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MICROECONOMICS



96/97

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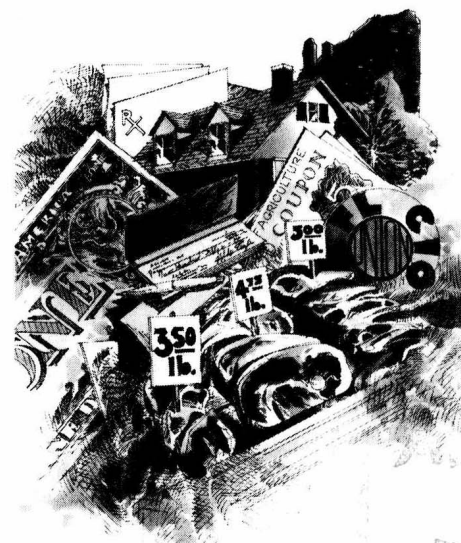
Editor

Don Cole
Drew University

Don Cole, Professor of Economics at Drew University, received his Ph.D. from Ohio State University. He has served as consultant to a variety of public and private organizations and is cofounder of the Drew University Semester on the European Union in Brussels, Belgium. An innovator in the use of computer-assisted instruction in the teaching of economics, Dr. Cole is the author of articles on various subjects, including economic policy, monetary theory, and economic education. He is also the editor of other Dushkin Publishing Group/Brown & Benchmark Publishers publications, including *The Encyclopedic Dictionary of Economics* and two other *Annual Editions* anthologies: *Economics* and *Macroeconomics*.

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Third Edition

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Don Cole
Drew University

Members of the Advisory Board are instrumental in the final selection of articles for each edition of Annual Editions. Their review of articles for content, level, currentness, and appropriateness provides critical direction to the editor and staff. We think you'll find their careful consideration well reflected in this volume.

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To the Reader

In publishing ANNUAL EDITIONS we recognize the enormous role played by the magazines, newspapers, and journals of the *public press* in providing current, first-rate educational information in a broad spectrum of interest areas. Within the articles, the best scientists, practitioners, researchers, and commentators draw issues into new perspective as accepted theories and viewpoints are called into account by new events, recent discoveries change old facts, and fresh debate breaks out over important controversies.

Many of the articles resulting from this enormous editorial effort are appropriate for students, researchers, and professionals seeking accurate, current material to help bridge the gap between principles and theories and the real world. These articles, however, become more useful for study when those of lasting value are carefully collected, organized, indexed, and reproduced in a low-cost format, which provides easy and permanent access when the material is needed. That is the role played by *Annual Editions*. Under the direction of each volume's Editor, who is an expert in the subject area, and with the guidance of an Advisory Board, we seek each year to provide in each ANNUAL EDITION a current, well-balanced, carefully selected collection of the best of the public press for your study and enjoyment. We think you'll find this volume useful, and we hope you'll take a moment to let us know what you think.

Annual Editions: Microeconomics 96/97 is an anthology that provides up-to-date readings in contemporary microeconomic issues. In view of the recent explosion of interest in economics, it is essential that students are given opportunities to observe how economic science can help them to understand major economic events in the real world. *Annual Editions: Microeconomics 96/97* is designed to meet such a need.

This anthology is divided into five sections, which generally correspond to the typical sequence of topics in microeconomics textbooks:

Introduction to Microeconomics. Microeconomics begins with a study of the way in which market values are established through the interaction of consumers (households) and producers (firms). As articles in this section indicate, estimating market values is a complex process.

Competition in Product Markets. A firm's decisions about price and output will depend upon the nature of the industry in which it is operating. Economists develop models that demonstrate how markets are structured between "perfect competition" (numerous small, price-taking firms) to "pure monopoly" (a single, price-making seller). As this section indicates, most "real world" markets lie somewhere between these two extremes, where many pressing issues (involving the competitive behavior of firms) can be found.

Labor Markets and Unions. This section discusses the ways in which labor markets work and the influence of unionization on them. Among the issues raised are: What explains the recent general decline in union membership? Does an increase in the federal minimum wage benefit labor? Is increased worker participation the key to improving American productivity?

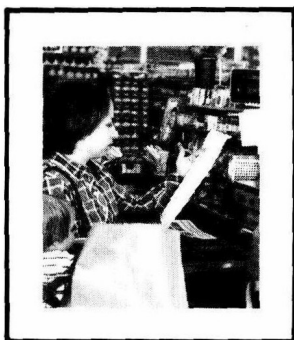
Market Failures and Public Microeconomics. Every market economy has certain shortcomings that might necessitate government action to modify its operation. This section deals with such questions as: Has the deregulation of industry gone too far, or not far enough? Should public services be contracted out to private firms? How might market forces be used to protect the environment?

