Chapter 1

ECONOMICS: THE CORE ISSUES

WHAT IS THIS CHAPTER ALL ABOUT?

The chapter introduces students to the basic building blocks of economics and the operation of markets. It presents the vocabulary, graphs, and key concepts essential for the study of economics.

This chapter also establishes the central theme of market reliance vs. government direction. Current public opinion and a brief historical view of how the balance has shifted in world economies are illustrated by references to Adam Smith, Karl Marx and John Maynard Keynes.

The first chapter focuses student attention on the core problem of scarcity. The four factors of production are limited, requiring choices to be made, illustrated with a production possibilities curve. Students should compare different economies according to how they answer the three fundamental questions of economics:

1. WHAT to produce with our limited resources.
2. HOW to produce the goods and services we select.
3. FOR WHOM goods and services are produced — that is, who should get them.

LEARNING OBJECTIVES: After this chapter the students should know:

1. How scarcity creates opportunity costs.
2. What the production possibilities curve represents.
3. The three core economic questions that every society must answer.
4. How market and government approaches to economic problems differ.

NEW TO THIS EDITION

The changes to this chapter include:

- New global rankings on the extent of market reliance
- North Korea military/food shortages
- 2011-2013 defense cutbacks and call for additional spending highlighting guns vs. butter dilemma (opportunity cost)
- 1 revised Discussion Question
- 6 revised Problems
LECTURE LAUNCHERS

How long will this chapter take? – Two 75-minute class periods.

Where should you start?

1. Begin your discussion by defining the term opportunity cost.
   a. Define the term opportunity cost, then explain that each student has an opportunity cost of being in class. For example, they could be sleeping, working, attending another class, etc.
   b. Ask a few students what they could be doing rather than being in class today.
   c. Discussions about what they could (or would rather) be doing instead of being in class are excellent introductions to opportunity cost concepts and production-possibility curves.
   d. Explain how they give up more than just money to attend class or go to the movies. Try to prioritize so that the “next best alternative” can be identified.

2. Define the terms scarcity and economics.
   Once you have defined the concept of opportunity cost, you can explain that students have a scarce amount of time that they must chose how to allocate among the many competing uses.

3. Remember the three questions: What, How and For Whom.
   When introducing the study of economics it is important to note that we make choices. An effective way to stimulate class discussions is to take an extreme stance on whether our economy should be pure market or government directed. Once students start to object to your stance, have them defend their answers.

   A stimulating discussion question is, “How many people would attend school if education was provided only by the private market?” If you teach in a state school, many people would say they could not attend college without state subsidies. If you teach in a private school, ask how many students receive guaranteed student loans, Pell grants, etc. Follow this discussion with the question “Then is there a role for government in subsidizing education?”

COMMON STUDENT ERRORS

The first statement in each “common error” below is incorrect. Each incorrect statement is followed by a corrected version and an explanation. These same common errors are included in the student Study Guide.

1. Words mean the same thing in economics that they do in our everyday conversation. **WRONG!**
   Words used in everyday conversation very often have different meanings when they are used in economics. **RIGHT!**
   You will have to be very careful here. Words are used with precision in economics. Like many subjects, to study economics, you must understand the language. Failure to do so will result in misinterpreting what your professor is saying or asking, especially on the exams. You will have difficulty if you confuse a term’s everyday meaning with its economic
meaning. For example, the term “capital” in economics means “final goods produced for use in the production of other goods.” In everyday usage, it may mean money, machines, a loan, or even the British response to the question “How are you feeling?”

2. Economic models are abstractions from the real world and are therefore useless in predicting and explaining economic behavior. **WRONG!**
Economic models are abstractions from the real world and as a result are useful in predicting and explaining economic behavior. **RIGHT!**
You have to be willing to deal with abstractions if you want to get anything accomplished in economics. By using economic models based on specific assumptions, we can make reasonable judgments about what’s going on around us. We try not to disregard any useful information. However, to try to include everything (such as what cereal we like for breakfast) would be fruitless. For example, the production-possibilities frontier is an abstraction. No economist would argue that it is an economy! However, it certainly is useful in focusing on choices, such as the choice between televisions and shoes.

