CHAPTER 15

Planning Guide

Key to Ability Levels	
BL Below level	AL Above level
OL On level	ELL English Language Learners

Key to Teaching Resources	
Print Material	DVD
CD-Rom	Transparency

Levels				Resources		Chapter Opener	Section 1	Section 2	Section 3	Chapter Assess
BL	OL	AL	ELL							
FOCUS										
BL	OL	AL	ELL	Transparency	Daily Focus Skills Transparencies		55	77	63, 78, 79	
TEACH										
BL	OL		ELL	Print Material	Guided Reading Activities*		p. 43	p. 44	p. 45	
BL	OL	AL	ELL	Print Material	Economic Content Vocabulary Activities*		p. 15	p. 15	p. 15	
	OL	AL		Print Material	Critical Thinking Activities			pp. 21, 23	p. 23	
BL	OL		ELL	Print Material	Reading Essentials and Note-Taking Guide*		p. 127	p. 130	p. 133	
		AL		Print Material	Enrichment Activities			p. 15		
	OL	AL		Print Material	Free Enterprise Activities			p. 21		
BL	OL	AL	ELL	Transparency	Economic Concepts Transparencies, Strategies, and Activities		pp. 27, 29	p. 37	p. 35	
BL	OL		ELL	Print Material	High School Reading in the Content Area Strategies and Activities	✓	✓	✓	✓	✓
BL	OL	AL	ELL	Transparency	High School Writing Process Transparencies	✓	✓	✓	✓	✓
BL	OL	AL	ELL	Print Material	Writer's Guidebook	✓	✓	✓	✓	✓
BL	OL	AL	ELL	CD-Rom	StudentWorks Plus CD-ROM	✓	✓	✓	✓	✓
BL	OL	AL	ELL	CD-Rom	Vocabulary PuzzleMaker CD-ROM	✓	✓	✓	✓	✓

*Also available in Spanish

TeacherWorks Plus
All-In-One Planner and Resource Center

- Interactive Lesson Planner
- Interactive Teacher Edition
- Fully editable blackline masters
- Economics & You videos
- Differentiated Lesson Plans
- Printable reports of daily assignments
- Standards tracking system

Levels				Resources	Chapter Opener	Section 1	Section 2	Section 3	Chapter Assess
BL	OL	AL	ELL						
TEACH *(continued)*									
BL	OL	AL	ELL	**Economics & You Video Program DVD—*Economic Growth and Stability***	✓	✓	✓	✓	✓
BL	OL	AL	ELL	**Graph Coach CD-ROM**	✓	✓	✓	✓	✓
Teacher Resources				**Differentiated Instruction Strategies**	✓	✓	✓	✓	✓
				Success with English Learners	✓	✓	✓	✓	✓
				Presentation Plus! CD-ROM	✓	✓	✓	✓	✓
ASSESS									
BL	OL	AL	ELL	**Section Quizzes and Chapter Tests**		p. 185	p. 186	p. 187	pp. 189, 193
BL	OL	AL	ELL	**Authentic Assessment Strategies and Activities**			pp. 20, 21	p. 20	
BL	OL	AL	ELL	***ExamView® Assessment Suite* CD-ROM**		15-1	15-2	15-3	Ch. 15
BL	OL	AL	ELL	**Interactive Tutor Self-Assessment CD-ROM**		15-1	15-2	15-3	
CLOSE									
BL			ELL	**Reteaching Activities***		p. 15	p. 15	p. 15	
BL	OL		ELL	**Reading and Study Skills Foldables**		p. 61	p. 61	pp. 61, 62	

*Also available in Spanish

Activity Using Puzzlemaker™ 3.1

Online Jumble Puzzles

Technology Product

Glencoe's Vocabulary PuzzleMaker™ 3.1 CD-ROM is an easy-to-use program that lets you create your own puzzles based on the glossary for classroom use. The PuzzleMaker allows you to

- create jumble puzzles based on content vocabulary and academic vocabulary that is specific to what is taught in the classroom;
- create online (LAN-based, or local area network) or paper jumble puzzles.

Objectives

After students complete the jumble puzzles, they will be able to

- recall and identify scrambled terms with the help of clues;
- reinforce their understanding of the vocabulary.

Steps

- Run PuzzleMaker™ 3.1. On the main menu, click on **Create a New Puzzle.**
- From the list of *Puzzle Databases*, select the appropriate database for the vocabulary.
- The *PuzzleMaker Wizard* will take you through selecting a puzzle type and grid type.
- Then select one or more chapters from the list. Indicate whether you want the words selected randomly or manually.
- Select the language and words you wish to use within the maximum for the puzzle. Click **Finish.**
- Save your jumble puzzle to a location that is easily accessible by your students with PuzzlePlayer™ 3.1, or print copies for your students to complete.
- Use PuzzlePlayer™ 3.1 to review the puzzles after your students have worked on and saved them.

Economics ONLINE

	Student	Teacher	Parent
Beyond the Textbook	•	•	•
Chapter Overviews	•	•	•
ePuzzles and Games	•		•
Concepts in Motion	•		•
Multi-Language Glossaries	•		•
Online Student Edition	•	•	•
Self-Check Quizzes	•		•
Student Web Activities	•		•
Study Central™	•		•
Time Current Events	•	•	•
Teaching Today		•	
Vocabulary eFlashcards	•		•
Web Activity Lesson Plans		•	

Glencoe Media Center

› glencoe.com

Study-To-Go
- Vocabulary eFlashcards
- Self-Check Quizzes

› **Audio/Video**
- Student Edition Audio
- Spanish Summaries
- Economics & You Videos

Additional Chapter Resources

Reading Support From Jamestown Education

- **Timed Readings Plus in Social Studies** helps students increase their reading rate and fluency while maintaining comprehension. The 400-word passages are similar to those found on state and national assessments.
- **Reading in the Content Area: Social Studies** concentrates on six essential reading skills that help students better comprehend what they read. The book includes 75 high-interest nonfiction passages written at increasing levels of difficulty.
- **Reading Social Studies** includes strategic reading instruction and vocabulary support in Social Studies content for both ELLs and native speakers of English. www.jamestowneducation.com

Reading List Generator CD-ROM — Glencoe BookLink 3

Use this database to search more than 30,000 titles to create a customized reading list for your students.

- Reading lists can be organized by students' reading level, author, genre, theme, or area of interest.
- The database provides Degrees of Reading Power™ (DRP) and Lexile™ readability scores for all selections.
- A brief summary of each selection is included.

Leveled reading suggestions for this chapter:

For students at a Grade 10 reading level:

- ***Considering a Job Offer,*** by Stuart Schwartz & Craig Conley

For students at a Grade 11 reading level:

- ***In Search of Excellence: Lessons From America's Best-Run Companies,*** by Thomas J. Peters & Robert H. Waterman

For students at a Grade 12 reading level:

- ***Presidential Leadership: Rating the Best and Worst in the White House,*** by James Taranto

*** Review suggested books before assigning them.**

NCEE

National Council on Economic Education

Voluntary Standards Emphasized in Chapter 15

Content Standard 12 Interest rates, adjusted for inflation, rise and fall to balance the amount saved with the amount borrowed, which affects the allocation of scarce resources between present and future uses.

Content Standard 17 Costs of government policies sometimes exceed benefits. This may occur because of incentives facing voters, government officials, and government employees, because of actions by special interest groups that can impose costs on the general public, or because social goals other than economic efficiency are being pursued.

Content Standard 20 Federal government budgetary policy and the Federal Reserve System's monetary policy influence the overall levels of employment, output, and prices.

Resources Available from NCEE

- Virtual Economics®: An Interactive Center for Economic Education Version 3.0
- Capstone: The Nation's High School Economics Course
- Focus: High School Economics, Second Edition
- Focus: Institutions and Markets

To order these materials, or to contact your State Council on Economic Education about workshops and programs, call 1-800-338-1192 or visit the NCEE Web site at store.ncee.net.

The BIG Idea

As students study the chapter, remind them to consider the chapter-based Big Idea. The **Essential Question** in the chapter launch activity below ties in to the Big Idea and helps students think about and understand important chapter concepts. In addition, the Hands-On Chapter Project relates the content from each section to the Big Idea. The steps in each section build on each other and culminate in the Wrap-Up Activity on the Visual Summary page.

Economics & You Video To generate student interest and provide a springboard for class discussion, access the Economics & You Topic 22, **Economic Growth and Stability,** at glencoe.com or on the video DVD.

FOLDABLES Study Organizer

Dinah Zike's Foldables are three-dimensional, interactive graphic organizers that help students practice basic writing skills, review key vocabulary terms, and identify main ideas. Have students complete this chapter's Foldable activity or activities in *Dinah Zike's Reading and Study Skills Foldables* booklet. **OL**

Economics ONLINE

Introduce students to chapter content and key terms by having them access *Chapter 15—Chapter Overviews* at glencoe.com.

CHAPTER 15

Economic Stabilization Policies

Why It Matters

Do you remember Hurricane Katrina or the invasion of Iraq and the subsequent war? How did these events—along with growing demand—affect gasoline prices? Did the higher gasoline prices change the spending habits of you and your friends? How and why? Conduct a simple survey of your friends and family to find out how higher prices impacted their lives. Present the survey to your class. Read Chapter 15 to learn what the government might do to stabilize the economy.

The BIG Idea

Governments strive for a balance between the costs and benefits of their economic policies to promote economic stability and growth.

A busy lunch hour at Times Square in New York City indicates a stable, growing economy.

Economics ONLINE **Chapter Overview** Visit the *Economics: Principles and Practices* Web site at glencoe.com and click on *Chapter 15—Chapter Overviews* to preview chapter information.

Activity: Launching the Chapter

Speculating Remind students that they studied the concepts of supply and demand in Chapters 4 and 5. Have students brainstorm a list of factors that they believe can affect the total supply and total demand in the U.S. economy. Write their ideas on the board. Ask for volunteers to briefly explain how a certain factor might affect supply and demand in the nation. **Essential Question:** **What are different ways that the government can impact total supply and demand in the U.S. economy?** *(Answers may include raising or lowering taxes, increasing spending, and adjusting interest rates.)* Have students write a paragraph predicting what they think they will learn about in this chapter. **OL**

SECTION 1

Macroeconomic Equilibrium

GUIDE TO READING

Section Preview

In this section, you will learn that macroeconomic equilibrium takes place at the intersection of aggregate demand and aggregate supply.

Content Vocabulary

- macroeconomics *(p. 413)*
- equilibrium price *(p. 414)*
- aggregate supply *(p. 414)*
- aggregate supply curve *(p. 414)*
- aggregate demand *(p. 415)*
- aggregate demand curve *(p. 415)*
- macroeconomic equilibrium *(p. 416)*

Academic Vocabulary

- framework *(p. 416)*
- unduly *(p. 417)*

Reading Strategy

Listing As you read the section, complete a graphic organizer similar to the one below by listing at least three factors that could lower production costs and lead to an increase in aggregate supply.

[ ]	→	Effect: Increase in aggregate supply
[ ]	→	
[ ]	→	

ISSUES IN THE NEWS

–BusinessWeek

This Porridge Looks a Little Too Warm

Goldilocks lives. The economic scenario, that is. Those who believe in her think the economy this year will be not too hot, not too cold, but just right. Currently, it's the view most widely held by economists, investors, and Wall Street pros. So, the tale goes, after the unusually warm winter heated up the economy in the first quarter, growth will cool down to a pace of about 3%. . . .

