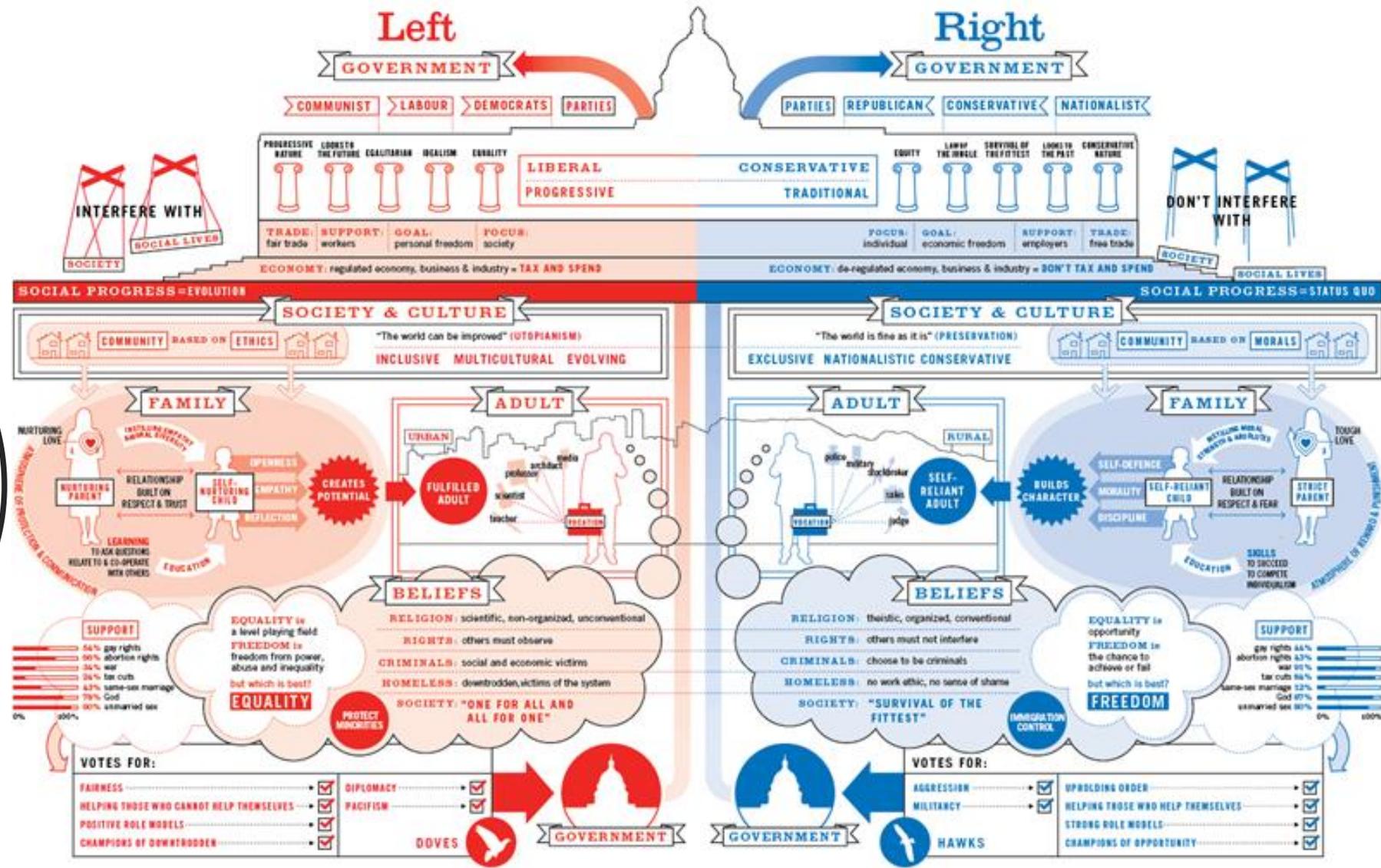


Your political views?





3 QUESTIONS ANSWERED BY THE ECONOMY

- 1) What, and how much, to produce?
- 2) How to produce?
- 3) For whom to produce?
- Your opinions about how we should answer these questions form the economic part of your political views.



