CHAPTER 2: ECONOMICS AND BANKING

CHAPTER OPENER

Chapter 2 covers the fundamentals of economics—how business decisions are shaped by supply and demand and the degrees of competition.

This chapter will introduce students to concepts such as:

- the different types of economic systems throughout the world
- how economic indicators such as the gross domestic product (GDP), price indices, the unemployment rate, and productivity reflect the health of an economy
- the four stages of the business cycle
- how the government uses fiscal policy to smooth swings in the business cycle

Finally, students will learn about the money supply, the Federal Reserve Bank, and the tools it uses to stabilize the economy through monetary policy.

DETAILED LECTURE OUTLINE

I. The Basics of Economics

A. Economics Defined
   1. So what is economics?
      a. **Economics** is the study of how individuals and businesses make decisions to best satisfy wants, needs, and desires with limited resources.
      b. There are two basic studies of economics: *microeconomics* and *macroeconomics.*
         i. **Microeconomics** is the study of how individual businesses, households, and consumers make decisions to allocate their limited resources in the exchange of goods and services.
         ii. **Macroeconomics** is the study of the behavior of the overall economy.

B. Economic Systems
   1. What are the different types of economic systems?
      a. An **economy** is a system that tries to balance the available resources of a country, such as land, capital, and labor, against the wants and needs of consumers.
      b. An economy is defined by:
         i. What is produced
         ii. How it is produced
         iii. Who gets the finished product
      c. The world's different economies are classified into three basic economic systems: planned (or controlled) economies, free market economies, and mixed economies (Table 2.1).

C. Planned Economic Systems
   1. In a **planned economic system,** the government plays a significant role in determining the goods and services produced and distributed.

2. **Communism** is an economic system in which a state's government makes all economic decisions and controls all social services, as well as many of the major resources required for the production of goods and services.
3. **Socialism** is a system whereby the government owns or controls many basic businesses and services, and the profits from them are distributed evenly among the people.
    a. The government charges high tax rates to pay for the services it provides.
    b. This economic system may tend to reduce people's motivation to work as hard as they might otherwise.
    c. Many socialist and communist countries are beginning to change their economies into free market economies through **privatization**—the conversion of government-owned production and services to privately owned, profit-seeking enterprises.

D. Market Economies
1. In a **market economy**, individuals are more able to make their own economic decisions.
2. **Capitalism** is an economic system that allows freedom of choice and encourages private ownership of resources required to make and provide goods and services.
3. The production and pricing of goods and services is determined through the operation of a **market**—the mechanism by which buyers and sellers exchange goods and services.

E. Mixed Economies
1. Most economic systems are **mixed economies**—a blend of market and planned economies. See Figure 2.1.

F. Business and Economics
1. Why do business managers need to be concerned with economics?
    a. Businesses need to know how much of their goods to produce or services to offer, as well as how much to charge.
    b. They need to be aware of the potential impact that government decisions and the decisions of collective businesses can have on their individual business.

II. Determining Price: Supply and Demand

A. Definitions
1. **Currency** is a unit of exchange for the transfer of goods and services and provides a consistent standard.
2. The **market price** for a good or service is the price at which everyone who wants the item can get it—without wanting more or without any of the items being left over.

B. Supply
1. What is supply?
    a. **Supply** refers to how much of a product or service is available. It is derived from a producer's desire to maximize profits.
    b. The **law of supply** states that the amount supplied will increase as the price increases; if the price is lower, then less of the product is supplied.

c. A **supply curve** shows the relationship between supply and price.

C. Demand
1. What is demand?
a. **Demand** refers to how much people want to buy at any given time.
b. The amount demanded increases as price declines.
c. A **demand curve** illustrates the relationship between demand and price.

D. Factors That Determine Price
1. What factors determine price?
a. As a price of a product increases, more of it is likely to be supplied.
b. As the price of the produce decreases, more of it is likely to be demanded by customers.
c. If supply exceeds demand, there is a **surplus**.
d. If demand exceeds supply, there is a **shortage**.
e. The price at which supply equals demand is the *market price* or the **equilibrium price** and is illustrated in a supply-and-demand curve.

