

Sixth Edition

ECONOMICS

Edwin Mansfield

E C O N O M I C S

PRINCIPLES/PROBLEMS/DECISIONS

E D W I N M A N S F I E L D

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S I X T H E D I T I O N



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PREFACE

The American economy, while basically strong and vibrant, is beset by a number of problems which must be faced in the next decade. With the students of a new decade in mind, a major thrust of this revision has been to devote space to these central economic problems. Major new sections, each two or more pages long, have been added on the following “Economic Issues of the 1990s”: (1) The Enormous Federal Budget Deficits, (2) What’s Become of the Relationship between the Money Supply and GNP? (3) America’s Chronic Trade Deficit, (4) Can American Firms Compete? (5) Corporate Takeovers: Boon or Problem? (6) The AIDS Epidemic and Who Will Pay, (7) Should the Minimum Wage Go Up? (8) Has the United States Lost Its Technological Edge? Each of these new sections indicates how economic analysis can help to illuminate these central public issues. Based on my own classroom experience, this new feature of this text should be of great use in whetting the interest of students and in helping them to thread their way through complex contemporary issues.

Many of these “Economic Issues of the 1990s” are concerned with the international competitiveness of American industry and international economic relationships. Reflecting their continued growth in importance to the American economy, this new edition places much more emphasis on these topics. The principle of comparative advantage is presented in Chapter 2. New sections on the effects of exports and imports on net national product, as well as on fiscal policy in an open economy, are now in Chapter 11. Detailed treatments of international trade and international finance have been moved forward to Chapters 17 and 18. A new insert on strategic trade policy is found in Chapter 17.

The organization of the book has been changed in other major ways as well. The discussion of government expenditures and taxation is now placed later (in Chapters 27 to 29), thus permitting a fuller analysis of these important topics. The re-positioning of these chapters has the important advantage as well of allowing us to get to macroeconomics more quickly: the coverage now begins in Chapter 5. Also, the treatment of aggregate supply in Chapter 7 has been beefed up considerably. Further, a substantial amount of material has been added (in Chapters 10 and 28) concerning budget deficits and the federal debt, including more on the New Classical Economists’ views in this regard. Chapter 11 contains a new boxed example called “How Good Were Chairman Greenspan’s Forecasts?” that gives students a pointed look at the advantages—and problems—of macroeconomic forecasting. In addition, the treatment of rational expectations in Chapters 15 and 16 has been expanded, while some of the Keynesian-monetarist issues

that are no longer of central importance have been dropped. The material on economic growth in developed and developing countries, which has been brought together in Chapters 33 and 34, contains new material, including a boxed example on the economic plight of Nigeria.

The microeconomic chapters, like the macroeconomic ones, have been revised significantly. Chapter 4 contains a new insert on the stock market crash of 1987, as well as a boxed example dealing with another Wall Street market: a hot dog vendor. The examination of consumer behavior in Chapter 20 now begins with a recent study of the finances of a Jacksonville, Florida, family. Chapter 25 includes a boxed example on “The End of the Cozy Milk Oligopoly in New York,” as well as new material on the prisoner’s dilemma and “tit for tat.” Chapter 27 deals with Sematech, the Pentagon-financed R and D consortium in the semiconductor industry. Chapter 30 contains a new insert on “Equal Pay for Work of Comparable Worth.” Chapter 35 provides a new section on Mikhail Gorbachev’s economic reforms in the Soviet Union.

Besides adding new features and material, this edition builds on and extends some unique features of the previous edition. To help students see (and remember) the forest, as distinct from a hodgepodge of trees, a relatively small number of Basic Ideas (one or two per chapter) are highlighted. In this edition, these basic ideas have been sharpened and reduced in number, and each is accompanied by an example. One can reasonably expect these Basic Ideas to stick with students; and if so, their time will have been well spent because these ideas really constitute the heart of elementary economics, stripped of frills and details.