Income Distribution and Economic Justice. Questions raised in this section include: What explains the rise in U.S. income inequality over the past decade? Why does poverty affect women more than men and children more than adults? Should federal welfare programs be reformed—or abandoned altogether—and at what cost?

Whether you are someone who is currently pursuing studies in economics, or just a casual reader eager to learn more about some of the major economic issues of the day, you will find *Annual Editions: Microeconomics 96/97* to be one of the most useful and up-to-date anthologies available. Your input can be valuable for the next edition. Please offer your opinions by filling out and returning to us the article rating form on the last page of this book.



Don Cole
Editor

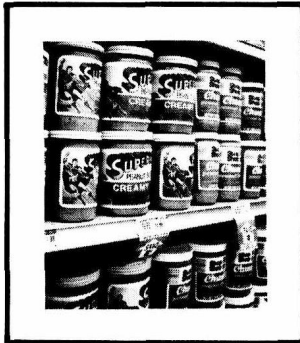


Unit 1

Introduction to Microeconomics

The nine articles in this section examine some of the common economic choices made by individuals and firms as they react to the dynamics of society.

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1. How Much for a Life? Try \$3 Million to \$5 Million , Peter Passell, <i>New York Times</i> , January 29, 1995.	6
A great deal of economic reasoning is based on the opportunity cost principle—the idea that any decision involving scarce resources must involve costs in terms of forgone alternatives elsewhere. Peter Passell applies this principle to an age-old question: What is the value of human life?	
2. “Does Prison Pay?” Revisited: Returning to the Crime Scene , Anne Morrison Piehl and John J. Dilulio Jr., <i>The Brookings Review</i> , Winter 1995.	9
Economists frequently employ cost-benefit analysis for the purpose of assessing the relative merits of public projects. Anne Morrison Piehl and John Dilulio conduct a study of New Jersey correctional institutions in order to determine whether they “cost too much” or “protect too little.”	
3. What’s All This about Pharmacoeconomics? Richard J. Willke, <i>Business Economics</i> , April 1995.	14
Health care resources are limited and must be allocated efficiently. The dollars that can be spent on health care, both public and private, cannot cover the full range of services that health care has to offer. Richard Willke shows how pharmacoeconomics , a relatively new and growing field, can be used to aid in the solution of these problems.	
4. Disneyland and the Old U.S.S.R.: Sharing Something in Common , Peter Passell, <i>New York Times</i> , April 27, 1995.	20
Peter Passell draws parallels between pricing in Disneyland and pricing in the former Soviet Union (as demonstrated by Disney’s successful ability to make people stand in line and like it). It is assumed that efficiency is not everything, that rationing with time instead of money allows people to avoid confronting the unwelcome realities of inequality and limited income.	
5. King Customer , <i>Business Week</i> , March 12, 1990.	22
This article maintains that business exists to serve customers , and it should bend over backward to satisfy their needs. Failure to understand this lesson may cost companies dearly in the 1990s.	
6. Corporate “Ownership,” Margaret M. Blair, <i>The Brookings Review</i> , Winter 1995.	26
In much of the media coverage about takeovers and boardroom shakeups, the unexamined assertion is made that corporations are “owned” by the individuals and institutions that hold the common stock of the companies. Margaret Blair asserts that corporate governance involves questions about the rights and prerogatives not only of shareholders, but of other participants in the firm as well.	
7. How the Marketplace Fosters Business Honesty , Dwight R. Lee and Richard B. McKenzie, <i>Business and Society Review</i> , Winter 1995.	30
Business is frequently perceived as being full of dishonest scoundrels who cheat, lie, and do worse things to increase their profits. The authors maintain that, if businesspeople act honestly, it is in part because they pay a high price for behaving dishonestly .	



Unit 2

Competition in Product Markets

The nine articles in this section discuss the concept of the market in the American economy. Some of the topics include competition, the effects of international markets on our economy, and corporate restructuring.

8. **Costing the Factory of the Future**, *The Economist*, March 3, 1990. 34

Factories run by numbers, which calculate **profits and losses**, analyze costs, and chart corporate strategies. *The Economist* shows why managers may be relying on numbers that are not appropriate for the competitive challenges of the 1990s.

9. **The Strange World of Business Forecasters**, Liz Roman Gallese, *World Monitor*, March 1991. 36

Sound business decisions require a steady flow of accurate, up-to-date **economic information**. Wrong decisions can convert millions of dollars in profits into losses. Liz Roman Gallese demonstrates the hazards of business decision making in a world in which, more often than not, economic data is seriously flawed.