Principle #6: Markets are usually a good way to organize economic activity., p.9

Principle #6:
Markets are
usually a good
way to
organize
economic
activity.
p.9

- Market Economy – allocates resources through the decentralized decisions of many firms and households as they interact in markets for goods and services.
- Key assumptions
 - Private property rights
 - Self-Interest Motivates

How a Market Economy Answers the 3 Big ?s

- 1. What and how much to produce
 - Market – what people are willing and able to buy
 - Consumer Sovereignty
- 2. How to produce
 - Private Enterprise
 - Goal – maximize profit
 - Efficiency?
 - Hard budget constraint
- 3. For whom to produce
 - share of economic “pie” based on inheritance, ability, and effort
 - Equality? Equity?



A MARKET-based economy does
not imply the absence of
GOVERNMENT.

- Markets answer 3 economic ?s, but government is needed to:
 - Protect private property rights
 - Support law enforcement and a judicial system
 - Acts as referee for market activity

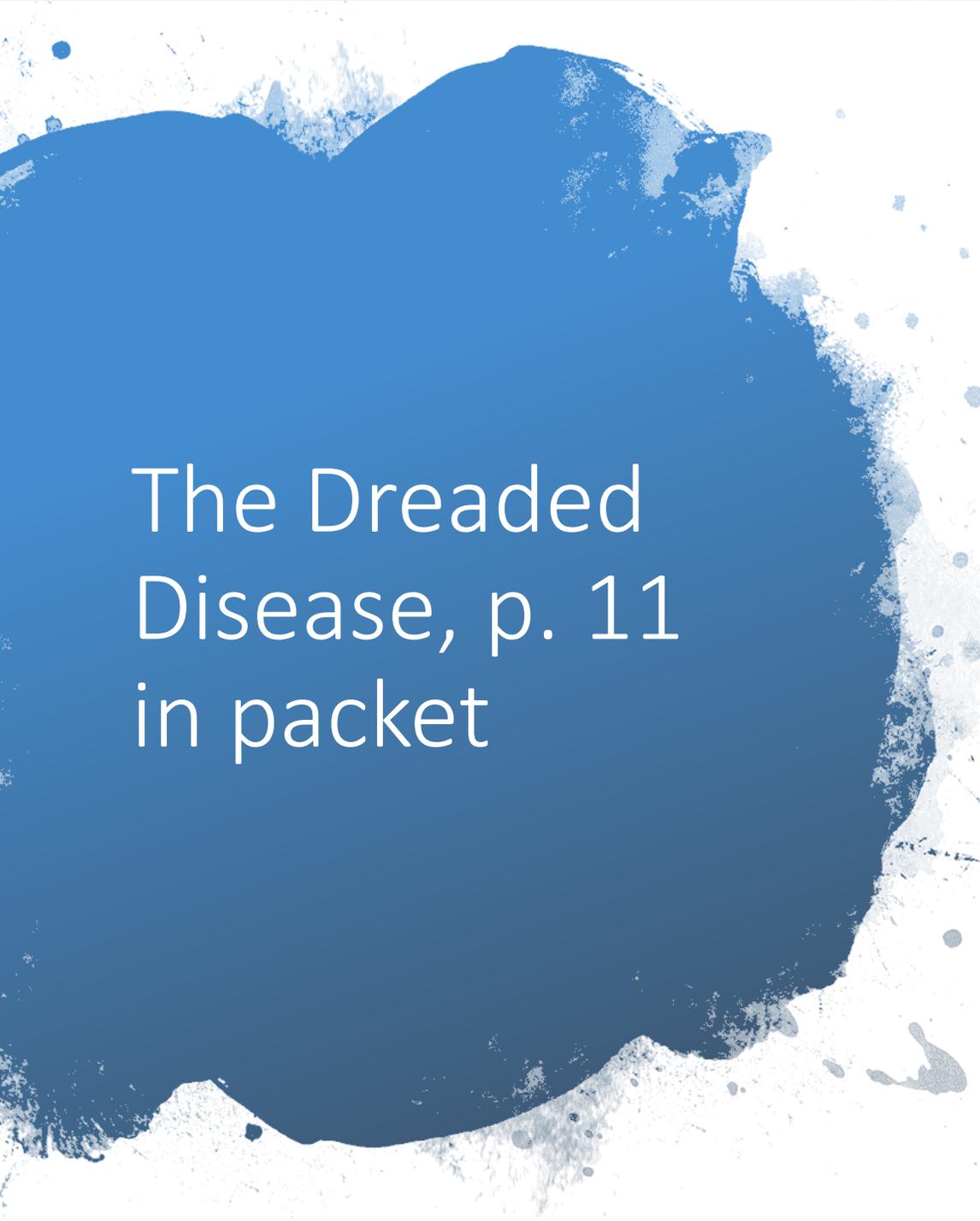
Another way to
organize economic
activity
p.10

Command Economy-
an economy in which
production,
investment, prices,
and incomes are
determined centrally
by a government.