[T]wo things are happening right now that are affecting both manufacturing and the economy. One, businesses are rushing to expand their operations in the face of strong demand and insufficient production capacity. And two, because factory output is growing . . . manufacturing operating rates have risen sharply during the past year. The only way to know for sure . . . is to watch the economy and the data. ■

"Not too hot, not too cold, but just right." According to the news story above, the concept of equilibrium seems to be alive and well. In literature as well as in life, we seem to like things best when they can achieve a reasonable balance. The economy is no exception.

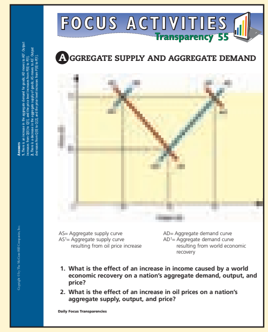
When we deal with **macroeconomics**, the part of economics concerned with the economy as a whole and decision making by large units, we also seek a balance. To do so, we can use a set of "tools" already familiar to us—supply and demand—to find out just where the balance is.

macroeconomics part of economics that deals with the economy as a whole *(also see page 197)*

Focus

Bellringer

Daily Focus Transparency 55



GUIDE TO READING

Answers to Graphic: decline in price of energy; lower interest rates; higher labor productivity

Resource Manager

R Reading Strategies	C Critical Thinking	D Differentiated Instruction	W Writing Support	S Skill Practice
Teacher Edition • Questioning, p. 415 • Academic Vocab., p. 417 **Additional Resources** • Guid. Read. Act., p. 43 • Read. Ess. & Note-Taking Guide, p. 127	**Teacher Edition** • Assessing, p. 415 • Drawing Con., p. 416 **Additional Resources** • Econ. Concepts Trans., Strat. & Act., p. 27 • Econ. Content Vocab. Act., p. 15	**Teacher Edition** • ELL, p. 414 • Visual/Spatial, p. 418 **Additional Resources** • Reteach. Act., p. 15 • Quizzes and Tests, p. 185	**Teacher Edition** • Expository Writing, p. 416 **Additional Resources** • High School Reading in the Content Area Strat. and Act.	**Teacher Edition** • Analyzing Graphs, p. 414 **Additional Resources** • Reading and Study Skills Fold., p. 61

Teach

D Differentiated Instruction

English Language Learners
Instruct students to write a definition of the word *aggregate* based on how it is used in the text. Next, have students look up the dictionary definition of the word and compare it with their own definitions. Finally, ask students to write a sentence using the word *aggregate* to refer to something other than supply or demand. *(Possible sentence: The company's aggregate profits this quarter exceeded expectations.)* **ELL**

S Skill Practice

Analyzing Graphs **Ask:** **Which of the two curves in Figure 15.1 would consumers prefer? Explain.** *(AS¹; that curve represents an increased supply, which would lower the price level)* **OL**

Economic Analysis
Answer: increased production costs

equilibrium price price where quantity supplied equals quantity demanded *(also see page 149)*

aggregate supply the total value of all goods and services that all firms would produce in a specific period of time at various price levels

aggregate supply curve hypothetical curve showing different levels of real GDP that would be produced at various price levels

Aggregate Supply and Demand

MAIN Idea Aggregate supply and demand help us study supply and demand for the economy as a whole.

Economics and You In your English classes, you might study a part of a novel in depth to understand the whole book better. Read on to learn about a similar approach in economics.

When we study markets, we often use the tools of supply and demand to show how the **equilibrium price** and quantity of output are determined. When we study the economy as a whole, we can use these tools in much the same way.

Aggregate Supply

You learned in Chapter 5 that supply is the amount of a particular product offered for sale at all possible prices. When it comes to the economy as a whole, economists like to look at **aggregate supply**, the total value of goods and services that all firms would produce in a specific period of time at various price levels. If the period was exactly one year, and if all production took place within a country's borders, then aggregate supply would be the same as GDP.

The concept of aggregate supply assumes that the money supply is fixed and that a given price level prevails. If prices should change, however, then individual firms would respond by adjusting their output to produce a slightly different level of GDP. If it were somehow possible to keep adjusting the price level to observe how total output changed, we could then construct an **aggregate supply curve**, which shows the amount of real GDP that would be produced at various price levels.

Figure 15.1 shows how an aggregate supply curve for the whole economy might look. Like the supply curve of an individual firm or the market supply curve, it is shown as upward sloping as you move from left to right. To distinguish the aggregate supply curve from other supply curves, it is labeled **AS**.

In Figure 15.1, note that the vertical axis of the graph is labeled 'Price level' rather than just 'Price', as you have seen in earlier chapters. The price level includes the price of everything produced in the economy. In contrast, the word *price* would indicate the cost of only a single good or service. Economists often use an aggregate measure like the price level rather than a single price. Aggregate measures help them better explain changes in the economy.

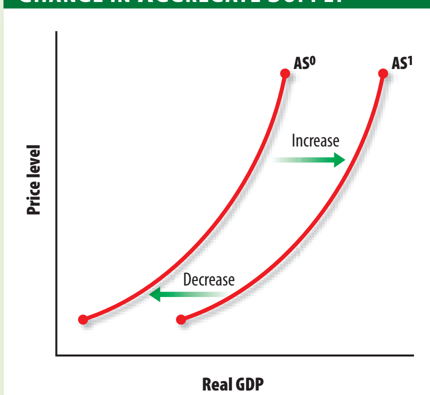
Figure 15.1 ▸ **The Aggregate Supply Curve**

▸ The aggregate supply curve shows the amount of real GDP that would be produced at various price levels. An increase in aggregate supply occurs when production costs decrease for all individual producers. When economists use 2 curves to show changes in aggregate supply, they label the first curve **AS⁰** and the second **AS¹**.

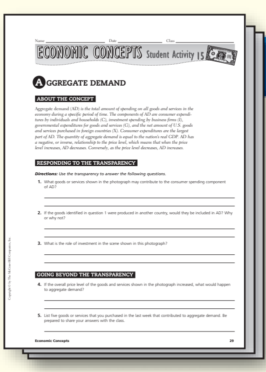
Economic Analysis ***What causes a decrease in aggregate supply?***

Graphs In MOtion
See StudentWorks™ Plus or glencoe.com.

CHANGE IN AGGREGATE SUPPLY



Differentiated Instruction



Economic Concepts Trans., Strat. and Act., p. 29

Aggregate Demand

Objective: Understand the concept of aggregate demand.

Focus/Teach: Ask students to list the different components that comprise aggregate demand. Write their responses on the board. Then have students answer the activity questions.

Assess: Review the students' answers as a class.

Close: Ask students to write a paragraph describing any new insights about aggregate demand that they learned from this activity.

Differentiated Instruction Strategies

BL Have students describe other goods and services that could have been shown to teach the same lesson.

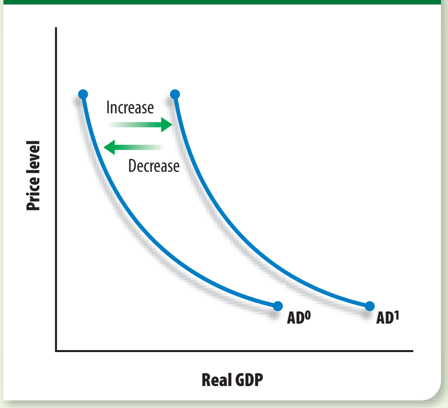
AL Have students answer the "Suggested Activities" questions that appear on page 30 of the booklet.

ELL Have students illustrate the concept of aggregate demand.

Figure 15.2 ▶ **The Aggregate Demand Curve**

Graphs In MOtion
See StudentWorks™ Plus or glencoe.com.

CHANGE IN AGGREGATE DEMAND



▶ The aggregate demand curve shows the amount of real GDP the economy would demand at all possible price levels. Aggregate demand, like aggregate supply, can either increase or decrease. When economists use two curves to show changes in aggregate demand, they label the first curve **AD⁰** and the second **AD¹**.

Economic Analysis ***What causes the aggregate demand curve to shift?***

Finally, note that the horizontal axis is labeled 'Real GDP'. This is because we want to know the value of all goods and services produced, not just the output of a single product. While there are some other differences between the supply curve of a single product and aggregate supply, the two curves are otherwise fairly similar.

R

Changes in Aggregate Supply

Aggregate supply, like the supply of an individual firm, can increase or decrease. Many increases in aggregate supply are tied to the cost of production for an individual firm. For example, if the price of energy should suddenly go down, most if not all firms will be able to produce a little more output, and real GDP will go up. Since this increase in output would happen at all price levels, the increase shows as a shift of the original aggregate supply curve **AS⁰** to the right, and the new aggregate supply curve **AS¹**.

Factors that increase the cost of production for individual firms tend to decrease aggregate supply. These factors include higher oil prices, higher interest rates, and lower labor productivity. Any increase in cost that causes individual firms to offer fewer goods and services for sale at each and every price would shift the aggregate supply curve to the left.

Aggregate Demand

In Chapter 4 you learned that demand is the desire, ability, and willingness to purchase a product. If it were possible to add up everyone's demand for every good and service in the economy, we would have a measure of aggregate, or total, demand. Accordingly, economists call this concept **aggregate demand**, the total value of all goods and services demanded at different price levels. Aggregate demand is labeled **AD** to keep it separate from other demand curves. It is a summary measure of all demand in the economy. Like aggregate supply, it can be represented as a graph, and it can either increase or decrease.

The **aggregate demand curve** appears in **Figure 15.2** and shows the amount of total output, measured in terms of real GDP, that would be purchased at every possible price level. This curve is labeled **AD** and represents the sum of all consumer, business, government, and net foreign demands

aggregate demand the total value of goods and services demanded at all different price levels

aggregate demand curve hypothetical curve showing different levels of real GDP that would be purchased at various price levels

C

R Reading Strategy

Questioning Instruct students to write a five-question multiple-choice quiz about the important ideas presented on this page. After they finish writing their quizzes, ask students to write an explanation for why they chose to ask each question. **OL**

C Critical Thinking

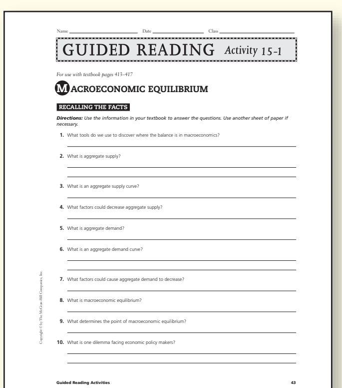
Assessing Ask: Why is the aggregate demand curve a hypothetical curve? *(because desire, ability, and willingness to purchase a product are abstract concepts that are not easily quantified, especially across an entire population)* **OL**

Economic Analysis

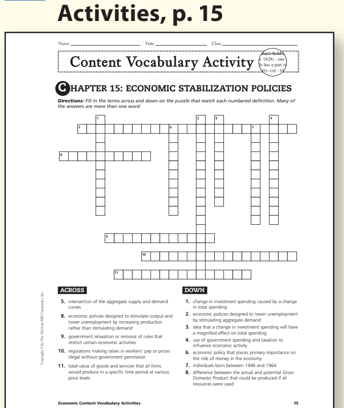
Answer: changes in taxes, transfer payments, and consumer spending preferences

Leveled Activities

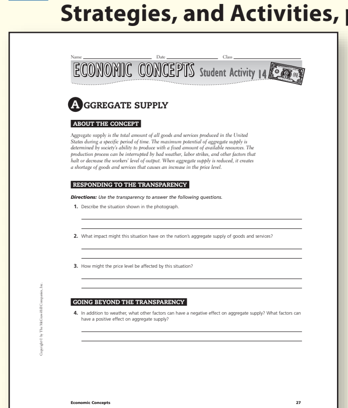
BL **Guided Reading Activities, p. 43**


GUIDED READING Activity 15-1
MACROECONOMIC EQUILIBRIUM

OL **Economic Content Vocabulary Activities, p. 15**


Content Vocabulary Activity
CHAPTER 15: ECONOMIC STABILIZATION POLICIES

AL **Economic Concepts Transparencies, Strategies, and Activities, p. 27**


ECONOMIC CONCEPTS Student Activity 14
AGGREGATE SUPPLY

W Writing Support

Expository Writing Have students use reliable online and print resources to investigate the subject of American saving and spending habits. Ask students to write a paper explaining why the personal savings rate is so low among people in the United States. Students should support their points with facts from articles and books. **AL**

C Critical Thinking

Drawing Conclusions
Ask: How would increased competition in the economy likely affect aggregate demand? *(Increased competition would lower prices and thus increase aggregate demand.)* **OL**

✓Reading Check Answer: Rather than using the price or output of a single product, economists use aggregates, like price level and real GDP, to measure AS and AD. Nonetheless, the slopes of those curves are similar to the slopes of curves measuring individual supply and demand.