E. Factors That Affect Demand
1. What other factors besides price affect demand?
a. **Determinants of demand** include:
i. Changes in income levels
a.) When income levels increase, people are able to buy more products.
b.) When income levels decrease, people cut back on spending and buy fewer products.
ii. Population changes
a.) Increases in population create greater demand.
b.) Demographic changes also affect demand for certain goods and services.
iii. Consumer preferences
a.) Demand for a product can change based on what is popular at any given moment.
iv. Complementary goods
a.) Products or services that go with each other and are consumed together, such as apps and iPhones, are considered **complementary goods**.
v. Substitute goods
a.) Goods that can be used in place of other goods, such as Coke for Pepsi, are **substitute goods**.
b. A positive change in any of these shifts the demand curve to the right.
c. A negative change in any of these shifts the demand curve to the left.

F. Factors That Shift Supply
1. What makes supply change?
a. Factors that can create a change in supply are known as **determinants of supply** and include:
i. Technology changes

a.) Improvements in technology enable suppliers to produce goods or services more efficiently and with fewer costs, thus increasing their ability to supply more.

ii. Changes in resource prices

a.) Increases and decreases in the price of the resources used to produce a good or a service affect the cost of their production.

i.) An increase in resource prices increases the cost of production and reduces profits, thus lowering the incentive to supply a product.

iii. Price expectations

a.) The expected future price of a product will affect how much of it producers are willing to supply.

i.) If prices are expected to increase in the future, a supplier might stockpile the product and supply more at a later time when prices are higher.

ii.) If prices are expected to decrease, the supplier might attempt to sell its supply while prices are high.

iv. The number of suppliers

a.) The supply of a good or a service increases as the number of competitors increases.

v. The price of substitute goods

a.) If there are equally comparable goods available at a lower price, the supply of the more expensive good will be affected.

b. Changes in any of these factors can shift the supply curve to the left (negative impact on supply) or to the right (positive impact on supply).

III. Degrees of Competition

A. Monopolies

1. What is a monopoly?

a. A **monopoly** occurs when a provider of a good or service has control of all or nearly all of its market.

2. Why aren't there many monopolies?

a. Without competition, a firm that has a monopoly can charge a higher price and may be less responsive to consumer needs.

b. The U.S. Federal Trade Commission (FTC) and the Department of Justice must review mergers between large competitors to determine whether the combined firm would result in a monopoly that would thwart competition.

c. Natural monopolies (such as utility companies that sell natural gas or water) may be permitted in the United States to conserve natural resources but the government regulates the prices, preventing the companies from overcharging.

B. Duopolies and Oligopolies

1. What happens when one or two other companies enter a monopolistic market?

a. A **duopoly** is where only two suppliers exist, or only two firms dominate a market.

b. An **oligopoly** is a form of competition in which only a few sellers exist and each seller has a fairly large share of the market.

C. Monopolistic Competition

1. What happens when there isn't much differentiation between products?
   a. **Monopolistic competition** occurs when there are many buyers and sellers and the products are similar but not identical.
   b. Often there is a *perceived* difference among consumers so the products are not perfectly substitutable products.

D. Perfect Competition

1. What happens when products are almost identical?
   a. **Perfect competition** occurs when there are many buyers and sellers of products that are virtually identical and any seller can easily enter and exit the market.
   b. No single supplier can influence the price.

IV. Economic Indicators

A. Definitions

1. Business managers need to be aware of certain statistics about economic activities, called **economic indicators**.
   a. *Leading indicators* are statistics that can be used to help predict how the economy will do in the near future.
   b. *Coincident indicators* are statistics that reflect how the economy is currently doing.
   c. *Lagging indicators* are statistics that change only after the economy as a whole changes.
2. The gross domestic product, consumer and producer price indices, and the unemployment rate are three economic indicators closely watched by businesspeople.

B. The Gross Domestic Product

1. How do we determine the health of an economy?
   a. The broadest measure of the health of any country's economy is its **gross domestic product (GDP)**, which measures how productive a nation is; that is, the overall market value of final goods and services produced in a country in a year.
   b. Only those goods that are actually *produced* in the country are counted in the country's GDP.
2. How does the GDP act as an economic indicator?
   a. A rising GDP indicates that more goods and services are being produced and that businesses are doing well.
   b. A downward-moving GDP indicates that fewer goods are being produced, fewer services are being sold, and businesses are not doing as well.
   c. A nation's GDP is often viewed in tandem with the country's debt level.
      i. A low debt-to-GDP ratio indicates an economy that is healthy.
      ii. A high debt-to-GDP ratio indicates a country that is spending beyond its means.