3. Because economics is a “science”, all economists should come up with the same answer to any given question. **WRONG!**
Economics is a science, but there is often room for disagreement in trying to answer a given question. **RIGHT!**
Economics is a social science, and the entire society and economy represent the economist’s laboratory. Economists cannot run the kind of experiments that are done by physical scientists. Therefore, two economists may attack a given problem or question in different ways using different models. They may come up with different answers, but since there is no answer book, you cannot say which is right. The solution is, then, to do more testing, refine our models, compare results, and so on. By the way, discoveries by physicists using the Hubble space telescope have given physicists cause to reevaluate much of their theory concerning the solar system, and there is much controversy concerning what the new evidence means. Nevertheless, physics is still a science, as is economics!

4. Increasing opportunity cost results from increasing inefficiency. **WRONG!**
Increasing opportunity cost occurs even when resources are being used at their peak efficiency. **RIGHT!**
Increasing opportunity cost and inefficiency are confused because both result in a lower amount of output per unit of input. However, inefficiency results from poor utilization or underemployment of resources, while increasing opportunity results from the increasing difficulty of adapting resources to production as more of a good is produced. Inefficiency can be represented as a movement inward toward the origin from the production-possibilities curve, while increasing opportunity cost can be measured in movements along the production-possibilities curve. Specifically, opportunity cost is measured by the absolute value of the slope of the production-possibilities curve. A production possibility curve that is curved away from the origin demonstrates increasing opportunity cost. As the slope becomes steeper in movements down the production-possibilities curve, the good on the x-axis experiences increasing opportunity cost (a steeper slope). Similarly, a movement up along the production-possibilities curve represents a higher opportunity cost for the good on the y-axis – this time in the form of a flatter slope as more of the good on the y-axis is produced.
I. Introduction
   A. Barack Obama was reelected President of the U.S. in the hope that he would improve the economy.
      1. Government policy is used to help ease economic problems.
      2. The President and Congress have choices to make.
   B. The economic choice revolves around scarce resources. Here are a few questions the President and policy makers might pose:
      1. What do we want the economy to produce?
      2. How can we assure that outcome?
      3. Will the output of the economy be distributed fairly?
      4. Will the environment be protected?
      5. What role should government play in answering these questions?
      6. How much should we rely on the private sector—markets—to answer these questions?
   C. This introduces the concept of making difficult choices because of scarce resources
   D. Definition: Economics – The study of how best to allocate scarce resources among competing uses.
   E. The three core issues that must be resolved are:
      1. WHAT to produce with our limited resources.
      2. HOW to produce the goods and services we select.
      3. FOR WHOM goods and services are produced; that is, who should get them.

II. The Economy is Us
   A. “The Economy” is simply an abstraction that refers to the sum of all our individual production and consumption activities. In this sense, the economy is us, the aggregation of all of our supply and demand decisions.
   B. We may not always be happy with the output of the economy. Nevertheless, we cannot ignore the link between individual action and collective outcomes.

III. Scarcity: The Core Problem
   A. Although we can change economic outcomes, we cannot have everything we want. Like every other nation, we have to grapple with the core problem of scarcity.
   B. Definition: Scarcity – The fact that available resources are insufficient to satisfy all desired uses thereof.
   C. Factors of Production
      1. Definition: Factors of Production – Resource inputs used to produce goods and services, e.g., land, labor, capital, entrepreneurship.
      2. There are four basic factors of production.
         - Land – refers not just to the ground but to all natural resources such as crude oil, water, air and minerals.
         - Labor – refers to the skills and abilities to produce goods and services. Hence, both the quantity and the quality of human resources are included in the “labor” factor.
         - Capital – Fishing nets are a final good in Thailand that are themselves a factor of production in obtaining the final goods (fish) that people desire.
            - Definition: Capital – Final goods produced for use in the production of other goods, e.g., equipment, structures.
• **Entrepreneurship** – It’s not just a matter of what resources you have but also of how well you use them.
  - **Definition:** **Entrepreneurship** – The assembling of resources to produce new or improved products and technologies.

D. **Limits to Output**
1. No matter how an economy is organized there is a limit to how fast it can grow.
2. The most evident limit is the amount of resources available for producing goods and services.
3. **Definition:** **Scarcity** – the imbalance between our desires and available resources – forces us to make economic choices.
4. President Bush’s proposal to colonize the Moon and explore Mars will require scarce resources; fewer resources for other earthly goods.

E. **Opportunity Costs**
1. Every time we choose to use scarce resources in one way we give up the opportunity to use them in other ways.
2. **Definition:** **Opportunity Cost** – The most desired goods or services that are forgone in order to obtain something else.
3. Everything we do involves an opportunity cost.