Overview 40

10. **A Leap into Economic Change**, Steven Pearlstein, *Washington Post National Weekly Edition*, July 18-24, 1994. 42

During the first half of the 1990s, nearly all economic growth came from only three percent of all firms, the so-called **new corporate "gazelles."** Steven Pearlstein traces the sources of their success.

11. **Small Business, Growth Patterns, and Jobs**, Daniel Asquith and J. Fred Weston, *Business Economics*, July 1994. 46

Small business is now widely regarded as the principal generator of net new employment in the United States. The authors examine recent employment patterns and show the role that knowledge industries play in **small business job generation**.

12. **Is Big Really Bad?** Alan R. Winger, *Business Economics*, July 1994. 50

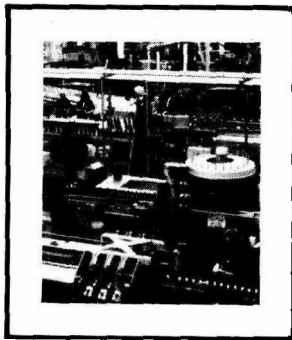
The highly visible problems faced by many "mega corporations" in recent years have led some people to conclude that a radical transformation of the structure of the U.S. economy is under way, dramatically reducing **the role of the big firm**. Alan Winger examines this possibility.

13. **Multinationals: The "Who Is Us" Debate**, Daniel F. Burton Jr., Erich Bloch, and Mark S. Mahaney, *Challenge*, September/October 1994. 55

American corporations have become so "**globalized**" in terms of where they manufacture and conduct research that they are no longer truly American. At the same time, foreign-owned U.S. subsidiaries are becoming larger and larger contributors to the U.S. economy. The authors consider the implications of these developments for public policy.

14. **The Troubled Airline Industry: Impacts on Plane Makers and the U.S. Economy**, Robert D. Shriner, *Business Economics*, January 1994. 60

Faced with sluggish passenger growth, continued losses, and tighter credit conditions, **U.S. air carriers** have cut all but immediately essential services. Robert Shriner describes competitive pressures in the airline industry.

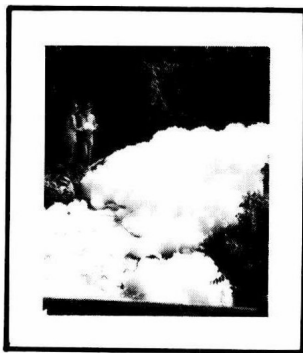


Unit 3

Labor Markets and Unions

The eight selections in this section examine the current state of labor and unions. Some of the topics include the state of unionism today, the impact of technology on labor, and a review of the workforce in other parts of the world.

15. **1980s Gigantomania Follies**, Walter Adams and James W. Brock, *Challenge*, March/April 1992. 66
Walter Adams and James Brock examine lessons that can be learned from the **merger-takeover-buy-out explosion of the 1980s**. They conclude that during this time America lost sight of the critical distinction between productive capitalism and speculative capitalism.
16. **Reengineering U.S. Manufacturing: Implications of Structural Changes in the U.S. Economy**, Daniel J. Meckstroth, *Business Economics*, July 1994. 71
Daniel Meckstroth examines **structural changes** presently at work in the U.S. economy. He argues that companies that reengineer their organizational structure, work practices, production processes, products, systems, and culture will be able to adapt to these changes.
17. **How Japanese Industry Is Rebuilding the Rust Belt**, Martin Kenney and Richard Florida, *Technology Review*, February/March 1991. 78
Following nearly a decade of decline, **American manufacturing** is on the rebound. Ironically, the agents of this revitalization are the Japanese. The authors believe that integrated production networks can serve as a model of a powerful new method of economic development.
18. **The Dynamics of the Drug Market**, Edward J. Nell, *Challenge*, March/April 1994. 87
Although the federal government has sought to control the market for illegal drugs since 1916, the results are nearly the opposite of those intended. In an **economic analysis of the "War on Drugs,"** Edward Nell underscores ways in which federal policy is at odds with the dynamics of supply and demand.
- Overview 96
19. **We're #1 and It Hurts**, George J. Church, *Time*, October 24, 1994. 98
George Church shows how the **increases in productivity**, which have recently helped make the United States so competitive in the world economy, have also had a downside: wave after wave of downsizing layoffs, forgone wage increases, and replacement of full-time workers by part-time workers.
20. **The New World of Work**, *Business Week*, October 17, 1994. 103
This essay reports on ways in which new technologies have **transformed workplaces** throughout the United States. Teamwork, empowerment, cross-training, and restructuring are the buzzwords in these new offices. But for every highly skilled worker moving up the ladder, there is another, marginalized worker, struggling to make ends meet.
21. **Collapsing Wages and Rising Inequality: Has Computerization Shifted the Demand for Skills?** David R. Howell, *Challenge*, January/February 1995. 107
Are falling real wages and sharp increases in earnings inequality the result of a technology-induced "skill-mismatch"? The prevailing view is that **labor demand has shifted away from low-skill workers**—due in large part to computerization. David Howell takes issue with this view.