C. Consumer and Producer Price Indices

1. What else is used to gauge the health of an economy?
    a. There are two price indices used as economic indicators: the consumer price index and the producer price index.
    b. A consistent increase in either indicator indicates inflation.
        i. **Inflation** is a rise in the general level of prices over time.
        ii. A decrease in the rate of inflation is **disinflation**.
        iii. A continuous decrease in prices over time is **deflation**.
2. How are changes in the price of consumer products measured?
    a. The **consumer price index (CPI)** tracks changes in prices over time by measuring changes in prices of goods in services that consumers purchase.
    b. It is a lagging indicator, so it shifts after the economy changes.
    c. The CPI measures price changes by creating a "market basket" of a specific set of goods and services that represent the average buying pattern of urban households.
3. What goods and services are included in the CPI?
    a. The expenditure items fall into eight major groups: apparel, education and communication, food and beverages, housing, medical care, recreation, transportation, and other goods and services (Figure 2.8).
4. Does the CPI measure the change in price of all goods?
    a. The CPI measures the change in prices of consumer goods only.
    b. The **producer price index (PPI)** tracks the average change in prices at the wholesale level.
        i. It tracks the prices of goods sellers use to create products, such as raw materials, product components that require further processing, and finished goods sold to retailers.
5. Why are price indices important?
    a. They measure purchasing power and consequently trigger business decisions.
    b. During periods of increasing prices, consumers' purchasing power decreases.
        i. As a result, wages increase to compensate for the higher cost of living, and businesses must eventually increase the prices of their products to offset higher labor costs, again decreasing the consumer's purchasing power.

D. The Unemployment Rate
1. What other indicators are used to measure the economy?
    a. The **unemployment rate** measures the number of workers who are at least 16 years old, are not working, and who have tried to find jobs within the past four weeks.
    b. There are different measurements of unemployment:
        i. **Frictional unemployment** is temporary unemployment that results when workers move among jobs, careers, and locations.
        ii. **Structural unemployment** is permanent unemployment that occurs when an industry changes and jobs are terminated completely.
        iii. **Cyclical unemployment** occurs when firms must cut back their workforces when there is a downturn in the business cycle.

iv. **Seasonal unemployment** occurs when workers get laid off during the off-season or after the holiday shopping season ends.

2. Why is unemployment an important economic measure?
   a. High unemployment results in an increase in unemployment benefits and government spending on social programs such as welfare.
   b. If the unemployment drops too low, more workers have increased buying power and spend more, causing prices to rise and resulting in inflation.

E. Productivity of Firms
1. How is the productivity of a firm's workforce measured?
   a. **Productivity** measures the quantity of goods and services that a firm's human and physical resources can produce in a given time period.
2. Why is measuring productivity important to businesses?
   a. An increase in productivity indicates that workers are producing more goods or services in the same amount of time, often resulting in lower costs and lower prices.

V. Government and the Economy

A. Economic Policies
1. Why does the state of the economy change?
   a. Over time, the economy naturally goes through periodic increases and decreases, called the **business cycle**. There are four stages (Figure 2.9):
      i. **Peak** occurs when an economic expansion is at its most robust point.
      ii. **Recession** is a decline in the GDP for two or more successive quarters. A very severe or long recession is a **depression**.
      iii. A **trough** occurs when the recession hits bottom and the economy begins to expand again.
      iv. **Expansion** or **recovery** refers to the phase when the economy begins to grow again and enters into an expansionary or recovery phase. Eventually the recovery will hit a peak and the cycle begins again.
2. How does the government control swings in the business cycle?
   a. To smooth out the swings in the business cycle, lawmakers use **fiscal policy** to determine the appropriate level of taxes and government spending.

B. Fiscal Policy
1. Why does the government increase taxes to influence the economy?
   a. Tax increases mean consumers spend less, which slows down the growth of businesses and the economy by reducing the amount of money in the system, and this lowers inflation.
   b. Decreasing taxes does not have the opposite effect because the amount of money entering the system depends on how much of the reduction in taxes consumers spend and how much they save.
2. How does government spending help stimulate the economy?
   a. The government spends money on a wide variety of projects, such as infrastructure improvements and projects that benefit the military, education, and health.

b. This increases the cash flow in the economy faster than decreasing taxes does and also creates additional jobs, which also helps stimulate the economy.