- Key Assumptions:
 - Communal resource ownership, common property rights
 - Significant government intervention and control
 - Goodwill toward community motivates

How a
Command-
oriented
Economy
Answers the 3
Big ?s

- 1. What and how much to produce
 - What government deems necessary
- 2. How to produce
 - Central planner determines
 - State-owned enterprise
 - Soft budget constraint
 - Typically less “efficient” than market
- 3. For whom to produce
 - share economic “pie” equally (“equity”)



The Dreaded Disease, p. 11 in packet

Imagine an island economy that is periodically struck by an epidemic disease that affects only children. From past experience, the islanders found that the disease strikes randomly, affecting 80% of all children. They also discovered a preventive antidote that reduces the chance of death if it is taken before the disease strikes. A child who has taken no doses of the antidote has a 90% chance of dying when he or she contracts the disease. With one dose of the antidote, the chance of death is reduced to 10%. Two doses reduce the chance to 8%; three doses reduce the chance to 6%; four doses reduce the chance to 5%. Beyond four doses, the antidote has no further effect, and the chance of death remains at 5%. Suppose the island has 1,000 children and that at the first sign of a new outbreak of the dreaded disease, the people have produced 1,000 doses of the antidote. The antidote must be used immediately if the children's lives are to be saved.

The Dreaded Disease Group Activity



- a) What would be the market solution to this problem if the island economy operated as a pure market economy?
- b) What would be a command solution to this problem if the island operated in this fashion?
- c) Suppose that only 200 doses are available. What might the command economy solution be in this case?

IClicker –
REEF POLLING



In class quiz #3



1. What would be the market solution to this problem if the island economy operated as a pure market economy?

- A. Every child would get one dose of medicine.
- B. Children from families with high incomes might get multiple doses of medicine while children from lower income families might not get any medicine.
- C. All male children will get a dose of medicine, but female children will not get medicine.
- D. Children under the age of 6 will get two doses of medicine each, but children over the age of 6 will not get a dose of medicine.

2. If this economy operated as a pure command economy, what is the most likely allocation of medicine?

- A. Every child would get one dose of medicine.
- B. Children from families with high incomes might get multiple doses of medicine while children from lower income families might not get any medicine.

The Dreaded Disease, p. 11

- **c) Suppose that only 200 doses are available. What might the command economy solution be in this case?**



All economies are “mixed”

Economic Transition

Governments remaining command-oriented

(China, Laos, Vietnam – market-oriented)

(North Korea, Cuba – less market-oriented)

As you think about the pros and cons of both market-oriented and command-oriented economies – that forms your economic/ political views.

Dmitri



Seeing the Invisible Hand
from Outer Space



- A. A market-oriented economy
- B. A command-oriented economy
- C. A baking-oriented economy

Which type of economic system is most likely to strive to ensure that everyone in the economy gets an equal size piece of the “economic pie?”



Principle #7:
Governments can
sometimes
improve market
outcomes, p.12

- When government intervenes in market:
- **REGULATE** and **MANDATE**



Government corrections
and market failure

- Market Failure: Market fails to allocate resources efficiently.
- Due to things like
 - externalities
 - lack of information
 - concentrated market power

Chapter 1
Macroeconomic
Principles of Economics
How the Economy Works
as a Whole, p.13

- Principle #8: A country's standard of living depends on its ability to produce goods and services
- Principle #9: Prices rise when the government prints too much money
- Principle #10: Society faces a short-run trade-off between inflation and unemployment
- We will not study principles #9 and #10 in ECO201