Most textbooks do not encourage the student to get involved in the subject. They simply lay out the material, leaving the student to absorb it passively. In previous editions, I have invited students to *do* economics in order to understand it better. Scores of examples were provided, each describing a real (or realistic) situation and then calling on the student to work through the solution. Also, in each chapter there were two problem sets, both designated “Test Yourself” that enabled students to check their comprehension of what they had just read. The reaction of instructors and students was very favorable, and the emphasis on doing economics is maintained in this Sixth Edition.

All of the empirical and policy-oriented chapters have been updated. Since a text should reflect current conditions and concerns, the government policies in all the major economic areas—fiscal, monetary, incomes, farm, energy, environmental, antitrust, and international—are reviewed in depth. The latest data available have been incorporated in the tables, diagrams, and discussions, while revisions in sections on economic forecasting, reserve requirements, Social Security, and a variety of other topics have brought them into line with current developments.

Since instructors differ considerably in their choice and ordering of topics, the Sixth Edition, like its predecessors, is organized for maximum flexibility. Many instructors take up microeconomics before macroeconomics. This book will work just as well for these instructors as for those who prefer to present macroeconomics first. (A suggested ordering of chapters is presented for them on p. xix.) As an alternative to reversing the chapter sequence in the one-volume edition, some instructors may want to consider the two-volume paperbound version,

Principles of Microeconomics and Principles of Macroeconomics, Sixth Editions.

This book can also be adapted for use in one-semester courses. Pages xix–xx present outlines for a one-semester course stressing microeconomics, a one-semester course stressing macroeconomics, and a one semester course covering both.

As supplements to this text, I have prepared both a book of readings and a study guide containing problems and exercises. The book of readings is in two parts, *Principles of Macroeconomics: Readings, Issues, and Cases*, Fourth Edition, and *Principles of Microeconomics: Readings, Issues, and Cases*, Fourth Edition. It provides a substantial set of supplementary articles, carefully correlated with the text for instructors who want to introduce their students to the writings of major contemporary economists. It is designed to acquaint the student with a wide range of economic analysis, spanning the spectrum from the classics to the present-day radicals. The emphasis, as in the text, is on integrating theory, measurement, and applications.

The *Study Guide*, Sixth Edition, contains, in addition to problems, review questions, and tests, a large number of cases that require the student to work with quantitative material in applying concepts to practical situations. Both students and instructors have reported that such cases are important in motivating students and illuminating economic theory.

An *Instructor's Manual* has been prepared by Michael Claudon of Middlebury College to accompany the text. A *Test Item File*, prepared by Herbert Gishlick of Rider College, is available both in printed form and on computer tape. *Transparency Masters* are also available to instructors who adopt the text.

Finally, it is a pleasure to acknowledge the debts that I owe to the many teachers at various colleges and universities who have commented in detail on various parts of the manuscript. The first, second, and third editions benefited greatly from the advice I received from the following distinguished economists, none of whom is responsible, of course, for the outcome: Wallace Atherton, California State University at Long Beach; Bela Balassa, Johns Hopkins; Robert Baldwin, University of Wisconsin (Madison); Arthur Benavie, North Carolina; Lee Biggs, Montgomery College; Donald Billings, Boise State; William Branson, Princeton; Martin Bronfenbrenner, Duke; Edward Budd, Penn State; Phillip Burstein, Purdue; Wade Chio, U.S. Air Force Academy; Michael Claudon, Middlebury; Warren Coates, Federal Reserve; Richard Cooper, Yale; Alan Deardorff, Michigan; William Desvousges, Missouri (Rolla); F. Trenery Dolbear, Brandeis; Robert Dorfman, Harvard; James Duesenberry, Harvard; William Dugger, North Texas State University; Richard Easterlin, University of Southern California; Jonathan Eaton, Princeton; David Fand, Wayne State; Judith Fernandez, University of California (Berkeley); David Gay, University of Arkansas; Howard A. Gilbert, South Dakota State University; Gerald Goldstein, Northwestern; Robert Gordon, Northwestern; Edward Gramlich, Michigan; Herschel Grossman, Brown; William Gunther, Alabama; Jerry Gustafson, Beloit; Judith Herman, Queens College; Alan Heston, University of Pennsylvania; Albert Hirschman, Harvard; Ronald Jones, Rochester; John Kareken, Minnesota; Ann Krueger, Duke; Robert Kuenne, Princeton; Simon Kuznets, Harvard; William Leonard, St.