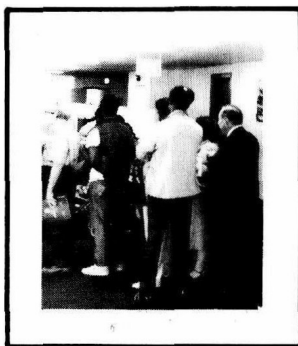
Unit 4

Market Failures and Public Microeconomics

The ten articles in this section examine the current state of product and market failures. Some of the topics include the impact of deregulation, market forces on the environment, and the effect OSHA has on the workplace.

22. **Labor Confronts the End of Unionism**, Leo Troy, *USA Today Magazine (Society for the Advancement of Education)*, May 1995. 116
Leo Troy maintains that, with American industries struggling to exist in an era of worldwide competition fueled by low worker compensation in developing nations, **private-sector unions cannot hope to survive.**
23. **What Do Unions Do for Women?** Heidi Hartmann, Roberta Spalter-Roth, and Nancy Collins, *Challenge*, July/August 1994. 120
This report asserts that **unions need women to be trained in leadership positions.** And women need to be actively involved in determining issues and formulating organizing and bargaining strategies.
24. **Why Temporary Workers Have Become a Permanent Fixture**, Robert E. Parker, *Business and Society Review*, Fall 1994. 128
Since the early 1970s, the rate of part-time, temporary, and subcontracted employment (otherwise known as "**contingent employment**") has grown far faster than the rate of full-time work. Robert Parker explains management's drive for a contingent workforce.
25. **A Pay Raise's Impact**, Louis Uchitelle, *New York Times*, January 12, 1995. 134
According to conventional economic analysis, increases in the **federal minimum wage** could result in one of two things: those who remain employed get higher incomes, while other, less productive workers lose jobs as employers trim payrolls. New evidence exposes the flaws in this view.
26. **Workers of the World, Unwind**, Juliet B. Schor, *Technology Review*, November/December 1991. 136
The average American currently spends about 163 hours more at work—almost a month in time—than he or she spent in 1969. At the same time, people report nationwide that their leisure time has dropped by as much as one-third. Juliet Schor examines these trends and attributes them to an insidious cycle of "**work-and-spend.**"
- Overview 144
27. **The Law as the Free Market's Rogue: Hostage to the Prisoner's Dilemma**, Peter Passell, *New York Times*, March 25, 1994. 146
Competitive markets sometimes fail to produce efficient outcomes. Peter Passell notes that the market for legal services fails in a particularly perverse and fascinating way, known as "**the prisoner's dilemma.**"
28. **Congested Parks—A Pricing Dilemma**, Dan M. Bechter, *Monthly Review (Federal Reserve Bank of Kansas City)*, June 1971. 149
Overcrowding at public parks creates a **classic microeconomic dilemma**: outdoor recreationists face insufficient parking space, which must be allocated through adjusting park fees. This article investigates possible solutions to this problem.