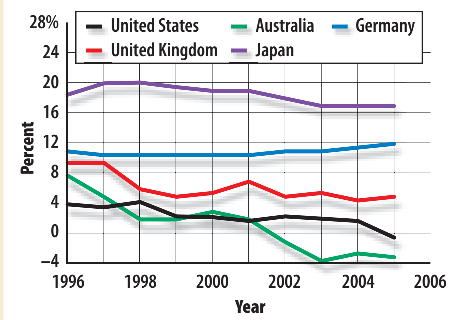
The Global Economy & YOU

Banking on the Future

W When consumers save less and spend more, the aggregate demand curve shifts to the right. This has been the case recently in the United States, where seemingly tireless consumers shop online, in the mall, and at every stop in between. In a country where the minimum wage is $5.15 per hour—compared to Mexico's $4.36 per day—one would think Americans could afford to sock away substantial savings. Instead, we are spending our money at an astonishing rate.

Why are Americans not saving more? Given the dismal outlook for Social Security, shaky pension plans, and rising interest rates, they should be more concerned than ever about their economic future. Despite these issues, the U.S. personal savings rate dipped lower in 2005 than it has since 1933, during the Great Depression. That year it reached negative 0.4 percent.

PERSONAL SAVINGS RATE



Source: St. Louis Federal Reserve

Compared with personal savings rates from around the globe, those of Americans are well below the international average.

macroeconomic equilibrium level of real GDP consistent with a given price level and marked by the intersection of aggregate supply and aggregate demand

at various price levels. It slopes downward and to the right like the individual and the market demand curves.

Changes in Aggregate Demand

Aggregate demand can increase or decrease depending on certain factors. For example, if consumers decide to spend more and save less, the increase in consumer spending also increases aggregate demand, shifting the original aggregate demand curve AD^0 to the right to form the new aggregate demand curve AD^1.

C A decrease in aggregate demand can occur if the same factors act in an opposite manner. If people were to save more and spend less, the aggregate demand curve would shift to the left. Higher taxes and lower transfer payments could also reduce aggregate spending. Such decisions shift the aggregate demand curve to the left because all sectors of the economy collectively buy less GDP at all price levels.

✓Reading Check **Comparing** How do AS and AD compare to individual supply and demand?

Macroeconomic Equilibrium

MAIN Idea Macroeconomic equilibrium is reached when the level of real GDP is consistent with a given price level.

Economics and You You learned earlier about the equilibrium price. Read on to learn how this concept applies to the economy as a whole.

Aggregate supply and demand curves are useful concepts because they provide a **framework** to help us analyze the impact of economic policy proposals on economic growth and price stability. They also can give us an idea of the way and direction in which things will change. They do not provide us with exact predictions, however. Even so, they are useful when we analyze macroeconomic issues.

Macroeconomic equilibrium, for example, is the point at which the level of real GDP is consistent with a given price level. It is determined by the intersection of the aggregate supply and demand curves.

Hands-On Chapter Project

Step 1

Effects of Government Stabilization Policies

In this project, students will assess how government economic policies and other factors impact the economy.

Step 1: Assessing Aggregate Supply and Demand. Student groups will use graphs to show how various factors impact aggregate supply and aggregate demand.

Directions: Organize the class into small groups. Ask each group to create a poster-sized graph illustrating the condition of macroeconomic equilibrium. Instruct each group to use actual price level figures for the vertical axis and actual GDP figures for the horizontal axis. Next, assign a different hypothetical economic situation to each group (for example, growing underemployment, sharp cuts to Social Security, OPEC oil embargo, increase in minimum wage, rise in consumer confidence, and so on). Ask each group to prepare a second graph demonstrating how its assigned event affected the equilibrium it depicted on its first graph. Have groups present their two graphs to the class.

Summarizing Choose two or more of the economic situations you assigned to the groups. Have students write a short paper explaining how these multiple factors, if they occurred at the same time, would impact the macroeconomic equilibrium. **OL**

(Chapter Project continued in Section 2.)

This equilibrium is shown in **Figure 15.3.** In this figure, quantity **Q** is the level of real GDP that is consistent with price level **P,** or where the aggregate supply curve **AS** and the aggregate demand curve **AD** intersect. This equilibrium represents a specific situation at a particular point in time and could change if either **AS** or **AD** changes.

For example, if a new government policy caused the aggregate demand curve **AD** to shift to the right, the new equilibrium would take place at a higher level of real GDP and a higher price level. This is one of the dilemmas facing economic policy makers—how to make real GDP grow without **unduly** increasing the price level and thereby the rate of inflation. R

As you will see in the next section, we can use aggregate supply and demand to analyze the impact of fiscal and monetary policies, two of the major ways of affecting the level of output and real GDP.

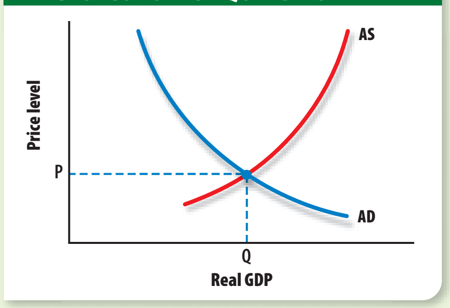
✓Reading Check **Explaining** How does the macroeconomic equilibrium work? How is it used?

Figure 15.3 ▶ **The Economy in Equilibrium**

▶ The economy is at equilibrium when the quantity of real GDP demanded is equal to the real GDP supplied.

Economic Analysis ***What happens to the price level when output increases?***

MACROECONOMIC EQUILIBRIUM



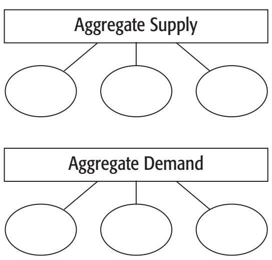
SECTION 1 Review

Vocabulary

1. **Explain** the significance of macroeconomics, equilibrium price, aggregate supply, aggregate supply curve, aggregate demand, aggregate demand curve, and macroeconomic equilibrium.

Main Ideas

2. **Identifying** Use a graphic organizer like the one below to identify the factors that might cause aggregate supply to increase and aggregate demand to decrease.



3. **Explaining** Why is macroeconomic equilibrium important?

Critical Thinking

4. **The BIG Idea** How do aggregate supply and aggregate demand help economic policy makers?
5. **Drawing Conclusions** How is it possible for an economy to grow without a general increase in price levels?
6. **Analyzing Information** What kind of effect would higher taxes have on aggregate supply? Explain.
7. **Analyzing Visuals** Look at Figure 15.3 on this page. What would happen to the price level if AD decreased?

Applying Economics

8. **Aggregate Supply and Demand** Search your local newspaper for articles relating to the impact of changing gasoline prices. Summarize the articles and answer the following question: "How do changing gasoline prices impact AS and AD?" Explain your answer.

R Reading Strategy

Academic Vocabulary Have students write three different sentences related to economics that use the word *unduly.* OL

Economic Analysis

Answer: It decreases.

✓Reading Check **Answer:** By marking the intersection of aggregate supply and aggregate demand, the macroeconomic equilibrium indicates the level of real GDP consistent with a given price level. Economists use it to analyze economic policies.

Assess

Use the Interactive Tutor Self-Assessment CD-ROM to review Section 1, and then assign the Section 1 Review as homework or as an in-class activity.

Close

Summarizing Have students summarize the main points of the section. OL

Review SECTION 1

Answers

1. All definitions can be found in the section and the Glossary.
2. **Aggregate Supply:** price of energy drops; lower interest rates; higher labor productivity. **Aggregate Demand:** decline in consumer spending; higher taxes; lower transfer payments
3. Economists can use it to assess the impact of factors that affect the economy.
4. They provide a framework for analyzing equilibrium, economic growth, and price stability.
5. Students will likely realize that it is possible if lower productivity costs increase aggregate supply.
6. Higher taxes on businesses increase production costs, which in turn causes the AS curve to shift to the left.
7. The price level would increase.
8. Answers will vary but should demonstrate an understanding that increasing gasoline production costs reduces AS and that higher gas prices at the pump reduce AD.

BusinessWeek

Teach

D Differentiated Instruction

Visual/Spatial Instruct students to research how an Asian automaker markets its cars in the United States. Ask students to create a collage-type poster that illustrates the company's marketing techniques. **OL**

BusinessWeek ONLINE

To find up-to-date news and analysis on the economy, business, technology, markets, entrepreneurs, investments, and finance, have students search feature articles and special reports on the BusinessWeek Web site, www.businessweek.com.

Examining the Newsclip

Answers:

1. Asian automobile products are in tune with American customer preferences.
2. The Japanese economy declined in recent years, and an aging population will continue to limit demand.

Additional Support

BusinessWeek NEWSCLIP

Aggregate demand and aggregate supply are becoming global concepts. When demand for a product drops in one country, producers often look for markets in other countries to take up the slack. Asian automakers did just that when demand for Japanese cars decreased in Japan.

Asia's Automakers Think Globally

The global market may be becoming increasingly competitive, but Japan's and Korea's top automakers are hitting new production records and expanding outside their domestic markets at a rapid pace. Faced with stagnant demand in their home countries and a need to reduce foreign exchange risks, the big automakers in both countries are rapidly expanding production overseas and shearing off market shares from the foreign incumbents.

So far, the big three Japanese companies—Toyota Motor Corp., Honda Motor Co. Ltd., and Nissan Motor Co. Ltd.—are enjoying successes as their tight controls on costs and mostly competitive product lineups enable them to take market share from overseas rivals. . . .

Over the past decade, Japanese automakers have been setting up and expanding production facilities overseas. . . . In comparison, Hyundai and its subsidiary Kia are late starters in their localization plans in the U.S. and Europe.