F. **Guns vs. Butter**
1. One of the persistent choices about resource use entails defense spending.
2. The U.S. government spends more than $700 billion a year on national defense.
3. From an economic view, those defense expenditures also represent an enormous claim on scarce resources.
4. The 1.4 million men and women serving in the armed forces aren’t available to build schools, program computers, or teach economics.
5. The land, labor, capital, and entrepreneurship devoted to producing military hardware are not available for producing civilian goods, thus the “guns vs. butter” dilemma.
6. Since the end of the Cold War, the United States has chosen to produce more “Butter” (Civilian goods) and fewer “guns” (Military goods) resulting in defense spending declining from a high of 6.3 percent of total output in 1986 to less than 4 percent.
7. This freeing up of resources from the military sector is referred to as the “peace dividend”.

IV. **Production Possibilities**
A. **The Production Possibilities Schedule and Curve** (Table 1.1 and Figure 1.1)
1. **Definition:** **Production Possibilities** – The alternative combinations of final goods and services that could be produced in a given time period with all available resources and technology.
2. Each point on the production possibilities curve depicts an alternative mix of output.
3. The production possibilities curve illustrates two essential principles:
   - **Scarc resources** – There is a limit to the amount we can produce in a given time period with available resources and technology.
   - **Opportunity costs** – We can obtain additional quantities of any desired good only by reducing the potential production of another good.

B. **Increasing Opportunity Costs** (Figure 1.1)
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1. The shape of the production possibilities curve reflects another limitation on our choices.
2. The production possibilities curve illustrated in Figure 1.1 demonstrates increasing opportunity costs.
3. Why do opportunity costs increase? Mostly because it is difficult to move resources from one industry to another.
4. The “law” of increasing opportunity cost says that we must give up ever-increasing quantities of other goods and services in order to get more of a particular good.

C. The Cost of North Korea’s Military (Figure 1.2)
1. North Korea maintains the fifth largest army in the world.
2. To do so, it must allocate nearly 16 percent of all its resources to feeding, clothing, and equipping its military forces.
3. As a result, there aren’t enough resources available to produce food.
4. World View: “Chronic Food Shortage Shows Despite Efforts by North Korea to Hide It”
North Korea suffered severe food shortages and famine due to its spending on a huge military; resources used for the military aren’t available for producing food. 
World View: “Rocket Launch Cost Enough to End Famine in North Korea for a Year”
In 1998 North Korea stepped up plans to produce more missiles and construct new launch facilities.
In 2006, the missile test was a failure, but the cost was real. Food was sacrificed for the missile research, development and testing.
5. The military share of total output is shown here. (Figure 1.3)

D. Efficiency (Figures 1.1 and 1.2)
1. Although not all the choices on the production possibilities curve are equally desirable, they are all efficient.
2. Efficiency means obtaining the most output possible from an economy’s available resources – that is, using factors of production in the most productive way.
3. Definition: Efficiency – Maximum output of a good from the resources used in production.
4. All points on the PPC curve demonstrate efficiency.

E. Inefficiency (Figure 1.4)
1. There’s no guarantee, of course, that we’ll always use resources efficiently.
2. A production possibilities curve shows potential output, not necessarily actual output.
3. If we are inefficient, actual output will be less than the potential output.
4. All points inside the PPC curve demonstrate inefficiency.

F. Unemployment
1. Countries may also end up inside their production possibilities curve if all available resources aren’t used.
2. In October 2009, for example, over 14.5 million Americans were unemployed.
3. As a result, we were stuck inside the production possibilities curve producing less output than we could have.

G. In the News: Jobless Workers Outnumber Manufacturing Workers (Figure 1.4)
1. 15.0 million Americans unemployed exceeded the number holding jobs in manufacturing in 2009.
2. Unemployment means that we are not producing to our capabilities. We are definitely inside the PPC.
H. Economic Growth  (Figure 1.5)
1. In figure 1.4, point X lies outside the production possibilities curve.
2. It suggests that we could get more goods than we are currently capable of producing!
3. All output combinations that lie outside the production possibilities curve are unattainable with available resources and technology.
4. Over time, population increases and we get more labor. Also, if we would build more factories and machinery, the stock of available capital would also increase.
5. The quality of labor and capital can also increase if we train workers and pursue new technologies.
6. All of these changes will increase potential output and will shift the production possibilities curve outward.
7. With more resources or better technology, our production possibilities increase.
8. Definition: Economic Growth – An increase in output (real GDP); an expansion of production possibilities.