C. Monetary Policy
1. What else can be done to control the economy?
a. The second tool to manage the economy is **monetary policy**, which is exercised by the **Federal Reserve System (the Fed)**, the central banking system of the United States.
i. It includes 12 regional Federal Reserve Banks, a Board of Governors, and the **Federal Open Market Committee**, which sets the policies of the Fed.
ii. Through its monetary policy, the Fed affects the nation's money supply and helps shape the direction of the economy.
2. What is the money supply?
a. The **money supply** is the combined amount of money available within an economy.
b. There are different components to the money supply (see Figure 2.11):
i. **M-1:** Coins and bills (currency), traveler's checks, and checking accounts. These are the most liquid assets.
ii. **M-2:** M-1 plus savings deposits, money market accounts, and certificates of deposit (CDs) less than $100,000.
iii. **M-3:** M-1, M-2, and less liquid funds such as larger CDs, money market accounts held by large banks and corporations, and U.S. dollars deposited in banks outside the United States.
3. Why is the money supply important?
a. The more money we have, the more we tend to spend.
b. As consumers spend more, businesses do better, increasing demand for resources, labor, and capital, and the economy improves.
c. However, when the money supply continues to expand, there may not be enough goods and services to satisfy demand and it may result in inflation.
d. When the economy begins to slow down due to decreased spending, either disinflation or deflation results.
e. The Fed uses three tools to affect money supply: reserve requirements, short-term interest rates, and open market operations.

D. Reserve Requirements
1. What are reserve requirements?
a. The **reserve requirement**, determined by the Fed, is the minimum amount of money banks must hold in reserve to cover deposits.
b. The Fed can ease or tighten the money supply by increasing or decreasing the reserve requirement.
i. If the Fed increases the reserve requirement, it forces banks to hold on to more money rather than lending it out, slowing down economic activity.
c. The Fed rarely uses the reserve requirement as a means of monetary policy.

E. Short-Term Interest Rates

1. What is the discount rate?
    a. When commercial banks borrow funds from the Fed, they are charged an interest rate called the **discount rate**.
    b. The Fed has the power to increase or decrease the discount rate in its efforts to control money supply.
        i. When the Fed lowers the discount rate, commercial banks are encouraged to obtain additional reserves by borrowing funds from the Fed and then lending those reserves to businesses, thereby stimulating the economy.
        ii. When the Fed increases the discount rate, it discourages banks from borrowing additional reserves and lending to businesses.
2. Is the discount rate the same as the federal funds rate?
    a. The **federal funds rate** is the interest rate that banks charge other banks when they borrow funds overnight from one another.
    b. The Fed does not control the federal funds rate directly. The rate is the equilibrium price created through the Fed's open market operations and the exchange of securities.
        i. The excess reserves that are available to lend among banks come from securities that the Fed buys and sells through its open market operations.
            a.) To increase the federal funds rate, the Fed sells bonds in the open market, and banks buy the securities, reducing their excess reserves available for loans.
            b.) To decrease the federal funds rate, the Fed buys bonds in the open market, increasing banks' excess reserves and making more money available.

F. Open Market Operations
1. What are open market operations?
    a. The primary tools the Fed uses in its monetary policy are **open market operations**, buying and selling U.S. Treasury and federal agency bonds on the "open market."
    b. When the Fed buys or sells U.S. securities, it is changing the level of monetary reserves in the banking system by adding or taking away money from the system.

NOTE: End the lecture by asking students to write down the muddiest points or main points of the lecture. This will allow you to know what might need to be reviewed during the next lecture.

SUPPLEMENTAL ACTIVITIES

Supplemental In-Class Activity
Comparing Economic Systems

Activity Overview: This activity gets students talking about how similar and different the U.S. economic system is to other systems.

Time Limit: 30 minutes

What to Do:

1. Divide the class into small groups. Ask the groups to assume they have just overheard a classmate say, "The United States is becoming more socialist every day—with all the government control." Have each group list reasons why the statement could be true and reasons why the statement could be false. (15 minutes)

2. Reassemble the class and discuss each group's thoughts. (15 minutes)

Don't Forget: Remind students that a government's level of control distinguishes capitalism from socialism. If you have foreign students in your class, you may want them to say a bit about the economic system in their native country.

