deep trouble. At least so it would appear to a casual reader of newspapers and news magazines or to one who listens to television news casts and candidates for political office. It has been plagued by inflation since 1967. Although the rate was down in 1983, the threat of an increase remains strong. The unemployment rate has been unacceptably high through the last half of the 1970s. Recession from 1981 to 1983 generated additional problems. Too many people are unable to attain "decent" living standards.

What is wrong? What are the forces causing the problems? Are they peculiar to, or a necessary part of, a capitalistic system? Would they be alleviated if the capitalistic system were supplanted by a socialistic system? Good answers to these questions are not easy to find. A great many people have answers, but they are not always good ones. Consistently good answers can result only from careful study and examination of the nature of economic activity and the processes through which it is carried on. The pages that follow are intended to help you consider these in a systematic way.

SCARCITY AND ECONOMIC ACTIVITY

The heart of economic analysis is that most of us want more goods and services than our incomes will let us have. Only a few at the very top income levels escape the problem. It extends beyond individuals; it occurs for any country as a whole; it exists throughout the entire world. Economic activity is triggered by unlimited human wants and scarcity of the means available for satisfying them.

Wants

The sum total of the wants of human beings is insatiable. Can you or any of your friends purchase enough of different goods and services to satiate yourselves with all of them simultaneously? Would you like a larger room or house? More or higher quality furnishings? Additional or more fashionable clothing? A newer car? Better food? Can you imagine an economy providing all of its inhabitants with such vast quantities of all goods and services that they could not possibly want more of anything?

Human wants arise from many sources. First, mere survival generates minimal demands for food and protection from the elements. But we human beings want more than mere survival.

We want increasing levels of comfort and security. We want variety. We want what our neighbors have. We want what our neighbors are likely to want. And the activity we engage in as we attempt to satisfy wants—for example, fulfilling the want for a university education—generates hosts of new wants. To look at the sources is enough to assure us that the possibility of fully satisfying all human wants is highly remote; unfulfilled wants hang out there in front of us and above us. Wants provide the mainspring of economic activity.

Resources

Limitations on the degree to which an economy can fulfill the wants of its inhabitants are partly determined by the resources available for producing want-satisfying goods and services. *Resources* are the ingredients that go into the production processes that turn out goods and services. For example, sand, gravel, cement, water, a hoe or a concrete mixer, and labor are resource inputs used to produce outputs of concrete. For clarity in thinking, we can classify the resources of an economy into two categories: (1) labor and (2) capital.

Labor resources consist of all efforts of mind and muscle available to be used in production processes. The surgeon who performs an appendectomy provides labor resources in a production process. So does the garbage collector who makes the morning rounds. The labor category includes a great many different occupations and skill levels. Some part of labor power results from the natural or inherited characteristics of human beings while the rest of it is made possible by education and training. The common denominator of the wide variety of labor resources available to an economy is that they are inseparable from the human beings who provide them.

Capital resources are the nonhuman ingredients that enter into production processes. Land areas, minerals, raw materials, wheat crops, semifinished materials like steel ingots, buildings, machines, tools, energy, and many other items constitute the capital category. Like labor resources, capital resources take many different forms.

The quantities of both labor and capital resources available for an economy to use during any given time period—say, one year—are *finite* or *scarce*. The labor force of an economy obviously cannot exceed its total population and will ordinarily amount to less than half of it. The proportion of the population