V. Basic Decisions
A. WHAT - There are millions of points along a production possibilities curve, and each one represents a specific mix of output. We can choose only one of these points at any time.
B. HOW – Decisions must also be made about HOW to produce.
C. FOR WHOM – After we’ve decided what to produce and how, we must address a third basic question: FOR WHOM? Who is going to get the output produced? Should everyone get an equal share?

VI. The Mechanisms of Choice
A. Answers to the question of WHAT, HOW, and FOR WHOM largely define an economy. But who formulates the answers?
B. The Invisible Hand of a Market Economy
1. Adam Smith, in The Wealth of Nations, said the “invisible hand” determines what gets produce, how, and for whom.
2. For example, in the auto industry, the interactions between consumers and producers determine how many cars are produced rather than some central planning agency.
3. Definition: Market Mechanism – The use of market prices and sales to signal desired outputs (or resource allocations).
4. The essential feature of the market mechanism is the price signal.
5. The market mechanism can also answer the HOW and FOR WHOM questions.
   • To maximize their profits, producers will seek to use the lowest-cost method of producing a good.
   • A market distributes goods to the highest bidder. Individuals who are willing and able to pay the most for a good tend to get it in a pure market economy.
C. Government Intervention and Command Economies
1. The laissez-faire policy Adam Smith favored has always had its share of critics.
2. Karl Marx emphasized how free markets tend to concentrate wealth and power in the hands of the few, at the expense of the many.
As Marx saw it, unfettered markets permit the capitalists (those who own the machinery and factories) to enrich themselves while the proletariat (the workers) toil long hours for subsistence wages. Marx argued that the government not only had to intervene but had to own all the means of production.

3. John Maynard Keynes seemed to offer a less drastic solution.
   - The market, he conceded, was pretty efficient in organizing production and building better mousetraps.
   - However, individual producers and workers had no control over the broader economy. He believed the cumulative actions of so many economic agents could easily tip the economy in the wrong direction.
   - In Keynes’ view, government should play an active but no all-inclusive role in managing the economy.

D. Continuing Debates
   1. The core of most debates is some variation of the WHAT, HOW, or FOR WHOM questions.
   2. Conservatives favor Adam Smith’s laissez-faire approach with minimum government interference.
   3. Liberals tend to think government intervention is needed to improve market outcomes.
      This World View gives the results of a poll of 15 countries regarding the effectiveness of the free market economic system. The consensus was that it is the best system for the world’s future; especially in China.
   5. World View: “Index of Economic Freedom”
      This World View provides a ranking of the world’s nations in terms of economic freedom. Hong Kong, Singapore and Australia rank at the top of the list while North Korea and Cuba rank at the bottom. The U.S. is not on the list. All nations must decide whether to rely on market signals or government directives to determine economic outcomes. Nations that rely the least on government intervention score highest on this Index of Economic Freedom.
   6. Countries answer the basic economics questions differently and their answers change over time.

E. A Mixed Economy
   1. Most economies use a combination of market signals and government directives to select economic outcomes.
   2. Definition: Mixed Economy – An economy that uses both market signals and government directives to allocate goods and resources.

F. Market Failure
   1. When market signals don’t give the best possible answers to the WHAT, HOW, and FOR WHOM questions, we say that the market mechanism has failed.
   2. Definition: Market Failure – An imperfection in the market mechanism that prevents optimal outcomes.

G. Government Failure
   1. Government intervention may move us closer to our economic goals. But government intervention may fail as well.
   2. Definition: Government Failure – Government intervention that fails to improve economic outcomes.
   3. Examples of government failures include:
      - Forcing an industry to clean up its pollution in a manner that is excessive.
Mandating pollution control technologies that are too expensive or even obsolete.
Imposing excessive taxes and transfer payments so that the total economic pie shrinks making society as a whole worse off.
4. Newly-introduced incentives, including increased private ownership, move China away from a centrally-planned economy in an effort to increase productivity and growth.

H. Seeking Balance
1. None of these failures has to occur, but they might.
2. The challenge for any society is to minimize failures by selecting the appropriate balance of market signals and government directives.
3. It requires that we know how markets work and why they sometimes fail.
4. We also need to know what policy options the government has and how and when they might work.