Wrap-Up: Wrap up the discussion by reminding students that the U.S. economic system and a socialist system share some similarities and many differences. For example, workers in socialist economies often work fewer hours, have longer vacations, and receive more health, education, and child-care benefits than do workers in capitalist economies. On the other hand, the federal government does control some basic services in the United States as well as various aspects of the market through agencies, such as the Food and Drug Administration (FDA) and the Federal Communication Commission (FCC).

Supplemental Homework Activity
Let's Go Shopping!

Homework Assignment: Visit a local shopping mall or shopping area. List each store that you see and determine what degree of competition it faces in its immediate environment. For example, if there is only one store in the mall that sells shoes, that store represents a monopoly. Note those businesses with direct competitors (e.g., two jewelry stores) and show how they compete with one another.

Deliverable: A brief paper reporting on degrees of competition and the tactics stores use to compete with one another. Answers will vary, but students should recognize different levels of competition and how stores respond to competition by advertising, reducing prices, and so on.

At-Home Completion Time: 1 to 2 hours.

ENHANCING THE ONLINE COURSE

Online Lecture: Define the terms *microeconomics* and *macroeconomics* and use examples to distinguish between the two disciplines. Video tape yourself giving the short "mini-lecture." Many institutions have video cameras for your use in the library or you can use a digital camera with the help of another professor. Load the short video online (using procedures as specified by your online platform). Have your students watch the short video and do a quiz afterward.

Economics Model Search: Ask students to search the Internet to illustrate each of the boxes in Table 2.1. Require students to develop and send in a table with graphics and examples in each of the cells to illustrate the differences among the systems of economics.

Create a Model: Ask your students to use photos or other graphics to show the relationship of supply and demand. Limit the written discussion (in words) to one page to be e-mailed back to the discussion board. Ask the students to relate the content of their responses to current events posted on the Internet.

Price Points: Require your students to check the prices of products for three weeks in a row (suggested products: bread, eggs, chicken, tomatoes, milk, oranges, coffee, potato chips, gasoline). What could account for the changes in price? Ask your students to report back on the findings of their "study," to analyze the price differences, and, using the information in the text, to develop some ideas about what has caused the price differences. Students can post the reports via the discussion board.

ANSWERS TO END-OF-CHAPTER MATERIALS

Self Test

Multiple Choice

2-1 Which of the following is a good example of microeconomics?
a. How a specific company would maximize its production and capacity so it could better compete in its industry
Learning Objective 2-1: The Basics of Economics
ACSB: Analytical thinking

2-2 There are four coffee shops in your town. All of them claim to have the "freshest tasting coffee." Each shop advertises the unique benefits of its coffee and prices. This is an example of
d. an oligopoly.
Learning Objective 2-3: Degrees of Competition
AACSB: Analytical thinking

2-3 Jeannette has a successful organic spa business in which she gives massages, facials, and organic body treatments. Last summer, another organic spa opened up in town. The supply curve for Jeanette's business would shift in which direction?
a. To the right
Learning Objective 2-2: Determining Price: Supply and Demand
AACSB: Application of knowledge

2-4 Which of the following is a determinant of demand?
c. Price of substitute goods
Learning Objective 2-2: Determining Price: Supply and Demand
AACSB: Application of knowledge

2-5 Racerback Swimwear, an Australian company, opens a factory near Tallahassee, Florida. The value of the swimsuits produced in the new Florida factory is included in which country's GDP?
b. United States
Learning Objective 2-4: Economic Indicators
AACSB: Application of knowledge

2-6 Which of the following tracks the prices of goods and resources sellers use to create their products?
b. CPI
Learning Objective 2-4: Economic Indicators
AACSB: Application of knowledge

2-7 Jackson Paulson works as a waterskiing instructor at Migis Lodge on Sebago

Lake. He claims unemployment from October through April. Jackson experiences which type of unemployment?
b. Seasonal
Learning Objective 2-4: Economic Indicators
AACSB: Application of knowledge

2-8 Which of the following is an example of the government's fiscal policy to stimulate an economy?
a. Increased government spending
Learning Objective 2-5 Government and the Economy
AACSB: Application of knowledge