Chapter 2

Thinking Like an
Economist and
Review of Graphing

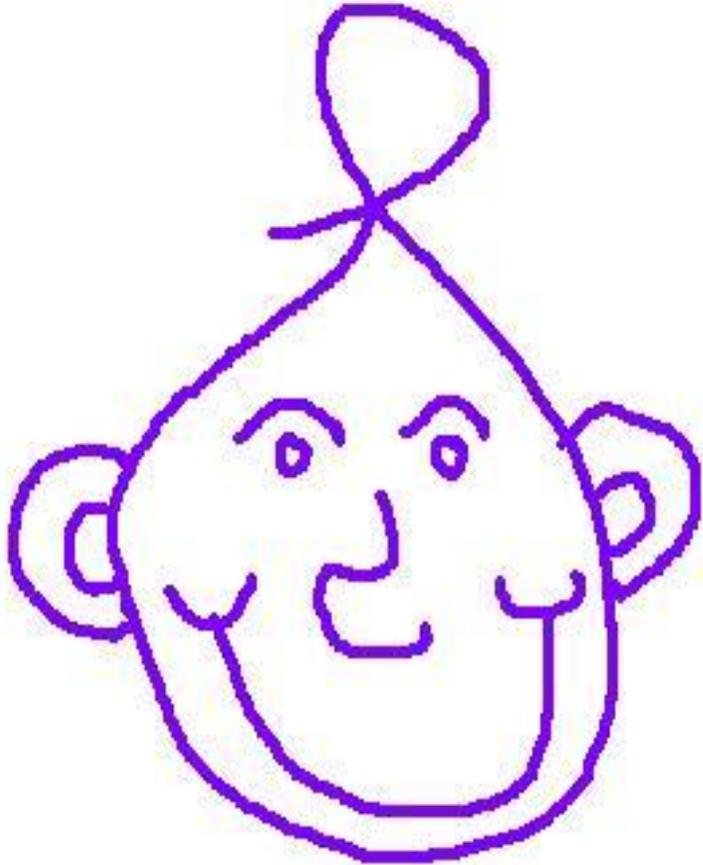
I. The Economist as Scientist and Policy Analyst, p.19

- Develop an economic theory
- Observe to test the theory
- Gather and analyze data

Theory: Workplace drug testing reduces the amount of employee drug use.



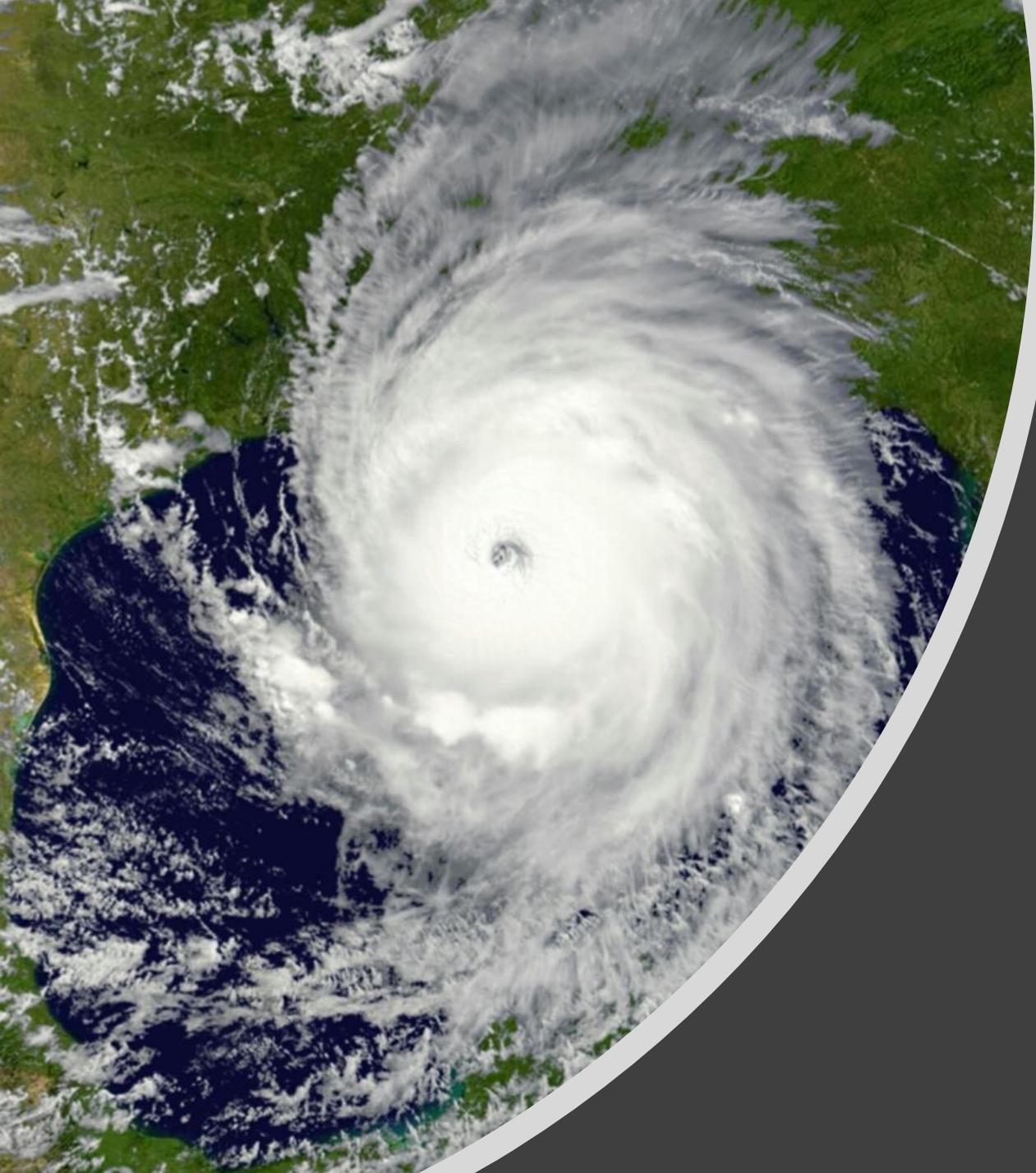
Economic Models: We use simple abstract models to study larger, more complex concepts