29. **An Economic Case for Funding AIDS Research**, Diane Cunningham, *The Margin*, Fall 1991. 155
Should taxpayers be required to fund AIDS research? Diane Cunningham argues that leaving the solution of AIDS to the marketplace amounts to a death sentence for those afflicted with the disease. The case for public funding is based on the presence of substantial **spillover benefits**.
30. **The Environmental Cost of Free Trade**, Jeffrey A. Mello, *Business and Society Review*, Fall 1994. 156
One of the major controversies surrounding the **North American Free Trade Agreement (NAFTA)** involves the debate over the alleged effect that free trade has upon the environment. Jeffrey Mello outlines the key issues in the debate over NAFTA's **social costs**.
31. **One Answer to Overfishing: Privatize the Fisheries**, Peter Passell, *New York Times*, May 11, 1995. 166
Is it possible that fresh fish will someday become a delicacy as rare and expensive as, say, truffles? Perhaps not, but recent developments in the commercial fishing industry suggest that the days of relying on the oceans as a primary source of food are numbered. Peter Passell asks, Would the **privatization of fishing rights** improve matters?
32. **Mailing Mania: Privatization Fever Grips the Postal Service**, Sarah Ryan, *Dollars & Sense*, January/February 1995. 168
Privatization of postal services has been suggested as a way to cut costs and provide opportunities for private businesses to enter the giant U.S. postal market. Sarah Ryan warns that the true result may be a deterioration of the wages and working conditions of postal employees.
33. **The Free Market for Clean Air**, David B. Webster, *Business and Society Review*, Summer 1994. 173
Recent amendments to the Clean Air Act of 1990 allow companies to buy and sell the right to pollute. **Pollution trading** has the potential to help society decide how much pollution we are willing to live with, and who will pay the cost of reducing it. But, as David Webster demonstrates, it is not a panacea.
34. **Acid-Rain Pollution Credits Are Not Enticing Utilities**, Matthew L. Wald, *New York Times*, June 5, 1995. 177
Matthew Wald traces development in the **market for pollution trading rights** over the past five years. In order for a free-market system for controlling emissions to work, major changes in both standards and attitudes are needed.
35. **Has the F.C.C. Become Obsolete?** Edmund L. Andrews, *New York Times*, June 12, 1995. 179
Established in 1934, the **Federal Communications Commission (FCC)** is an independent agency that regulates the U.S. communications industry. Given recent changes in the industry, Edmund Andrews notes that it is time to ask, Is the FCC obsolete, or is it still in the public interest?
36. **Are OSHA Penalties Effective?** Wallace N. Davidson III, Dan L. Worrell, and Louis T. W. Cheng, *Business and Society Review*, Winter 1995. 182
In this study of penalties assessed by the **Occupational Safety and Health Administration (OSHA)** for violations of workplace safety laws, the authors find a close link between stock prices and OSHA's effectiveness.



Unit 5

Income Distribution and Economic Justice

The nine selections in this section consider the dynamics of income distribution. Topics include American income inequality, the economic strain on the middle class, and problems with the welfare system.

- | | |
|--|-----|
| Overview | 186 |
| 37. The Inequality Express , Barry Bluestone, <i>The American Prospect</i> , Winter 1995. | 188 |
| In recent years the gap in earnings between the well-educated and not-so-well educated has increased steadily, while the real standard of living for a large portion of the workforce has sharply declined. Barry Bluestone surveys the major reasons for these trends in income distribution . | |
| 38. Gap in Wealth in U.S. Called Widest in West , Keith Bradsher, <i>New York Times</i> , April 17, 1995. | 196 |
| New studies show that, rather than being an egalitarian society, the United States has become the most economically stratified of industrial nations. Keith Bradsher examines global income disparities . | |
| 39. Do Poor Women Have a Right to Bear Children? Christopher Jencks and Kathryn Edin, <i>The American Prospect</i> , Winter 1995. | 199 |
| At the heart of the debate over welfare reform is the assumption (made by most politicians) that people should not have children until they are ready to support them . Christopher Jencks and Kathryn Edin ask, Are we really prepared to enforce this principle and all of its implications? | |
| 40. Ending Welfare as We Know It , Michael Tanner, <i>USA Today Magazine</i> (<i>Society for the Advancement of Education</i>), March 1995. | 208 |
| Michael Tanner argues that it is time to recognize that federal welfare cannot be reformed and should be ended altogether . In his view, this would be fairer than sacrificing another generation to a system that simply cannot work. | |
| 41. The Myths of Charity , <i>U.S. News & World Report</i> , January 16, 1995. | 213 |
| The idea that charities could pick up all or even most of the slack from cuts in federal social programs is rooted in two myths: that charities provide a private social safety net and that a golden age of charity can be rekindled. | |
| 42. There but for Fortune , John J. Dilulio Jr., <i>The New Republic</i> , June 24, 1991. | 215 |
| Available evidence suggests that, on any given night, between 1.5 and 3 million Americans are literally homeless, while another 4 to 7 million are so poor as to be precariously housed. In this survey of recent findings of homelessness in America , John Dilulio shows how both public and private efforts might be directed to resolving the crisis. | |
| 43. Blacks Locked Out of the American Dream , Scott Minerbrook, <i>Business and Society Review</i> , Fall 1993. | 222 |
| Millions of African Americans who have climbed into the security of the middle and upper classes find that the dream of buying a home is a nightmare of misuses and obstacles. Scott Minerbrook discusses the dilemmas of housing discrimination . | |