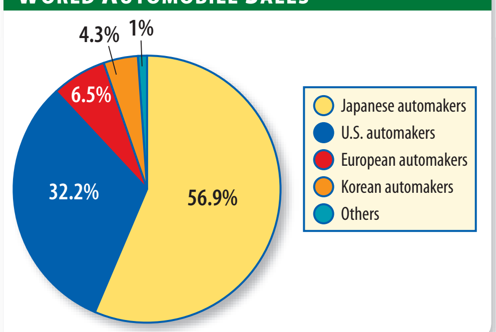
D But . . . all five automakers' prospects for further expansion in North America look promising. In the current high gasoline price environment, their product mixes look to be in tune with customer shifts, with more fuel-efficient cars becoming popular. . . .

Success in the U.S. carries some risks. . . . The impact of a sudden change in purchasing habits by American auto buyers on these companies' earnings and cash flow could be amplified because of this heavy dependence. . . .

The Japanese domestic market remains flat, however. Although the economy is recovering, weak demand is unlikely to be reversed. With a rapidly aging population, long-term growth prospects in Japan are very limited.

—Reprinted from *BusinessWeek*

World Automobile Sales



Source: Autodata Corp.

Examining the Newsclip

1. **Determining Cause and Effect** According to the article, what is causing demand for Japanese and other Asian autos to increase in the United States?
2. **Analyzing** Why is demand for Japanese cars decreasing in Japan?

Extending the Content

Imported Car Sales in the United States In 2005 Japanese manufacturers produced the five top-selling passenger cars in the United States:

1. Toyota Camry
2. Honda Accord
3. Toyota Corolla/Matrix
4. Honda Civic
5. Nissan Altima

Nonetheless, the Japanese share of the total U.S. car sales that year was little more than half of what it was two decades earlier. In 1980 Japanese-made automobiles accounted for 21.2 percent of retail car sales in the United States. In 2005 this figure was 12 percent. German manufacturers, on the other hand, have claimed a larger portion of the American car market. In 1980 cars made in Germany represented 3.3 percent of automobiles sold in the United States. Twenty-five years later, the German share of car sales in American had more than doubled to 7.0 percent.

SECTION 2

Stabilization Policies

GUIDE TO READING

Section Preview

In this section, you will learn how government can promote economic growth through economic policies.

Content Vocabulary

- Medicare *(p. 419)*
- fiscal policy *(p. 420)*
- Keynesian economics *(p. 420)*
- multiplier *(p. 420)*
- accelerator *(p. 420)*
- automatic stabilizer *(p. 422)*
- entitlements *(p. 422)*
- unemployment insurance *(p. 422)*
- supply-side policies *(p. 423)*
- deregulation *(p. 424)*
- monetarism *(p. 426)*
- wage-price controls *(p. 427)*

Academic Vocabulary

- unstable *(p. 420)*
- explicit *(p. 427)*

Reading Strategy

Describing As you read the section, complete graphic organizers similar to the ones below by describing the role of government under demand-side and supply-side policies.

Demand-side policies	Supply-side policies

ISSUES IN THE NEWS

—www.cato.org

Time for "Wise and Frugal"

Federal spending has increased 45 percent in the past five years; the government has run deficits in thirty-three of the past thirty-seven years; the costs of programs for the elderly are set to balloon and impose huge burdens on coming generations of young workers.

Clearly, policymakers are failing to run a "wise and frugal government," as Thomas Jefferson advised in his first inaugural address. A key problem is that federal budget rules stack the deck in favor of continual program expansion. The costly Medicare drug bill and the explosion in pork spending illustrate how a lack of structural controls leads to an undisciplined scramble to spend, spend, spend. ■

Whenever the government spends money on **Medicare**, the federal program that provides health-care expenditures for the elderly, it shifts the aggregate demand curve to the right. As you read in the news story above, it costs the government more money—and it puts an upward pressure on the price level.

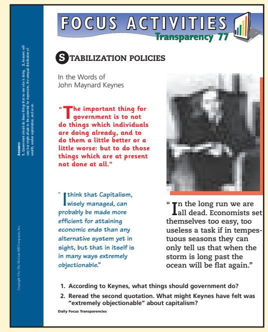
Medicare expenditures are important to those who benefit from them, since economic security is one of the seven major economic goals. Still, policy makers must often choose among a number of competing economic policies. Finding the proper balance between them is an important part of stabilization policy.

Medicare federal health-care program for senior citizens, regardless of income *(also see page 235)*

Focus

Bellringer

Daily Focus Transparency 77


FOCUS ACTIVITIES
Transparency 77

STABILIZATION POLICIES

In the Words of John Maynard Keynes

"The important thing for government is to not do things which individuals are doing already, and to do them a little better or a little worse: but to do those things which are at present not done at all."

"I think that Capitalism, wisely managed, can probably be made more efficient for attaining economic ends than any alternative system yet in sight, but that in itself is in many ways extremely objectionable."

"In the long run we are all dead. Economists set themselves too easy, too useless a task if in tempestuous seasons they can only tell us that when the storm is long past the ocean will be flat again."

1. According to Keynes, what things should government do?
2. Reread the second quotation. What might Keynes have felt was "extremely objectionable" about capitalism?

Daily Focus Transparencies

GUIDE TO READING

Answers to Graphic:

Demand-side policies: increase spending, lower taxes, enact measures that encourage businesses and consumers to spend more

Supply-side policies: cut spending, reduce number of federal agencies, relax regulations, lower taxes

Resource Manager

R Reading Strategies	C Critical Thinking	D Differentiated Instruction	W Writing Support	S Skill Practice
Teacher Edition • Act. Prior Know., p. 420 • Reading Charts, p. 424 • Predicting, p. 427 **Additional Resources** • Guid. Read. Act., p. 44 • Read. Ess. & Note-Taking Guide, p. 130	**Teacher Edition** • Contrasting, p. 420 • Ident. POV, p. 422 • Theorizing, p. 425 **Additional Resources** • Crit. Think. Act., pp. 21, 23 • Econ. Concepts Trans., Strat. & Act., p. 37	**Teacher Edition** • Auditory/Musical, p. 421 • Visual/Spatial, p. 423 • Intrapersonal, p. 426 **Additional Resources** • Enrichment Act., p. 15 • Authentic Assess., pp. 20, 21	**Teacher Edition** • Persuasive Writing, p. 422 • Expository Writing, p. 424 • Narrative Writing, p. 428 **Additional Resources** • High School Writing Process Trans.	**Teacher Edition** • Ident. the Main Idea, p. 421 • Using Tables and Charts, p. 423 • Making Gen., p. 426 **Additional Resources** • Reading and Study Skills Fold., p. 61

Teach

R Reading Strategy

Activating Prior Knowledge

Ask: Why do you think Keynes's theories were so well-received at the time he posited them? *(Possible answer: In 1936 the economy was still mired in the Great Depression, so people were more open to trying new economic ideas.)* **OL**

C Critical Thinking

Contrasting Have students consult books or Web sites to identify and research the economic theory that prevailed in the United States prior to the Great Depression. Ask students to write a report contrasting the main points of that economic theory with Keynesian economics. **AL**

Caption Answer:
John Maynard Keynes

Additional Support

fiscal policy use of government spending and revenue collection measures to influence the economy

Keynesian economics government spending and taxation policies suggested by John Maynard Keynes to stimulate the economy

multiplier magnified change in overall spending caused by a change in investment spending

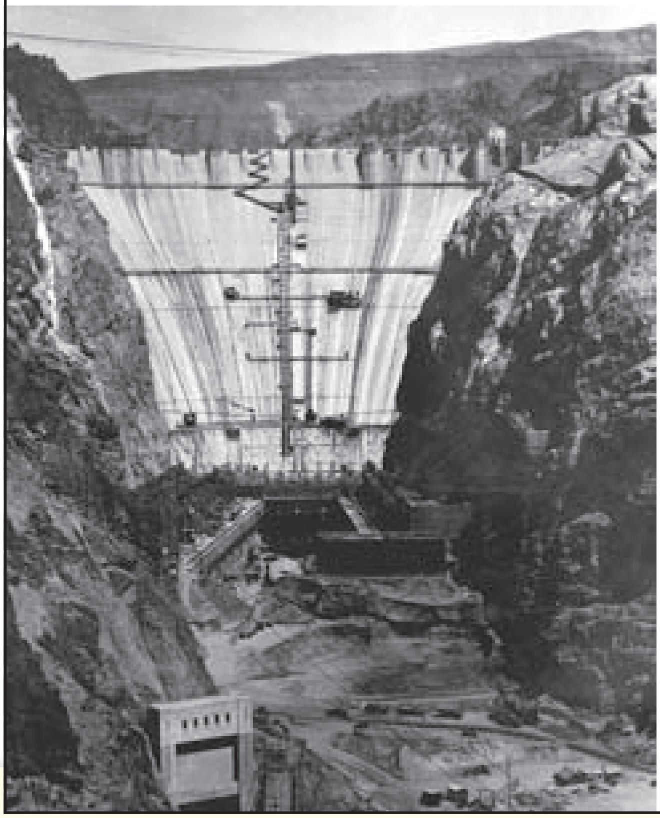
Demand-Side Policies

MAIN Idea Demand-side policies are designed to affect total demand through taxing, government spending, and automatic stabilizers.

Economics and You You learned earlier that government implements policies to help people. Read on to learn how it uses policies to affect the economy.

Demand-side policies are designed to increase or decrease total demand in the economy. These policies try to shift the aggregate demand curve to the right or the left. One approach to changing demand is known as **fiscal policy**—the federal government's attempt to influence or stabilize the economy through taxing and government spending.

Government Spending During the Great Depression, the government funded public works, such as the construction of Hoover Dam shown below, to stabilize the economy. ***Which economist made fiscal policy popular?***



Fiscal policies are derived from **Keynesian economics**, an economic policy approach designed to lower unemployment by stimulating aggregate demand. John Maynard Keynes put forth these theories in 1936, and they dominated the thinking of economists until the 1970s.

Keynesian Economics

Keynes provided the basic framework by using the output-expenditure model, GDP = C + I + G + F. According to this model, any change in GDP on the left side of the equation could be traced to changes on the right side of the equation. The question was: which of the four components caused the instability?

According to Keynes, the net impact of the foreign sector (F) was so small that it could be ignored. The government sector (G) was not the problem either, because its expenditures were normally stable over time. According to Keynes, spending by the consumer sector (C), was the most stable of all. It appeared that the business, or investment, sector (I) was to blame for the instability.

In Keynes's theory, spending by the investment sector was not only **unstable** but had a magnified effect on other spending. If investment spending declined by $50 billion, for example, many workers would lose their jobs. These workers in turn would spend less and pay fewer taxes. Soon, the amount of spending by all sectors in the economy would be down by more than the initial decline in investment.

This effect is called the **multiplier**. It says that a change in investment spending will have a magnified effect on total spending. The multiplier is believed to be about 2 in today's economy. Thus, if investment spending goes down by $50 billion, the decline in overall spending could reach $100 billion. The multiplier also works in the other direction. An increase in spending by $50 billion would increase overall spending by twice that amount.

Extending the Content

Demand-Side Policies During a recession, demand-side economics calls for an expansionary fiscal policy. This involves increased government spending, or tax cuts, or a combination of both. This approach would tend to move the government's budget toward a deficit. In times of high inflation, demand-side economics calls for a contractionary fiscal policy. This would mean government spending cuts, or tax increases, or a mix of the two. This approach would move the government's budget toward a surplus.