2-9 What results when there is an increase in overall prices?
a. Inflation
Learning Objective 2-4: Economic Indicators
AACSB: Application of knowledge

2-10 At which point in the business cycle is the economy when GDP declines for two or more successive quarters?
b. Recession
Learning Objective 2-5: Government and the Economy
AACSB: Analytical thinking

True/False

2-11 Microeconomics is the study of the behavior of the overall economy.
☐ **False**
Learning Objective 2-1: The Basics of Economics
AACSB: Analytical thinking

2-12 The discount rate is what is charged when banks borrow emergency funds from each other.
☐ **False**
Learning Objective 2-5: Government and the Economy
AACSB: Analytical thinking

2-13 Sweden, with its high taxes and widespread government programs, is a good example of a market economy.
☐ **False**
Learning Objective 2-1: The Basics of Economics
AACSB: Analytical thinking

2-14 To celebrate the first day of summer, an ice cream shop dropped the price of its cones to 10 cents and sold out of them within two hours. This created a shortage of ice cream cones.
☐ **True**
Learning Objective 2-2: Determining Price: Supply and Demand

AACSB: Application of knowledge

2-15 The M-1 money supply measure consists of currency, traveler's checks, and checking accounts.
☐ **True**
Learning Objective 2-5: Government and the Economy
AACSB: Analytical thinking

Critical Thinking Questions: Suggested Answers

2-16 Both monetary and fiscal policy are used to stimulate economic growth or control inflation.

Monetary policy is carried out by the Federal Reserve System (the Fed), and it involves controlling the supply of money. The Fed has three tools with which it can do this:

- The reserve requirement involves raising or lowering the percentage of commercial bank's checking and savings accounts that they must keep in the bank as cash.
  - To increase the money supply, the Fed would lower the reserve requirement.
  - To decrease the money supply, the Fed would increase the reserve requirement.
- Open market operations consist of the buying and selling of government bonds.
  - To increase the money supply, the Fed buys government bonds from individuals, corporations, or organizations that are willing to sell.
  - To decrease the money supply, the Fed sells government bonds.
- The discount rate is the interest rate that the Fed charges for loans to its member banks.
  - To increase the money supply, the Fed would lower the discount rate, encouraging banks to borrow money and thereby increasing the funds they have available for loans.
  - To decrease the money supply, the Fed would increase the discount rate, discouraging banks from borrowing money and thereby reducing the funds they have available for loans.

Fiscal policy refers to the federal government's efforts to stabilize the economy. The government can do this in one of two ways:

- Taxation
  - When the government wants to slow down inflation, it can increase taxes. A tax increase means that consumers have less money to spend. This in turn slows the growth of businesses, because they have to produce less, and consequently slows down the economy.

- Although decreasing taxes conceptually gives consumers more money to spend, it does not have the same direct effect because consumers may choose to save the money rather than spend it.

- Fiscal spending
  - To simulate the economy, the government spends money on a wide variety of projects, such as infrastructure improvements (highways, bridges, etc.) and other projects that benefit the military, education, and health care. This creates additional jobs, puts money into consumers' hands, and stimulates spending.

    Learning Objective 2-5: Government and the Economy
    AACSB: Application of knowledge

2-17 Answers will vary regarding the privatization of the U.S. Postal Service and Amtrak. Some of the points the students should consider are:

Pros
1. Privatization can be an effective way to fund critical infrastructure needs.
2. Privatization can provide a source of immediate revenue for strained public budgets.
3. Private infrastructure funds are an attractive investment vehicle for certain investors, making infrastructure privatization appealing to potential bidders.
4. Historically low interest rates enable private firms to make highly leveraged infrastructure investments.
5. Because the private sector can often deliver greater efficiencies than government, privatization can result in better service at lower cost
6. Privatization can be a politically expedient solution to public problems.

Cons
1. Privatization constrains future options.
2. Privatization may have social implications, adversely affecting certain groups.
3. Stealing from the future? Privatization deals typically generate huge cash windfalls in the present in exchange for revenue streams that would otherwise accrue to citizens in the future.
4. Privatization may result in an undervalued deal.
5. Private entities may fail to fulfill contractual obligations.
6. A lack of public input.