Assumptions:

Models often involve simplifying assumptions.

Models of Production



Positive Statement:

A statement that can be tested, proven or disproven.

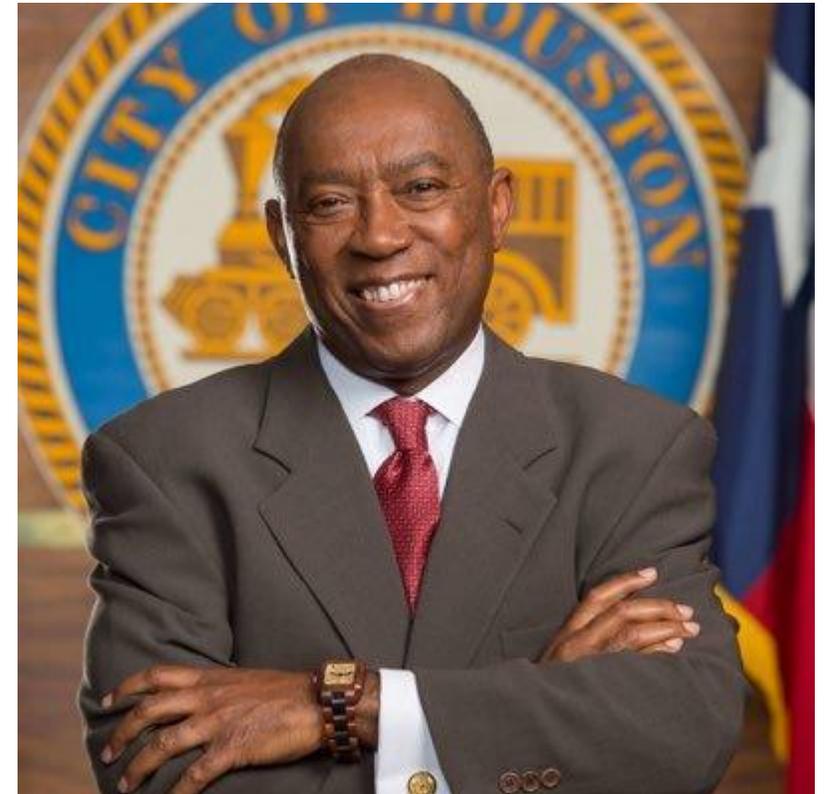
“Hurricane Harvey caused 55 billion dollars in damage.”



- **Example: “The Mayor’s evacuation order for Houston was handled properly.”**

Normative Statement

- A statement of opinion, cannot be proven or disproven.
(key words: ought, should, good, bad)



Sylvester Turner – Houston Mayor

The Art of Economics

Policy Analyzing Precautions, p. 19

- 1. Good policy intentions don't necessarily generate good policy outcomes.
- 2. Anticipate potential secondary effects or unintended consequences of policy.
- 3. Economists may not agree on the best policy in a given situation. (i.e. tax reform)

The National Flood Insurance Program Provides heavily subsidized flood insurance to homeowners in high risk areas.



Insurance intended to help homeowners after disaster but unintended consequence is to encourage people to build in high risk areas.

IClicker –
REEF POLLING



In class quiz #3



Which of the following is an example of a *normative* question?



A. How will an increase in the price of diesel fuel affect truck drivers?



B. What fraction of an income-tax rebate check will be spent on consumer goods?



C. Should the government provide free prescription drugs to lower-income citizens?



D. How will an increase in the minimum wage affect migrant workers?