VII. What Economics is All About
A. Understanding how economies function is the basic purpose of studying economics – to learn how:
   1. An economy is organized
   2. It behaves
   3. Successfully it achieves its basic objectives.

B. End vs. Means
   1. Economists don’t formulate an economy’s objectives.
   2. Instead, they focus on the means available for achieving given goals.
   3. Normative vs. Positive Analysis—Normative analysis incorporates subjective judgments of what ought to be done. Positive analysis focuses on how things might be done, without subjective judgments of what is “best”.

C. Macro vs. Micro
   1. **Definition:** Macroeconomics – The study of aggregate economic behavior, of the economy as a whole.
   2. **Definition:** Microeconomics – The study of individual behavior in the economy, of the components of the larger economy.
   3. For example, in macroeconomics, we might be concerned about how much money, in total, consumers will spend on goods and services. In microeconomics, economists focus attention on how much consumers spend on specific goods.
   4. Although the study of microeconomics and macroeconomics operate at different levels of abstraction, they are intrinsically related. Macro (aggregate) outcomes depend on micro behavior, and micro (individual) behavior is affected by macro outcomes.

D. Theory vs. Reality
   1. The distinction between macroeconomics and microeconomics is one of many simplifications we make in studying economic behavior.
   2. The economy is much too vast and complex to describe and explain in one course (or one lifetime).
   3. We therefore focus on basic relationships.
   4. We isolate basic principles of economic behavior and then use those principles to predict economic events and develop economic policies.
   5. We formulate theories, or models, of economic behavior and then use those theories to evaluate and design economic policy.
6. In these theories, we typically ignore the possibility that many things can change at one time.

7. **Definition:** **Ceteris Paribus** – The assumption of nothing else changing.

8. Although the assumption of ceteris paribus makes it easier to formulate economic theory and policy, it also increases the risk of error. If other things do change in significant ways, our predictions (and policies) may fail.

9. **Imperfect Knowledge**
   - It may be impossible to understand and explain how the economy works without getting tangled up in subjective value judgments.
   - It is not clear where the truth lies. For more than 200 years, economists have argued about what makes the economy tick.
   - However, we can acquire an understanding of basic economic principles.

**VIII. The Economy Tomorrow**

A. **Harnessing the Sun**
   1. Solar power is an exciting technology we can use to power our homes and cars in the future.
   2. The full scale development of solar power could cost trillions of dollars. The opportunity costs may be the cure for cancer, AIDS, or the eradication of the flu.
   3. There may also be benefits of the program. Just think how clean the air could become.
   4. Society will ultimately have to make decisions regarding allocating resources to harnessing the energy of the sun.
IN-CLASS DEBATE, EXTENDING THE DEBATE, AND DEBATE PROJECTS

In-class Debate

Do we work too hard?

One constraint in our economy is time. As a society, we make choices about the allocation of time between work and other pursuits. In the US, most workers are eligible for overtime pay if they work more than 40 hours a week, whereas most European workers become eligible at 35 hours per week. In addition, workers in Europe have guaranteed vacation time—five weeks in France—a benefit not available in the US. As a result the typical US worker puts in about 2000 hours per year compared to 1700 hours per year in France and Germany.

Should US laws be changed to require a shorter work week and longer vacation time?

For each side of the question list three strong arguments. Use the following concepts from the chapter at least once.

Production possibilities curve
Economic growth
Market mechanism
Market failure

Teaching notes

Classroom discussion often encourages students to debate one another. Although lively, such discussion usually involves a minority of students. A cooperative controversy ensures that every student is involved in the debate while using a relatively short period of class time. Moreover, it can help students see the arguments on both sides of an issue, often a difficult task for college students. Finally, the technique helps focus on an outcome such as identification of the strongest argument on each side. These outcomes may be useful later, if students are assigned an appropriate essay.

Format: Organize students into groups of two. (Use instructor assignment or random assignment so that friends don’t work together.) One half of the groups take the pro side; the other half takes the con side. Each pair lists the strongest arguments for their position. Then, pairs combine into groups of four, with one pair on each side of the debate. One pair reads their reasons while the other side listens. Then they reverse roles and repeat. Finally, each group of four selects the strongest argument on each side and, if appropriate, reaches a consensus on a final position.