Public Works The federal government continues to fund large-scale public works projects, such as the Hyperion water treatment facility in Los Angeles. ***How does public spending offest the loss of business spending?***

Conditions are likely to be made even worse by the **accelerator**—the change in investment spending caused by a change in total spending. After a decline in overall spending begins, investors tend to become cautious, causing investment spending to be reduced even further. Before long, the economy is trapped in a downward spiral. The combined multiplier-accelerator effect is important because it contributes to the instability of GDP.

accelerator change in investment spending caused by a change in overall spending

Role of Government

Keynes argued that only the government was big enough to step in and offset changes in investment-sector spending. The government could take a direct role in the economy and undertake its own spending to offset the decline in spending by businesses. The government could also play an indirect role by lowering taxes and enacting other measures to encourage businesses and consumers to spend more.

Suppose the government wanted to take direct steps quickly to offset a $50 billion decline in business spending. To do this, it could spend $10 billion to build a dam, give $20 billion in grants to cities to fix up poor neighborhoods, and spend another $20 billion in other ways. By adding up individual programs, government spending would replace the $50 billion that businesses do not spend. Thus, the overall sum of C + I + G + F would remain unchanged.

Instead of spending the $50 billion, the government could affect the economy indirectly by reducing tax rates to give investors and consumers more purchasing power. If they spent the $50 billion not collected in taxes, investors and consumers would offset the initial decline in investment spending. Again, there would be no change in the sum of C + I + G + F.

Either way, the government would run the risk of a short-term federal deficit. In Keynes's view, the deficit was unfortunate but necessary to stop further declines in economic activity. When the economy recovered, tax collections would rise, the government would run a surplus, and the debt could be paid back. The justification for *temporary* federal deficits was one of the lasting contributions of Keynesian economics and a major departure from the economic thinking of the time.

D Differentiated Instruction

Auditory/Musical Ask students to write a song, rap, or jingle that explains Keynes's theory of the output expenditure model (GDP = C + I + G + F). Encourage students to provide catchy, memorable lyrics that will help their classmates learn this topic. Ask for volunteers to perform their songs, raps, or jingles for the class. **OL**

S Skill Practice

Identifying the Main Idea

Ask: **Does the federal government's recent pattern of deficit spending match Keynes's ideas about the topic? Why or why not?** *(No; Keynes advocated temporary federal deficits, whereas the federal government's current deficits are ongoing.)* **OL**

Caption Answer: More public spending would increase the value of G, which would offset the decrease in I (business spending), leaving the overall sum of C + I + G + F unchanged.

Additional Support

Teacher Tip

Sharing the Workload
Suggest that students divide the responsibilities so that those who play a smaller role in the creation of the Web site have a larger role in researching information, and so forth.

Activity: Technology Connection

Building a Web Site Organize the class into small groups. Ask students to research the major principles of Keynesian economics. Instruct each group to construct a Web site that explains Keynes's economic theories in an engaging manner. Possible topics that could be discussed on these Web sites include output-expenditure model, government spending, short-term deficits, and the Great Depression. Students may also wish to include graphs that demonstrate Keynesian theories, as well as quotes from Keynes's writings. Have students present their Web sites to the class. **AL**

C Critical Thinking

Identifying Points of View
Ask: Why might some people criticize the entitlement programs of the United States? *(Answers may include higher taxes, reduced incentives to work, or fear of creating a permanent welfare class.)* **OL**

W Writing Support

Persuasive Writing Direct students to write and then perform a speech arguing for or against a greater application of Keynesian principles in the U.S. economy. Instruct students to use the information in the text as well as reliable Internet or library resources that provide factual material to strengthen their arguments. **OL**

Economic Analysis
Answer: point a

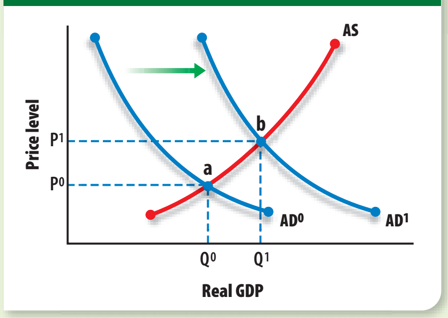
Reading Check Answer: Keynes's ideas dominated the thinking of economics from the 1930s to the 1970s. Elements of this fiscal policy are still practiced today.

Figure 15.4 ▶ Fiscal Policy and Aggregate Demand

▶ Fiscal policies are designed to affect aggregate demand. Increases in government spending or tax reductions increase aggregate demand. As a result, the economy moves from **a** to **b.**

Economic Analysis ***Which point on the graph represents the lowest aggregate demand?***

THE AGGREGATE DEMAND CURVE



automatic stabilizer program that automatically provides benefits to offset a change in people's incomes

entitlement broad social program that uses established eligibility requirements to provide health, nutritional, or income supplements to individuals *(also see page 283)*

unemployment insurance government program providing payments to unemployed workers

Automatic Stabilizers

Another key component of fiscal policy is the role of **automatic stabilizers**, programs that automatically trigger benefits if changes in the economy threaten income. The benefits are automatic because they were approved in prior legislation.

Most **entitlements**—broad social programs that use established eligibility requirements to provide health, nutritional, or income supplements—function as automatic stabilizers. These progams provide some financial assistance to people who lose a job, are injured on the job and receive medical benefits, or are forced to retire because of age or health.

One such entitlement program is **unemployment insurance**—insurance that workers who lose their jobs through no fault of their own can collect from individual states for a limited amount of time. This insurance cannot be collected by people who are fired because of misconduct or who quit their jobs without good reason.

Another important automatic stabilizer is the progressive income tax. For example, if someone loses his or her job or ends up working fewer hours because of cutbacks, that person will earn less. If the reduction in income is significant, that person is likely to fall into a lower tax bracket, which cushions the decline in income.

Fiscal Policy and Aggregate Demand

We can illustrate the impact of such fiscal policies with the aggregate demand curve AD. **Figure 15.4** shows a single aggregate supply curve and two aggregate demand curves. When aggregate demand is weak, the economy would be at point **a,** where **AD⁰** intersects **AS.** Increases in government spending or tax reductions could shift aggregate demand to **AD¹** and move the economy to point **b,** where both real GDP and the price level are higher.

Because aggregate demand basically is the sum of C + I + G + F, it makes little difference which sector provides the stimulus. As long as government policies cause the spending of one sector to expand, AD will shift to the right.

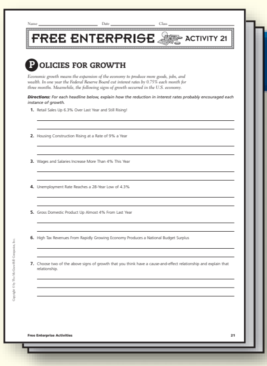
Limitations of Fiscal Policy

Keynes envisioned the role of government spending as a counterbalance to changes in investment spending. Ideally, the government would increase its spending to offset declines in business spending, and conversely government would decrease spending whenever business spending recovered. In practice, however, the federal government generally has not been able to limit or reduce spending.

As a result, the most effective fiscal policies to counter business cycles are the automatic stabilizers. The advantage of the stabilizers is the speed at which they can be implemented because the legislation is already approved.

Reading Check **Analyzing** Why are Keynes's ideas important in the study of economics?

Differentiated Instruction



Free Enterprise Activities, p. 21

Policies for Growth

Objective: Understand how a reduction in interest rates can trigger economic growth.

Focus: Ask students to speculate about why the Federal Reserve Board would cut interest rates.

Teach: Have students complete the activity.

Assess: Call on students to share their answers.

Close: Ask students to write a paragraph summarizing how cuts in interest rates can impact the economy as a whole.

Differentiated Instruction Strategies

BL Have students write a brief article to accompany one of the headlines.

AL Ask students to write about the negative effects that excessive interest rate reductions could cause.

ELL Instruct students to write a definition for the term *interest rate*. Allow them to use a dictionary, if necessary.

Supply-Side Policies

MAIN Idea Supply-side economics focuses on policies that increase production through less government and lower taxes.

Economics and You If you and your family had to pay less in taxes, would you spend or save the extra money? Read on to find out what supply-siders think.

Supply-side policies are policies designed to stimulate output and lower unemployment by increasing production rather than by stimulating demand. The supply-side view gained support in the late 1970s because demand-side policies did not seem to be controlling the nation's growing unemployment and inflation. In the 1980s, supply-side policies became the hallmark of President Ronald Reagan's administration.

The differences between supply-side policies and demand-side policies are smaller than most people realize. Both policies, which are summarized in **Figure 15.5,** have the same goal: increasing production and decreasing unemployment without increasing inflation.

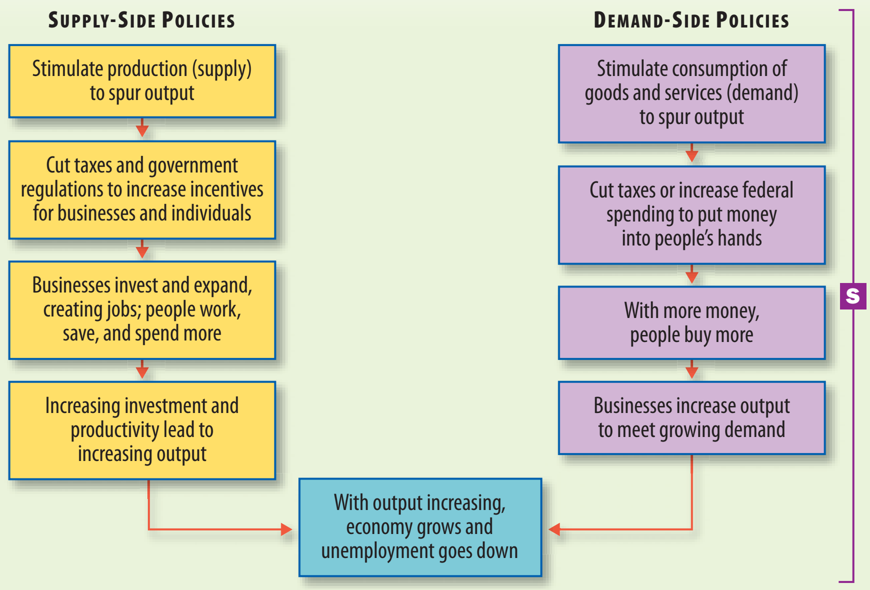
supply-side policies economic policies designed to stimulate the economy by increasing production

D

Smaller Role for Government

A key goal for supply-siders is reducing government's role in the economy. One way to do this is to reduce the number of federal agencies. Another way is to spend less at the federal level. Yet another way is to lessen the government's role by relaxing

Figure 15.5 ▶ Comparing Supply-Side and Demand-Side Policies



S

▶ Supply-side policies and demand-side policies have the same goal: continuous and stable economic growth without price inflation.

Economic Analysis ***How does the role of the government differ under supply-side and demand-side policies?***

Charts In MOtion
See StudentWorks™ Plus or glencoe.com.