44. Myths of an Aging America , Charles F. Longino Jr., <i>American Demographics</i> , August 1994.	228
Will a growing elderly population place an overwhelming burden on American society? Most demographers foresee an increasing demand for long-term health care, but many ignore a wild card—new generations moving into retirement. Charles Longino shows why the future may not be as scary as we think.	
45. Beyond Supply and Demand: The Framework of the Market Economy , Patrick M. Boarman, <i>Challenge</i> , March/April 1994.	233
The search for a " capitalism with a human face " could become, in the view of Patrick Boarman, the dominant concern of the last years of this century and the first years of the next for economists everywhere.	
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Topic Guide

This topic guide suggests how the selections in this book relate to topics of traditional concern to students and professionals involved with the study of microeconomics. It is useful for locating articles that relate to each other for reading and research. The guide is arranged alphabetically according to topic. Articles may, of course, treat topics that do not appear in the topic guide. In turn, entries in the topic guide do not necessarily constitute a comprehensive listing of all the contents of each selection.

TOPIC AREA	TREATED IN:	TOPIC AREA	TREATED IN:
Accounting Practices	8. Costing the Factory of the Future	Econometrics	9. Strange World of Business Forecasters
AIDS Research	29. Economic Case for Funding AIDS Research	Economies of Scale	12. Is Big Really Bad?
Airline Industry	1. How Much for a Life? 5. King Customer 14. Troubled Airline Industry	Education	20. New World of Work 21. Collapsing Wages and Rising Inequality 23. What Do Unions Do for Women? 37. Inequality Express
Automobile Industry	13. Multinationals 15. 1980s Gigantomania Follies 17. Japanese Industry Is Rebuilding the Rust Belt 19. We're #1 and It Hurts	Elderly	44. Myths of an Aging America
Barriers to Entry	17. Japanese Industry Is Rebuilding the Rust Belt	Environmental Protection	30. Environmental Cost of Free Trade 33. Free Market for Clean Air 34. Acid-Rain Pollution Credits Are Not Enticing Utilities
Business Forecasting	9. Strange World of Business Forecasters	Federal Communications Commission (FCC)	35. Has the F.C.C. Become Obsolete?
Charity	41. Myths of Charity	Fishing Industry	31. One Answer to Overfishing
Common Resource Problem	28. Congested Parks—A Pricing Dilemma 31. One Answer to Overfishing	Health Care Industry	3. What's All This about Pharmacoeconomics? 29. Economic Case for Funding AIDS Research 44. Myths of an Aging America
Consumers	5. King Customer 7. How the Marketplace Fosters Business Honesty	Housing Industry	42. There but for Fortune 43. Blacks Locked Out of the American Dream
Contingent Workers	20. New World of Work 24. Why Temporary Workers Have Become a Permanent Fixture	Human Capital Theory	1. How Much for a Life?
Corporate Nationality	13. Multinationals	Immigration	37. Inequality Express
Cost-Benefit Analysis	1. How Much for a Life? 2. "Does Prison Pay?" Revisited 3. What's All This about Pharmacoeconomics?	Income Distribution	19. We're #1 and It Hurts 21. Collapsing Wages and Rising Inequality 25. Pay Raise's Impact 37. Inequality Express 38. Gap in Wealth in U.S. Called Widest 39. Do Poor Women Have a Right to Bear Children? 40. Ending Welfare as We Know It 42. There but for Fortune 43. Blacks Locked Out of the American Dream
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Drug Industry	3. What's All This about Pharmacoeconomics? 18. The Dynamics of the Drug Market		