1.1.1 The Pros & Cons of Privatization | Government Finance Officers ...
www.gfoa.org/**pros-cons-privatization** Date Published: June 2011

Learning Objective 2-5: Government and the Economy
AACSB: Application of knowledge

2-18. Answers will vary with some students arguing that the definition of GDP should be changed but most students will probably argue that the current definition is sufficient recognizing that whatever definition that is used will be criticized by somebody. The value of the current definition is the consistency when comparing various economies.

Learning Objective 2-4: Economic Indicators
AACSB: Application of knowledge

Team Time
The Great Debate

2-19 Answers will vary. However, the point of the exercise is to help students understand the process of monetary regulation and to discuss who has a right to regulate how money flows in the U.S. economy.

Learning Objective 2-5: Government and the Economy
AACSB: Application of knowledge

2-20 Answers will vary. However, the point of the exercise is to help students understand the process of monetary regulation and to discuss who has a right to regulate how money flows into the U.S. economy.

Learning Objective 2-5: Government and the Economy
AACSB: Application of knowledge

2-21 Answers will vary. However, the point of the exercise is to help students understand the process of monetary regulation and to discuss who has a right to regulate how money flows into the U.S. economy.

Learning Objective 2-5: Government and the Economy
AACSB: Application of knowledge

Ethics and Corporate Social Responsibility
Economic Inequality

Answers to questions 2-22, 2-23, 2-24, and 2-25 will vary. However, be sure to have students consider how the type of economy in which they are currently living (capitalism) influences their answers to this question. Would students living in a planned economy, such as communism or socialism, answer the questions in the same way?

Learning Objective 2-1: The Basics of Economics
AACSB: Application of knowledge

Web Exercises
2-26 Getting Acquainted with Your Local Federal Reserve Bank
The Federal Reserve Banks are: Boston, New York, Philadelphia, Cleveland, Richmond, Atlanta, Chicago, St. Louis, Minneapolis, Kansas City, Dallas, and San Francisco. Students' answers will vary, depending upon the Federal Reserve Bank selected and the latest news/policies on its website.

Learning Objective 2-5: Government and the Economy
AACSB: Application of knowledge

2-27 AT&T and Antitrust Regulations
Students' answers will vary, depending on their personal experience with the communications industry and their opinions regarding the government's intervention in breaking up the AT&T monopoly.

Learning Objective 2-3: Degrees of Competition
AACSB: Application of knowledge

2-28 Learning More About Supply and Demand
Students' answers will vary, depending on their experience with the game. The game puts students in the position of being the inventor of a new product and walks them through decisions such as determining demand and supply, plotting demand and supply curves, whether shortages or surpluses exist at certain price points, if other goods are complementary or substitute, and how certain factors will cause shifts in the demand and supply curve. Answers should reflect these concepts.

Learning Objective 2-2: Determining Price: Supply and Demand
AACSB: Application of knowledge

2-29 Pro Sports and the Economy
Students' answers will vary, depending on their experience with the game. The game is divided into nine "innings" and each inning examines a different issue, such as how the pro sports market evolved, how leagues gained market power, why athletes earn as much as they do, the sources of pro sports revenue, why tickets cost so much, why there is such a high level of economic conflict in modern pro sports, and the globalization of pro sports. Reference the Teacher's Guide for the game at
http://www.bostonfed.org/peanuts/teacher/guide.htm

Learning Objective 2-2: Determining Price: Supply and Demand
AACSB: Application of knowledge

5. Monetary Policy: You're in Control
Students' answers will vary, depending on their experience with the game. The game asks students to take charge of a simulated economy and make decisions about adjusting the federal funds rate every three months for the next four years. As they make decisions, they will see the resulting effects on inflation and unemployment, and they will also be asked to react to other events (such as oil shortages) that affect the economy.

Learning Objective 2-5: Government and the Economy
AACSB: Application of knowledge

MyBizLab: Suggested Answers

2-31 Answers will vary but students should focus on the shift in the supply curve based on an increase in the number of competitors.

Learning Objective 2-2: Determining Price: Supply and Demand
AACSB: Application of knowledge

2-32 Answers will vary. This question gives students and opportunity to focus on macroeconomic outcomes and the role that government plays in the economy.

Learning Objective 2-5: Government and the Economy
AACSB: Application of knowledge