D Differentiated Instruction

Visual/Spatial Have students draw a cartoon illustrating one or more of the concepts related to supply-side economics. Inform students that they may include relevant people (Reagan, for example) or events (savings and loan deregulation, for example) in their cartoons. **OL**

S Skill Practice

Using Tables and Charts

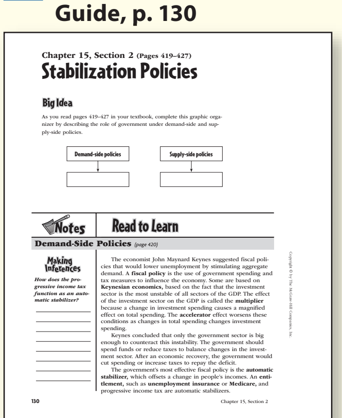
Ask: **How are supply-side policies and demand-side policies similar?** *(Both may use tax cuts, both intend for people to spend more money, and both have the goal of higher output and lower unemployment.)* **OL**

Economic Analysis

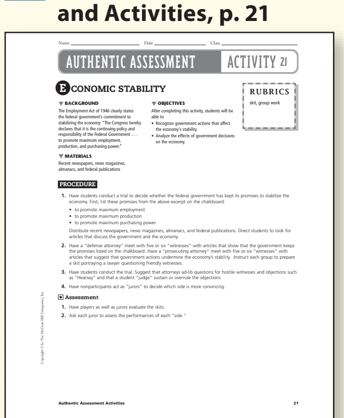
Answer: Under supply-side economics, the government's role in the economy is limited. With demand-side economics, the role of the government in the economy is expanded.

Leveled Activities

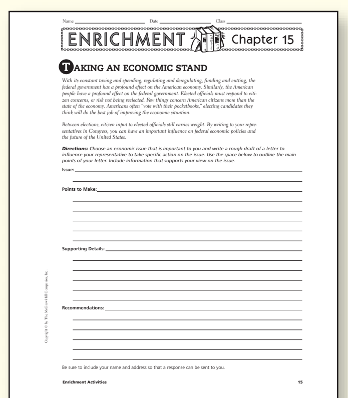
BL Reading Essentials and Note-Taking Guide, p. 130



OL Authentic Assessment Strategies and Activities, p. 21



AL Enrichment Activities, p. 15



R Reading Strategy

Reading Charts **Ask:** Does the data in Panel B support the Laffer Curve hypothesis? Why or why not? *(No. Tax receipts declined after tax rates were lowered in 2001; according to the Laffer Curve, tax receipts should have increased after 2001.)* **OL**

W Writing Support

Expository Writing
Instruct students to research the deregulation of the savings and loan industry or another deregulation that occurred in the 1980s. Ask students to write a paper explaining the goals and impact of the deregulation. **OL**

Economic Analysis
Answer: Though lower in 2000, personal income yielded more tax receipts that year than in 2005, when a higher level of personal income yielded less tax revenue.

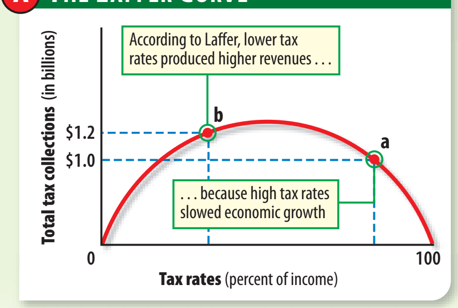
Additional Support

Figure 15.6 ▶ **Tax Rates and Tax Receipts**

▶ The Laffer curve is a hypothetical relationship between federal income tax rates and tax revenues. Panel A illustrates the argument that lower individual income tax rates would generate higher tax collections, as shown in the movement from **a** to **b.** Panel B shows that federal tax revenues declined after individual income tax rates were reduced in 2001.

Economic Analysis ***How does personal income in 2000 and 2005 compare to individual income tax receipts during the same years?***

A The Laffer Curve



B Tax Receipts

Year	Personal income (in billions)	Individual income tax receipts (in billions)
2000	$8,430	$1,004
2001	8,724	994
2002	8,882	858
2003	9,164	794
2004	9,731	809
2005	10,239	927

Source: *Economic Report of the President*

deregulation relaxation or removal of government regulations on business activities

or removing government regulations that restrict the activities of firms in certain industries—a process called **deregulation**.

Deregulation is a major objective of supply-siders. The policy has been popular among politicians ever since President Reagan deregulated the savings and loan industry in the 1980s. Since then, the American economy has seen a flood of deregulation ranging from airlines and banking to telecommunications and interstate trucking.

Lower Federal Taxes

Supply-siders also target the federal tax burden on individuals and businesses. They believe that if taxes are too high, people will not want to work as much, and businesses will therefore produce less. Lower tax rates, they argue, allow individuals to keep more of the money they earn, which encourages them to work harder. This would give workers more money to spend in the long run. Government revenues would also increase, as additional business activity leads to greater production, resulting in greater tax collections.

During the 1980s, somewhat optimistic supply-siders argued that lower individual income tax rates would stimulate the economy so much that the government could collect even more taxes than before. This idea of increased tax revenue was formalized in the Laffer curve—a hypothetical relationship between federal income tax rates and tax revenues.

The Laffer curve shown in **Panel A** of **Figure 15.6** illustrates the expected gain in tax revenues when taxes were reduced from point **a** to point **b.** This proposition was the basis for President Reagan's 1981 tax cut, which reduced the tax rates for individual income taxes 25 percent over a three-year period. The Laffer curve was popular at the time because it gave people a seemingly sound reason to have lower marginal tax brackets.

Activity: Hands-On Economics

Analyzing Opinions About Tax Cuts
Organize the class into groups of three students each. Instruct groups to interview at least 20 people about income taxes. Tell students to ask their subjects if they believe the current tax rates are satisfactory or if they think the rates should be changed. Direct students to also ask interviewees the primary reason for their opinions about tax rates. Ask groups to prepare a chart that organizes their findings by category (for example, charts could have three columns titled "Favors lower taxes," "Favors higher taxes," and "Favors no change in tax rates"; rows in the chart could then list the different reasons for these opinions). Have groups present their data to the class. Lead a discussion about how public opinion on taxation can impact the government's economic policies. **OL**

When President George W. Bush was elected in 2000, he also made individual income tax cuts one of his highest priorities. The first round of his proposed tax cuts was passed in 2001, and several extensions followed in subsequent years.

However, as **Panel B** in Figure 15.6 shows, individual income tax receipts generally declined from 2000 to 2004, even though personal income rose in each of those years. Unfortunately, the increased tax revenue collections predicted by the Laffer curve never materialized, although it is highly likely that the increase in personal income worked to stimulate economic growth.

Impact of Supply-Side Policies

The aggregate supply and demand curves can illustrate the impact of supply-side policies. As **Figure 15.7** shows, when aggregate supply is low, the economy is at point **a.** This is the point where the original aggregate demand curve **AS⁰** intersects with the aggregate demand curve **AD.**

If supply-side policies were successful, more would be produced at every price level. The aggregate supply curve would then shift to **AS¹**, and the point of macroeconomic equilibrium would move to **b.** As long as there was no corresponding change in aggregate demand, real output would grow, and the price level would come down.

Limitations of Supply-Side Policies

One limitation of supply-side policies is a lack of enough experience with them to know how they affect the economy. Even aggregate supply and aggregate demand are largely conceptual, making it difficult to predict the exact consequence of any particular supply-side policy.

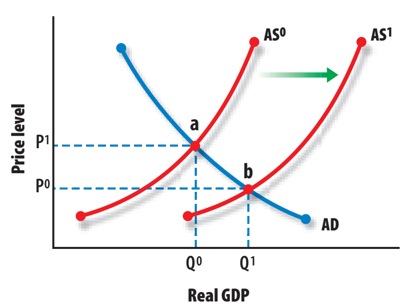
In the case of the Laffer curve, total personal income tax collections, when adjusted for inflation, actually declined after the implementation of President Reagan's 1981 tax reductions. They declined again after the Bush tax cuts of 2001. The result was that one of the main foundations of the supply-side school—that tax cuts would lead to higher tax revenues—proved to be false. Even so, policies that promote productivity, reduce unnecessary paperwork, or otherwise stimulate the economy to grow to its maximum potential are certainly worthwhile. Almost everyone, including demand-siders, favors these policies.

Finally, we should note that supply-side economic policies are designed to promote economic growth rather than to remedy economic instability. Many economists believe that supply-side policies during both the Reagan and the Bush presidencies weakened the automatic stabilizers by making the federal tax structure less progressive and by reducing many "safety net" programs. Both actions may have stimulated growth. However, neither was designed to add to short-term economic stability.

✓Reading Check **Interpreting** What are the main goals of supply-side economists?

Figure 15.7 ▸ Supply-Side Policies and Aggregate Supply

THE AGGREGATE SUPPLY CURVE



▸ Supply-side policies are designed to increase aggregate supply through decreased government spending and involvement as well as lower taxes.

Economic Analysis ***What happens to the price level when the aggregate supply curve shifts to the right?***

C Critical Thinking

Theorizing **Tell students:** In the 1980s, supply-side economics were sometimes referred to as "trickle-down economics." **Ask:** **Why do you think supply-side polices were called this?** *(The tax cuts and relaxed regulations were designed to increase the productivity of manufacturers and the wealthy, who in turn would create more jobs for the middle- and lower-classes. The benefits of supply-side policies were thus intended to "trickle down" to all elements of society.)* **OL**

✓Reading Check **Answer:** lower taxes and less government regulation, increased investing and business expansion, more jobs and more consumer spending, increased economic productivity and economic growth, less unemployment

Economic Analysis
Answer: It drops.

Additional Support

Extending the Content

Impact of Reaganomics The impact of President Reagan's economic policies remains the subject of intense debate, just as it was in the 1980s. Supporters point out that Reagan's tax cuts and deregulation efforts sparked a full recovery for the U.S. economy, which was mired in a severe downturn when he took office in 1981. Inflation, interest rates, and unemployment fell during the Reagan years, and the economy entered the longest period of continual expansion in American history. On the other hand, Reagan's supply-side policies created record budget deficits and a staggering national debt. Detractors also maintain that real wages declined during the Reagan years and that the growth of other leading world economies outpaced that of the United States in the 1980s.

D Differentiated Instruction

Intrapersonal Have students review the main ideas of demand-side, supply-side, and monetary policies. Ask students to write an essay describing their opinions about each of the three policies. Instruct students to include in their essays which policy they believe is best for the United States and the reasons for their selection. **OL**

S Skill Practice

Making Generalizations

Ask: Based on the text, what usually happened to the U.S. economy during wartime? *(expansive monetary policy and inflation)* Why do you think this happened? *(Students may note that the government needed money to fight the war, so it allowed excessive monetary growth, which brought about inflation.)* **OL**

Caption Answer: more borrowing and increased demand

Money Supply and Interest Rates
When the Fed decreases interest rates, more money becomes available to grow the economy. ***What is the short-run impact of lower interest rates?***

Monetary Policies

MAIN Idea Monetarist policies seek steady economic growth by controlling the money supply.

Economics and You Neither demand-siders nor supply-siders consider the money supply. Read on to learn why monetarists disagree with both.

Both demand-side policies and supply-side policies are concerned with stimulating production and employment. Neither assigns much importance to the money supply. An approach called **monetarism**, however, places primary importance on the role of money in the economy.

Monetarists believe that fluctuations in the money supply can be a destabilizing element that leads to unemployment and inflation. Therefore, they favor policies that lead to stable, long-term monetary growth at levels low enough to control inflation.

monetarism school of thought stressing the importance of stable monetary growth to control inflation and stimulate long-term economic growth

Skills Handbook
*See page **R52** to learn about **Sequencing Events.***

Short-Run Impacts

A monetary policy in which the money supply is tightened is called a contractionary monetary policy. In the short run, this policy can raise interest rates. Higher interest rates might be desirable if the economy is growing too fast and prices are rising. The higher interest rates would slow consumer and business borrowing, leading to a decrease in aggregate demand. As a result, the aggregate demand curve would shift to the left, lowering both the price level and real GDP.