TOPIC AREA	TREATED IN:	TOPIC AREA	TREATED IN:
Labor Productivity	16. Reengineering U.S. Manufacturing 19. We're #1 and It Hurts 20. New World of Work 21. Collapsing Wages and Rising Inequality 25. Pay Raise's Impact	Prisoner's Dilemma	27. Law as the Free Market's Rogue
Labor-Management Relations	6. Corporate "Ownership" 16. Reengineering U.S. Manufacturing 19. We're #1 and It Hurts 20. New World of Work 22. Labor Confronts the End of Unionism 23. What Do Unions Do for Women? 37. Inequality Express	Privatization	31. One Answer to Overfishing 32. Mailing Mania
Leisure-Work Trade-Off	26. Workers of the World, Unwind	Public Pricing	4. Disneyland and the Old U.S.S.R. 28. Congested Parks—A Pricing Dilemma 34. Acid-Rain Pollution Credits Are Not Enticing Utilities 35. Has the F.C.C. Become Obsolete?
Market Failure	27. Law as the Free Market's Rogue 28. Congested Parks—A Pricing Dilemma 29. Economic Case for Funding AIDS Research 30. Environmental Cost of Free Trade 42. There but for Fortune 45. Beyond Supply and Demand	Rationing	4. Disneyland and the Old U.S.S.R.
Minimum Wage	25. Pay Raise's Impact	Rent	42. There but for Fortune
Monopolistic Competition	11. Small Business, Growth Patterns, and Jobs 28. Congested Parks—A Pricing Dilemma	Service Industries	11. Small Business, Growth Patterns, and Jobs 23. What Do Unions Do for Women?
North American Free Trade Agreement (NAFTA)	30. Environmental Cost of Free Trade 37. Inequality Express	Skill Mismatch	21. Collapsing Wages and Rising Inequality 24. Why Temporary Workers Have Become a Permanent Fixture
Occupational Safety and Health Administration (OSHA)	36. Are OSHA Penalties Effective?	Steel Industry	17. Japanese Industry Is Rebuilding the Rust Belt
Oligopoly	10. Leap into Economic Change 12. Is Big Really Bad? 13. Multinationals 14. Troubled Airline Industry 15. 1980s Gigantomania Follies 16. Reengineering U.S. Manufacturing 17. Japanese Industry Is Rebuilding the Rust Belt	Telecommunications Industry	10. Leap into Economic Change 13. Multinationals 35. Has the F.C.C. Become Obsolete?
Opportunity Costs	1. How Much for a Life? 2. "Does Prison Pay?" Revisited	User Fees	28. Congested Parks—A Pricing Dilemma
Ownership Rights	6. Corporate "Ownership"	Vertical Integration	12. Is Big Really Bad? 16. Reengineering U.S. Manufacturing
Pollution Trading Rights	33. Free Market for Clean Air 34. Acid-Rain Pollution Credits Are Not Enticing Utilities	War on Drugs	18. Dynamics of the Drug Market
Postal Service	32. Mailing Mania	Welfare Programs	39. Do Poor Women Have a Right to Bear Children? 40. Ending Welfare as We Know It 41. Myths of Charity
		Worker Participation	6. Corporate "Ownership" 20. New World of Work 22. Labor Confronts the End of Unionism 24. Why Temporary Workers Have Become a Permanent Fixture
		Workfare	39. Do Poor Women Have a Right to Bear Children? 40. Ending Welfare as We Know It

Introduction to Microeconomics

Consumption is the sole end and purpose of all production; and the interest of the producer ought to be attended to, only so far as it may be necessary for promoting that of the consumer.

Adam Smith, *The Wealth of Nations*

While there are many ways to subdivide the science of economics, the most common one distinguishes between microeconomics and macroeconomics. Microeconomics involves the study of the economy "in the small"; it investigates the economy in terms of its separate components, and it focuses on the individual decision-making processes of consumers and producers in various market settings. Macroeconomics, on the other hand, is the study of the economy "in the large"; it concerns such broad issues as how gross domestic product, unemployment, inflation, and economic growth are determined.

The microeconomic decisions of individual consumers and producers always carry a price (known as "opportunity cost") in terms of alternatives forgone. This reflects an important principle in economics, first articulated more than a half century ago by the British economist Lionel Robbins. He suggested that we are unable to do all the things we might wish to do for the simple reason that our economic resources—human talents, the natural environment, and the stock of capital—are finite. Robbins defined "the economic problem" as one of scarcity. Our resources are scarce because the number of possible uses to which they might be put in meeting our material needs is unlimited. Economics, Robbins concluded, ultimately concerns the hard choices we must make about ways to employ these resources.

Recall the last time you shopped in a large supermarket. Seemingly endless varieties of canned goods, fresh produce, household products, and personal care items caught your eye. Each time you placed an item in

your cart you were making a consumption decision, based on such information as product price, your total budget, differences among brands, and so forth. The fact that you did not buy everything you saw reflects the fact that consumption entails opportunity costs: budgets limit the choices consumers make and force them to forgo some items that they might otherwise purchase. While you may not have been aware of it at the time, the producers of each of these items had to face a similar problem when they decided to make them: unable to produce everything they might wish to, these firms had to second-guess what you would finally put in your cart. Such decisions also involve opportunity costs. Take the case of a new, "natural" toothpaste: the fact that major toothpaste manufacturers have not entered this market yet suggests that they consider the present opportunity cost of doing so too high. Some day they may change their minds, but they must first consider such constraints on the production process as resource availability, the total costs of production, and the existing state of technology—all of which boil down to matters of profits and the "bottom line."