Sample answers:

No
1) A reduction in the work week would shift the production possibilities curve in, reducing the capacity of the economy to produce. Americans value the output that would
be lost more highly than the leisure time they lose by choosing to do it. If that were not the case, they wouldn’t be working those hours.

2) The reduction in production capacity would not just occur in the present. It would also affect the future. If the production possibilities curve shifts in, it seems likely that there will be less consumption goods and less capital goods produced. That will mean slower economic growth in addition to lower production in the present.

3) Government should not further involve itself in regulating hours of work or number of holidays. This is something that ought to be left to the market. To understand why, think about a simple example: suppose that compensation has only two dimensions: wages and paid vacation. Employers compete for workers by offering different mixes of compensation. Some offer higher wages and fewer weeks of paid vacation, others offer lower wages and more weeks of vacation. Workers will go to work for the employers offering the most attractive mix. As a result of this competition for workers, employers have a strong incentive to offer vacation benefits that reflect the preferences of workers.

Yes

1) It is tempting to think that Americans working 2000 hours per year, on average, simply reflects the preference of Americans. But market mechanisms don’t always produce the optimal mix of output; market failures occur. It’s possible that choices made through the market lead to our economy producing less leisure than would be optimal. This might be true, for example, if there were externalities imposed on third parties as a result of long hours of work. For example, maybe children spend many hours in bad day care as a result of their parents working long hours. If parents don’t fully understand the consequences to society, in terms of future aggressive behavior, or if they value the extra income more highly than they value well-socialized children, from society’s point of view they may work too many hours in the market and too few hours caring for their children.

2) To argue that market mechanisms will automatically get employers to offer vacation benefits that reflect worker preferences is to believe too readily in the power of the market. While there are times when employers are competing intently for workers, for many jobs, at many times, workers are in surplus. If the economy is operating inside its production possibilities frontier, for example during a recession, employers are free to think more about what is best for the business and less about getting the mix of wages and weeks of vacation right from the employee’s point of view.

Extending the Debate

Too much for the military—or not enough?

The allocation of resources to the military is a major policy choice for the US. First, find out how much currently is spent on military programs from the Center for Defense Information an independent watchdog on US military spending at:

http://www.cdi.org/

In Washington, DC, research organizations provide information to political leaders regarding the military budget. At the following two sites find three arguments in favor of the current budget level (or increasing it) and three arguments for reducing the current spending level. Select one argument from each side as the most important reason for
increasing/maintaining/reducing military spending. Then write a response to this argument, pointing out its weak points.

The Heritage Foundation is a think tank to promote conservative public policies based on a strong national defense.

http://www.heritage.org/Research

Project on Defense Alternatives is a think tank to promote the broadest range of defense options that will allow significant reductions in the level of armed forces and military spending.

http://www.comw.org/pda/

Teaching notes

Possible student answers:

**Raise the military budget**

1) The Four Percent for Freedom Solution: We should maintain a defense budget of 4 percent of gross domestic product (GDP) over the next five to 10 years or else the U.S. will be unable maintain its forces to secure America. “The Four Percent for Freedom solution would help to reassure financial markets about American strength, reduce risk within the international community, and promote economic growth both at home and abroad.”


2) Army Modernization Is Essential: “The President’s 2008 budget request of $3.7 billion to continue development of the FCS includes $100 million in procurement funding. FCS is the Army’s primary modernization program; this would be the first upgrade of this magnitude in nearly four decades. Given that the Army went to war in Iraq in 2003 with equipment that was already more than 20 years old, FCS is critical not only for future missions but also for soldiers on the battlefield today.”

   http://www.heritage.org/Research/NationalSecurity/wm1621.cfm

**Reduce the military budget**

1) Reducing America’s excess warfare spending can equal major savings. “During the fiscal year 2008, US national defense spending will significantly surpass the $650 billion mark. Since 1998, the nation has allocated about $4.5 trillion to defense adding more than $3 trillion to the gross federal debt - much of it borrowed from social security. Sometime in the middle of the next decade, Social Security will stop generating surplus revenues for use elsewhere, and the period of repaying - rather than borrowing from - the trust funds will begin.”

   http://www.comw.org/pda/0708bm42.html

2) “In February 2007, the Gallup polling organization asked a representative sample of US citizens if they thought the United States was spending too little, too much, or just the right amount on defense and the military... For the first time since the mid-1990s, a plurality of Americans said that the country was spending too much. Currently the Pentagon plans to spend more than $2.75 trillion during the next five years -- not counting the incremental cost of future combat operations. This is not easily reconciled with bringing the national debt under control, while also meeting pending demands on social security and medicare.”

   http://www.comw.org/pda/0703bm41.html
Debate Project

What is economic progress? What is freedom?