If the economy is growing too slowly, an expansionary policy can increase the money supply and lower interest rates. This would reduce the cost of consumer and business borrowing and increase aggregate demand. The aggregate demand curve would then shift to the right, causing real GDP and the price level to increase.

In the short run, monetary policy affects interest rates. Changes in the level of interest rates can have a significant impact on the demand for real GDP. In the longer run, however, monetary policy can have very different results.

Long Run Impacts

Expansionary monetary policy, with a larger money supply, can lower interest rates. At the same time, it could also increase the possibility of future inflation, as past events have shown. During the Revolutionary War, so much money was printed that prices rose dramatically, and the Continental dollar soon became worthless. Prices also increased significantly during the Civil War when too many greenbacks were printed. Finally, excessive monetary growth allowed by the Fed to help the government finance the Vietnam War resulted in the inflation of the 1970s.

The money supply can grow over time, but how fast should it be allowed to grow? According to the monetarists, it should grow at a slow but steady rate. Specifically, the rates of growth of real GDP and productivity would determine the rate at which the money supply grows.

For example, with real GDP growing by 3 percent and productivity growing by 1 percent, the money supply could be allowed

Hands-On Chapter Project

Step 2

Effects of Government Stabilization Policies

Step 2: Assessing Government Policies. Students will create graphs showing the effects of different government economic policies.

Directions: Have students return to the groups formed in Step 1. Ask groups to research examples from U.S. history when each of the three types of policies described in this section were implemented (for example, demand-side policies during the Great Depression, supply-side policies during the 1980s, the Fed lowering interest rates in 2001). Have each group create three sets of graphs showing the effects of the policies they researched. Students, for example, may draw a line graph showing how federal spending increased in the 1930s, or they may create a bar graph showing how unemployment rates changed after interest rates were lowered in 2001. Have students present their three sets of graphs to the class.

Summarizing Instruct students to work together within their groups to write a short summary report assessing the economic impact of the three policies they researched. **OL**

(Chapter Project continued in Section 3.)

to grow at about 4 percent without causing inflation. At this rate, there would be just enough extra money each year to buy the additional goods and services the economy produces.

This approach to inflation control is in sharp contrast to approaches that other administrations tried earlier. In the early 1970s, for example, President Richard Nixon attempted to stop inflation by imposing **wage-price controls**—regulations that make it illegal for businesses to give workers raises or to raise prices without the **explicit** permission of the government. Most monetarists at the time said the controls would not work. Events soon proved them correct, as prices rose despite the legislated controls.

Use of Monetary Policy

Economists have discovered that timing can be difficult when it comes to implementing monetary policy. An expansionary monetary policy may affect the economy right away—or several years later. The same thing is true for a contractionary monetary policy. In either case, the desired changes may happen immediately or only after a lag. For this reason, monetarists argue that changes in the money supply should be gradual so that they do not destabilize the economy.

Because of these lags, monetary policy does not seem to be very effective in reducing short-term unemployment. For example, when the Fed aggressively lowered interest rates in 2001 to move the economy out of the recession, it took several years for the unemployment rate to come down. In the end, most monetarists argue that monetary policy can be used to maintain long-term price stability. However, it must be used with caution because its short-run impacts are uncertain. **R**

✓**Reading Check** **Summarizing** What problems are associated with expansionist monetary policy?

wage-price controls policies and regulations making it illegal for firms to give raises or raise prices without government permission

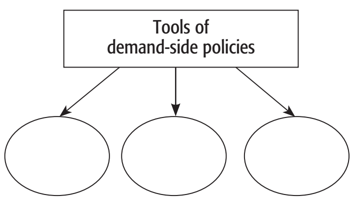
SECTION 2 Review

Vocabulary

1. **Explain** the significance of Medicare, fiscal policy, Keynesian economics, multiplier, accelerator, automatic stabilizer, entitlements, unemployment insurance, supply-side policies, deregulation, monetarism, and wage-price controls.

Main Ideas

2. **Listing** What are the assumptions of supply-siders?
3. **Explaining** What problems exist for monetary policy?
4. **Identifying** Use a graphic organizer like the one below to identify the tools of demand-side policies.



Critical Thinking

5. **The BIG Idea** How do supply-side economists and demand-side economists differ with regard to the role of government in the economy?
6. **Drawing Conclusions** Do you agree with the opinion that fiscal policy is ineffective? Explain your reasons for agreeing or disagreeing.
7. **Analyzing Information** According to monetarists, how do fluctuations in the money supply affect the economy?
8. **Analyzing Visuals** Look at the photo on page 420. How does it reflect the views of John Maynard Keynes on the role of government in the economy?

Applying Economics

9. **Deregulation** Identify an industry in your state that has been or is being deregulated. Why did legislators make the decision to deregulate the industry? Did deregulation have the expected benefits? Were there any unanticipated costs? Explain.

R Reading Strategy

Predicting Have students write a paragraph predicting the type of monetary policy, if any, the Fed is likely to pursue in the next few months. *(Answers will vary based on the current economic climate. If inflation is high, then the Fed may pursue a tight monetary policy. If unemployment is high, the Fed may promote an expansionary monetary policy.)* **OL**

✓**Reading Check** **Answer:** high inflation, devalued currency

Assess

Use the Interactive Tutor Self-Assessment CD-ROM to review Section 2, and then assign the Section 2 Review as homework or as an in-class activity.

Close

Organizing Ask students to create a graphic organizer that includes the main points of the three economic policies described in this section. **OL**

Review SECTION 2

Answers

1. All definitions can be found in the section and the Glossary.
2. deregulation and lower taxes will increase aggregate supply
3. uncertain short-term impacts; possible future inflation with an expansive monetary policy; high interest rates and a decline in borrowing with a tight monetary policy
4. taxing; spending; automatic stabilizers
5. Supply-side economists believe the government's role in the economy should be reduced through cutting federal agencies and deregulating business. Demand-side economists believe the government should take a greater role in the economy through increased spending and possibly by lowering taxes and enacting other measures to encourage business and consumer spending.
6. Answers will vary, but students should demonstrate a clear understanding of the limits of fiscal policy.
7. If the money supply grows too fast, then inflation will result; if the money supply contracts too much, then productivity will fall.
8. The government-funded Hoover Dam is an example of the government spending money to offset the decline in investment-sector spending that occurred during the Great Depression.
9. Answers will vary, but students should explain why legislators decided to deregulate the industry (to increase competition, for example) and the effects of this deregulation.

Teach

W **Writing Support**

Narrative Writing Direct students to review the main economic ideas of John Maynard Keynes. Ask students to then write a story in which Keynes uses a time machine to travel to the United States today. Instruct students to include in their stories Keynes's likely reactions to, and opinions about, the current economic situation in this country. **OL**

Examining the Profile

Answers:

1. Such a policy broke with longstanding governmental practice, and leaders in the 1930s generally believed that laissez-faire policies would allow the market to correct itself in the long run.
2. A government should spend money, taking on debt if necessary, to help lift a country out of a recession or depression; the government should save money during prosperous times to prevent inflation.

Additional Support

ECONOMIST

Profiles in Economics

John Maynard Keynes is widely regarded as the most influential economist of the twentieth century. His theories led the U.S. government to take an active role in preventing economic instability that could lead to widespread joblessness.

John Maynard Keynes (1883–1946)

- his "Keynesian economics" caused governments to implement fiscal policy
- instrumental in the planning of the World Bank

The Long Run

During the Great Depression of the 1930s, government leaders desperately sought solutions to widespread unemployment and poverty. Yet they remained reluctant to "unbalance" the budget by using federal money to help the nation's people directly. Instead, they believed that laissez-faire policies would allow the market to correct itself in the long run.

Enter Keynes

A brilliant intellectual, John Maynard Keynes established a reputation for straight talking and insightful critique early in his career. He served as an adviser to the British Treasury and as a British representative at the World War I peace conference at Versailles. He correctly predicted that the high reparations imposed on Germany after World War I would lead to another war.

As an economist, Keynes was not impressed with perfectly balanced budgets. In fact, he considered balanced budgets—when that meant government inaction—to be disastrous if a nation's consumer and business sectors had no money to spend or invest to create jobs. In his masterpiece, *The General Theory of Employment, Interest, and Money* (1936), Keynes argued that governments should spend money—and even take on debt—to help correct an economic **W** recession or depression. They should then save money during an overly successful period to prevent inflation.

To Keynes, it did not help anyone to wait for the long run because "in the long run we are all dead." His theories were revolutionary, and they provided much needed insight into the workings of a depression-era economy. Soon, the label *Keynesian economics* stood for any government spending or taxing policies designed to stimulate the private sector.

Examining the Profile

1. **Analyzing Information** Why were government leaders reluctant to help people during the Great Depression?
2. **Summarizing Information** What is the basic premise of Keynesian economics?

Activity: Collaborative Learning

Preparing an Exhibit Divide the class into small groups. Instruct students to use reliable online or print resources to research the implementation of Keynesian economics during the Great Depression. Ask groups to then prepare an exhibit based on their findings. Encourage students to be creative when thinking of ideas for their exhibits. Possible ideas include photos of Keynes from 1930s newspapers; a model of the Hoover Dam or other government-funded projects during the Depression; a copy of *The General Theory of Employment*, *Interest*, *and Money*; logos of New Deal agencies; a graph of government spending in the 1930s; and so on. Have groups display their exhibits in the class. Ask students to explain the various components as you review their exhibits. **AL**

SECTION 3

Economics and Politics

GUIDE TO READING

Section Preview

In this section, you will learn that economic policies change as time and circumstances change.

Content Vocabulary

- monetary policy *(p. 431)*
- baby boomers *(p. 432)*
- Council of Economic Advisers *(p. 433)*

Academic Vocabulary

- ideology *(p. 431)*
- advocates *(p. 433)*

Reading Strategy

Identifying As you read the section, complete a graphic organizer similar to the one below by identifying the different kinds of fiscal policy.

Fiscal policy → [ ]
Fiscal policy → [ ]
Fiscal policy → [ ]

ISSUES IN THE NEWS

—TIME

Enthusiastic Capitalism

American culture is today, as ever, uniquely suited for growth, innovation, and advancement.

The most obvious bedrock of success is entrepreneurial spirit. The U.S. has the most risk-taking, most laissez-faire, least regulated economy in the advanced Western world. America is heartily disdained by its coddled and controlled European cousins for its cowboy capitalism. But it is precisely America's tolerance for creative destruction—industries failing, others rising, workers changing jobs and cities and skills with an [enthusiasm] and [casualness] that Europeans find astonishing—that keeps its economy churning and advancing. . . . The mistake of the Soviets, Japanese, and so many others was to assume that creativity could be achieved with enough government planning and funding. . . . ■

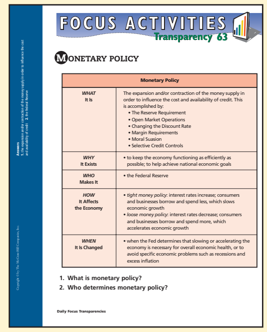
As we look at the economic history of the United States, it is clear that times are better than ever. Inflation is largely under control, and the economy is larger and more productive than ever. Recessions still occur, of course, but business cycles have generally turned into fluctuations, and economic expansions are longer than ever.