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Philadelphia, 1988

E.M.

Outline of a One-Year Course with Macroeconomics Following Microeconomics.

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|---|---|
| 1 Economic Problems and Analysis | 8 Determining National Output |
| 2 Economic Models and Capitalism, American-Style | 9 Multiplier Analysis and Changes in Output |
| 3 The Price System | 10 Fiscal Policy and National Output |
| 4 A Guided Tour of the Business Firm | 11 Foreign Trade, Business Fluctuations, and Economic Forecasting |
| 19 Market Demand and Price Elasticity | 12 Money and the Economy |
| 20 Getting behind the Demand Curve: Consumer Behavior | 13 The Banking System and the Quantity of Money |
| 21 Optimal Input Decisions by Business Firms | 14 Monetary Policy |
| 22 Cost Analysis | 15 Controversies over Stabilization Policy |
| 23 Perfect Competition | 16 Inflation and Anti-Inflationary Measures |
| 24 Monopoly and Its Regulation | 17 International Trade |
| 25 Monopolistic Competition and Oligopoly | 18 Exchange Rates and the Balance of Payments |
| 26 Industrial Organization and Antitrust Policy | 27 The Economic Role of the Government |
| 30 Determinants of Wages | 28 Government Expenditures, Taxation, and the Public Debt |
| 31 Interest, Rent, and Profits | 29 Government and the Environment |
| 32 Income Inequality and Poverty | 33 Economic Growth |
| 5 National Income and Product | 34 The Less Developed Countries |
| 6 Unemployment and Inflation | 35 The Communist Countries and Marxism |
| 7 Aggregate Demand, Aggregate Supply, and Business Fluctuations | |
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Outline of a One-Semester Course Emphasizing Microeconomics.

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|---|---|
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| 2 Economic Models and Capitalism, American-Style | 14 Monetary Policy |
| 3 The Price System | 19 Market Demand and Price Elasticity |
| 4 A Guided Tour of the Business Firm | 20 Getting Behind the Demand Curve: Consumer Behavior |
| 5 National Income and Product | 21 Optimal Input Decisions by Business Firms |
| 6 Unemployment and Inflation | 22 Cost Analysis |
| 7 Aggregate Demand, Aggregate Supply, and Business Fluctuations | 23 Perfect Competition |
| 8 Determining National Output | 24 Monopoly and Its Regulation |
| 9 Multiplier Analysis and Changes in Output | 25 Monopolistic Competition and Oligopoly |
| 10 Fiscal Policy and National Output | 26 Industrial Organization and Antitrust Policy |
| 12 Money and the Economy | 27 The Economic Role of the Government |
| | 32 Income Inequality and Poverty [optional] |
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Outline of a One-Semester Course Emphasizing Macroeconomics.

- | | |
|---|---|
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| 2 Economic Models and Capitalism, American-Style | 13 The Banking System and the Quantity of Money |
| 3 The Price System | 14 Monetary Policy |
| 4 A Guided Tour of the Business Firm | 15 Controversies over Stabilization Policy |
| 5 National Income and Product | 17 International Trade |
| 6 Unemployment and Inflation | 18 Exchange Rates and the Balance of Payments |
| 7 Aggregate Demand, Aggregate Supply, and Business Fluctuations | 33 Economic Growth |
| 8 Determining National Output | 34 The Less Developed Countries |
| 9 Multiplier Analysis and Changes in Output | 27 The Economic Role of the Government |
| 10 Fiscal Policy and National Output | 28 Government Expenditures, Taxation, and the Public Debt |
| 11 Foreign Trade, Business Fluctuations, and Economic Forecasting | |
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Outline of a One-Semester Course Emphasizing Macroeconomics and Microeconomics.

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