This section begins with several articles that deal with various aspects of pricing. First, Peter Passel demonstrates how opportunity cost analysis can be applied to an age-old question: What is the value of human life? Such calculations play a strategic role in business decisions and the formulation of government regulations. The next two articles show how economists use cost-benefit analysis to assess the relative merits of things, in this case the services of correctional institutions (a public good) and health care interventions involving ethical drugs (a private good). Then, parallels are drawn between pricing in two apparently dissimilar environments, Disneyland and the former Soviet Union. Both assume efficiency is not every-

thing, that rationing with time instead of money allows people to avoid confronting the unwelcome realities of limited income.

The following article involves consumers. "King Customer" reports on efforts by a number of U.S. firms aimed at "putting the customer first." This article maintains that businesses exist to serve consumers and "should bend over backward to satisfy their needs." But it adds "too many companies still don't get it."

The remaining unit articles focus on various aspects of producer behavior. In "Corporate 'Ownership'" Margaret Blair asserts that corporate governance involves questions about the rights and prerogatives not only of shareholders, but also of other participants in the firm. Dwight Lee and Richard McKenzie, in "How the Marketplace Fosters Business Honesty," show that, if businesspeople act honestly, it is in part because they pay a high price for behaving dishonestly. The essay "Costing the Factory of the Future" explains why managers may be relying on numbers that are not appropriate for the competitive challenges of the 1990s. Finally, Liz Roman Gallese warns of the hazards of business decision making in a world in which, more often than not, economic data is seriously flawed.

Looking Ahead: Challenge Questions

How much do you think a human life is worth?

Do you think that prisons cost too much? Why?

In what ways are Disneyland and the former Soviet Union similar?

What influences producer behavior? Who governs corporations?

Does the marketplace foster or hinder business honesty?



How Much For A Life? Try \$3 Million to \$5 Million

Even so, risk experts say some safety laws just aren't worth it.

Peter Passell

You've watched in horror a dozen times: Scenes of barely recognizable aircraft parts strewn across smoldering moonscapes, with the occasional shoe or child's toy the only reminders of lives snuffed out in unimaginable terror. And no doubt you've wondered when it would be your turn, a thought quickly shrugged away but never truly forgotten.

Flying, everyone knows, is a risky business. Any expense that makes it safer thus seems an expense worth making. And the only question most people ask after a crash is how to get the regulators to get off their duffs before the next one.

But the truth comes in shades of gray, not black and white. Americans' obsession with the tiny probability of dying in an airline accident is, at best, a distraction from the reality that commercial aviation is one of the great blessings of the age. At worst, it is an invitation to expensive and even self-defeating fixes, a symptom of our inability to cope sensibly with risk. But Republican conservatives in Congress are now pressing for a more sharp-penciled analysis of the cost of government health and safety regulations.

Just how safe is flying in America? Based on the experience of the last two decades, Arnold Barnett, a management professor at the Massachusetts Institute of Technology, sets the probability of dying from unnatural causes on your next commercial jet flight at about one in seven million. A flier who boards a jet each day can thus expect to meet the grim reaper every 19,000 years.

The propeller planes linking hundreds of small cities to big airports are three or four times as dangerous. But that only brings the odds of ending up a grim statistic to one in two million. The chance of suffering a heart attack while waiting for the conveyor belt to mangle your luggage is much greater.

The yawning gap between the actual and imagined risk of flying no longer surprises specialists in risk analysis, who make careers of explaining why people who brush aside the dangers of driving on icy highways or gorging on cookie dough ice cream are so ready to believe that portable phones cause brain cancer. But a comparison of the way risk analysts think about safety with the way Government balances risk against potential gain is sobering.

Probabilities alone don't offer much insight into which chances are worth taking. That question, suggests the brave new science of risk analysis, can be answered only by weighing the cost of avoiding a statistical death against the subjective value of life.

Try that one again. Assume for the sake of argument that it would cost \$500 per car to put anti-skid brakes in each of the 10 million cars sold this year—a total of \$5 billion. Assume that installing the gadgets on this year's fleet would ultimately save 5,000 lives, or \$1 million per life. Assume that, on average, people value their lives at up to \$5 million. Since the \$1 million cost of saving a life is less than the \$5 million value of life, the safety feature must be worth buying.

Sounds O.K., at least until the part about the value of life being \$5 million. Who is to say that a life is worth \$5 million rather than \$500 million?

One answer is Americans couldn't afford to spend \$500 million. Kip Viscusi, an economist at Duke University, estimates that if the entire gross national product were devoted to making life safer, there would only be \$55 million available to prevent each accidental death. So, at least in this limited sense, life must be worth less than \$55 million.

More to the point, people voluntarily accept the risk of death in return for money all the time. Dozens of studies have imputed a value to life from data on the extra wages required to lure workers to perform dangerous jobs. If, for example, it takes an extra \$100,000