Two research organizations rank countries by their economic competitiveness with quite different results.

- Why do they do reach different conclusions?
- Which ranking best describes the state of the world economy?


It describes itself as follows:

The World Economic Forum is an independent international organization committed to improving the state of the world by engaging business, political, academic and other leaders of society to shape global, regional and industry agendas.

Incorporated as a not-for-profit foundation in 1971, and headquartered in Geneva, Switzerland, the Forum is tied to no political, partisan or national interests.

The report on competitiveness is available at:


Another ranking, described in the textbook comes from the Heritage Foundation

http://www.heritage.org/

It describes itself as follows:

Founded in 1973, The Heritage Foundation is a research and educational institute - a think tank - whose mission is to formulate and promote conservative public policies based on the principles of free enterprise, limited government, individual freedom, traditional American values, and a strong national defense.

The report is available at:

http://www.heritage.org/index/Default.aspx
PRINT MEDIA EXERCISE

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Find an article that describes a tradeoff between two goods or services. Use the article you have found to fulfill the following instructions and question.

1. Mount a copy (do not cut up newspapers or magazines) of the article on a letter-sized page. Make sure there is room at the bottom of the article to write the answers to the questions.

2. What are the two goods or services (or groups of goods or services) involved in the tradeoff?
   - Use an arrow to indicate each good or service (or groups of goods or services) in the article. You should draw at least two arrows, but not more than two, in your article.
   - Below the article draw a pair of axes for a production-possibilities curve. Write the name of one of the goods or services on the horizontal axis and the other on the vertical axis.

3. Place brackets around the phrase (not more than a sentence) that indicates that there is a tradeoff between the two goods or services.

4. Are there increasing opportunity costs in the tradeoff between the two goods or services?
   - Under the article write one of the following:
     - Increasing opportunity costs exist.
     - No increasing opportunity costs exist.

5. What would the production-possibilities curve between the two goods or services look like?
   Carefully and neatly, draw a production-possibilities curve for the two goods or services. Don’t use any numbers. Be very careful to draw the correct shape of the production-possibilities curve on the evidence of the applicability or inapplicability of the law of increasing opportunity cost (see your answer in number 4 above).

6. On the basis of information in the article, is there a possible shift of the production-possibilities curve or a movement along it? The shift or movement may have occurred already, may be occurring presently, or may occur in the future. Possibly, the author of the article is implicitly advocating a shift or a movement. Underline the single word, phrase or sentence (not more than a sentence) that indicates a shift or a movement.

7. Use an arrow or your graph to indicate what direction there would be a movement along the production-possibilities curve or in what direction the curve would shift as a result of the event that you have just underlined.

8. In the remaining space below your article, indicate the source (name of newspaper or magazine, title (newspaper headline or magazine article title), date, and page for the article you have chosen. Use this format:

   Source: __________________ Date: ________________ Page: ________________
   Headline: _____________________________________________________
   If this information also appears in the article itself, circle each item.

Professor's Note

Learning Objective for Media Exercise

To test the student's understanding of increasing opportunity cost, the concept of tradeoff, and the difference between shifts of and movements along the production-possibilities curve.

Suggestions for Correcting Media Exercise

1. Check that the items indicated with an arrow correspond to what is on the axes of the production-possibilities curve that the student has drawn.
2. Check for the consistency between the student's drawing of the opportunity cost curve and his or her choice about whether or not there is increasing opportunity cost.
3. Check that the underlined passage indicates a shift or a movement along the production-possibilities curve. Then see if the student has correctly pointed the arrow in the diagram to indicate the shift.

Likely Student Mistakes and Lecture Opportunities

1. There are likely to be many articles about budgetary disputes in Congress. Implicitly, the scarce factor is money, and there would appear to be no applicable law of increasing opportunity cost. The point needs to be made that the production-possibilities curve usually applies to real goods and services with the factors of production such as labor, land, and capital.
2. The students are likely not to have a firm grasp on the difference between shifts of and movements along the production-possibilities curve. This assignment and a short lecture on the issue should clear up the difference quickly.

SUPPLEMENTARY RESOURCES