Major domestic or even international events can temporarily interrupt the economy, but capitalistic market economies have a remarkable ability to cope with adversity. If anything, the task before us is to manage our prosperity in a way that both improves our economic health and benefits everyone.

Focus

Bellringer

Daily Focus Transparency 63



GUIDE TO READING

Answers to Graphic: discretionary fiscal policy; passive fiscal policy; structural fiscal policy

Resource Manager

R Reading Strategies	C Critical Thinking	D Differentiated Instruction	W Writing Support	S Skill Practice
Teacher Edition • Using Context Clues, p. 430 **Additional Resources** • Guid. Read. Act., p. 45 • Read. Ess. & Note-Taking Guide, p. 133	**Teacher Edition** • Speculating, p. 431 • Making Predictions, p. 432 **Additional Resources** • Econ. Concepts Trans., Strat. & Act., p. 35	**Teacher Edition** • Adv. Learners, p. 430 • Visual/Spatial, p. 432 **Additional Resources** • Authentic Assess., p. 20 • Reteach. Act., p. 15	**Teacher Edition** • Persuasive Writing, p. 431 **Additional Resources** • Writer's Guidebook • Reading and Study Skills Fold., pp. 61, 62	**Teacher Edition** • Making Inferences, p. 430 • Problems and Solutions, p. 433 • Drawing Con., p. 434 **Additional Resources** • Daily Focus Trans. 63, 78, 79

Teach

D Differentiated Instruction

Advanced Learners To help build discussion skills for gifted students, appoint two or three students to plan and lead a class or panel discussion on the different approaches of fiscal policy. **AL**

S Skill Practice

Making Inferences **Ask:** **Based on this information, what can you infer about Congress after Roosevelt took office?** *(Possible answer: Congress was controlled by the Democrats and was supportive of Roosevelt's ambitious agenda.)* **OL**

R Reading Strategy

Using Context Clues Have students write a definition of *lag* based on how the word is used in this paragraph. *(Possible answers: delay; holdup)* **Ask:** **What context clues helped reveal the meaning of the word?** *(Students should point out references to the passing of time, such as "takes several months" and "a year or more.")* **OL**

Changing Nature of Economic Policy

MAIN Idea The government can influence the economy with discretionary, passive, or structural fiscal policies.

Economics and You Today, major recessions are rare in the United States. Read on to learn how this has affected government policies.

Fiscal policies are government attempts to influence the economy through taxing and spending actions. This may involve ways to speed up the economy with tax cuts or with additional federal spending. It may also include government efforts to slow the economy down by either increasing taxes or reducing spending.

D Types of Fiscal Policy

Several different kinds of spending and taxing policies exist. These fiscal policies can be either discretionary, passive, or structural.

Discretionary fiscal policy is policy that someone must choose to implement. It requires an action by Congress, the president, or an agency of government to take effect. One example is a federal expenditure to build a highway or renovate a downtown area in order to offset a decline in business spending. As you read in Chapter 10, about one-third of all federal spending is discretionary rather than mandatory.

Passive fiscal policies do not require new or special action to go into effect. Instead, the policies react automatically when the economy changes. Examples of passive fiscal policies include unemployment insurance and Social Security benefits. In fact, most of the automatic stabilizers you learned about earlier are examples of passive fiscal policies.

Finally, *structural* fiscal policies are policies designed to strengthen the economy over a longer period of time. Examples include reforms of popular programs such as Social Security and welfare in order to make the programs financially secure and more effective in the long run. Most of the supply-side policies, which advocate a smaller role for government and lower taxes, are structural fiscal policies.

Did You Know?

Early Practitioner While John Maynard Keynes was widely credited as the first person to advocate fiscal policy to stimulate the economy in the mid-1930s, President Franklin D. Roosevelt preceded him by several years. When Roosevelt took office on March 4, 1933, the U.S. economy was suffering from its worst depression. With little economic theory to guide him, Roosevelt introduced 15 new bills during his first 100 days in office, some of which poured billions of dollars into state-run welfare and public-works programs. Roosevelt's aggressive use of discretionary fiscal policy was instrumental in helping the economy out of the Great Depression.

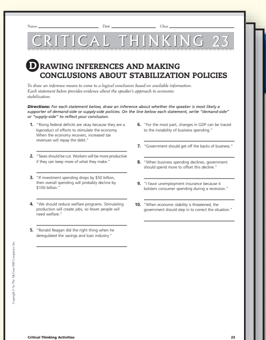
Decline of Discretionary Fiscal Policy

At one time, discretionary fiscal policies were the most popular economic policies. In the 1940s, massive government spending for World War II helped pull the economy out of the Great Depression. Both President Kennedy, in the early 1960s, and later President Reagan, in the early 1980s, used large tax cuts to get a sluggish economy moving again.

However, for several reasons discretionary fiscal policy is used less today. The first reason relates to the various lags that inevitably occur between recognizing that there is a problem and actually doing something about it. Suppose, for example, that the problem is a potential recession, and that the ideal remedy would be to spend $50 billion on roads and highways.

Policy makers first face a recognition lag because it normally takes several months to confirm that a recession is actually taking place. A legislative lag would follow because it may take a year or more for Congress to pass laws authorizing expenditures. This would be followed by an implementation lag because it often takes several more years to build the highways

Differentiated Instruction



Critical Thinking Activities, p. 23

Drawing Inferences and Making Conclusions

Objective: Categorize stabilization policies by drawing inferences based on available information.

Focus: Ask students to share instances in which they have made inferences.

Teach: Ask students whether each statement is an example of demand-side or supply-side economics.

Assess: Go over students' answers as a class.

Close: Ask students to think of other examples of supply-side or demand-side policies.

Differentiated Instruction Strategies

BL Explain reasons why each statement would be made by a supply-sider or a demand-sider.

AL Have students create a script for a debate between a supply-sider and a demand-sider.

ELL Ask students to explain *demand-side economics* in their own words.

and pump the money into the economy. In the end, the recession—which historically lasts for less than a year—will be over by the time the spending begins to stimulate the economy.

The second reason for the decline of discretionary fiscal policy is the gridlock that can occur when the political parties in Congress oppose each other's views on the budget. In both 1995 and 1996, for example, Congress shut down the federal government when Republicans and Democrats could not agree on the federal budget.

Ideology is the third reason. President Bush's tax cuts, for example, were based on the belief the American economy needed a structural change. As a result, in 2001 Bush proposed tax cuts that would extend to the year 2010 and beyond. Thus, the preference for structural policies has displaced the use of discretionary ones. C

Rise of Monetary Policy

The declining use of discretionary fiscal policy left a void filled by the Federal Reserve System, which has the responsibility for conducting monetary policy. As you learned earlier, **monetary policy** involves changing the amount and availability of credit in order to influence interest rates.

Such a situation occurred during the recession of 2001. That recession was so mild and so short—lasting about eight months—that policymakers altogether ignored discretionary fiscal policy. In addition, Congress was preoccupied with a response to the terrorist attacks on September 11.

On the other hand, the Fed was actively lowering the discount rate on an almost monthly basis in order to stimulate the economy. The policy worked, and the Fed took much of the credit for the short duration and mild impact of the recession.

Of course, even the Fed is not above criticism. For example, the Fed's efforts to prevent inflation by raising interest rates W in 2000 may have contributed to the 2001 slowdown. Even so, most members of Congress believe that the power to create money and to manage the money supply should remain with an independent agency rather than with elected officials.

✓Reading Check **Summarizing** Why is discretionary fiscal policy used less and less frequently?

monetary policy actions by the Federal Reserve System to expand or contract the money supply in order to affect the cost and availability of credit *(also see page 400)*

CAREERS

Credit Manager

The Work

* Manage the preparation of financial reports
* Oversee a firm's granting of credit by establishing credit-rating criteria, determining credit ceilings, and monitoring the collections of past-due accounts
* Solicit business, authorize loans, and direct the investment of funds

Qualifications

* Ability to analyze detailed information and draw conclusions
* Excellent communication skills to explain complex financial data
* Expertise on government appropriations, budgeting, tax laws, and regulations
* Knowledge about global trade, changes in federal and state laws, and new financial instruments
* Bachelor's degree in business, finance, accounting, or a related field, with many positions requiring a master's degree in business administration, economics, finance, or risk management

Earnings

* Median annual earnings: $81,880

Job Growth Outlook

* Average

Source: *Occupational Outlook Handbook*, 2006–2007 Edition

C Critical Thinking

Speculating Ask: **Why might President Bush's proposed tax cuts not extend to the year 2010 and beyond?** *(Possible answer: Bush's term in office cannot extend past January 2009; the next president, as well as the Congress in 2009–2010, may not support Bush's tax cuts.)* BL

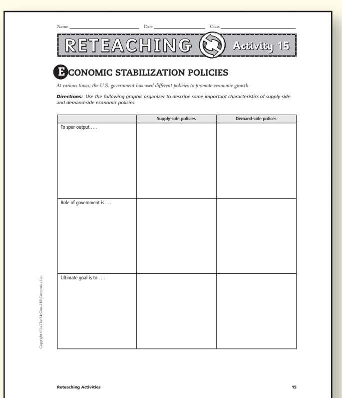
W Writing Support

Persuasive Writing Instruct students to search for recent news articles about the Fed in magazines, newspapers, and news Web sites. Ask students to write a letter to the editor expressing their opinions about the Fed's recent policies. Tell students to support their points with facts and convincing arguments. OL

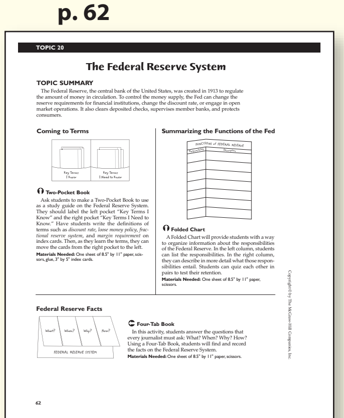
✓Reading Check **Answer:** Reasons include lags that occur after recognition of a problem, gridlock in Congress, and ideological preferences of politicians for structural policies.

Leveled Activities

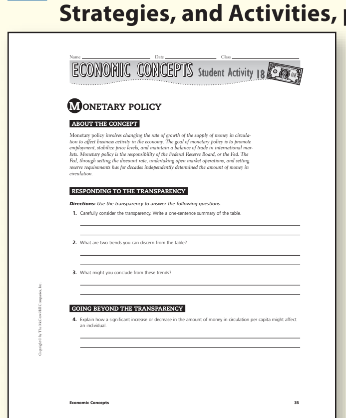
BL Reteaching Activities, p. 15



OL Reading and Study Skills Foldables, p. 62



AL Economic Concepts Transparencies, Strategies, and Activities, p. 35



D Differentiated Instruction

Visual/Spatial Have students draw a cartoon depicting how the views of an economist or economists can change. For example, a student may draw an economist sitting at a desk reading a book titled "supply-side economics." In a garbage can next to the desk is a book titled "demand-side economics." **OL**

C Critical Thinking

Making Predictions
Review with students the general concerns related to the issue of retiring baby boomers. **Ask:** **What economic problems do you think economists will focus on in the 2010s?** *(Answers may include bankruptcy of Social Security, massive national debt, and large trade deficits.)* **OL**

Caption Answer: Economists prioritize problems differently, they embrace theories based on the prevailing concerns of their times, and they have different ideologies.

Differing Opinions Economists have different ideas about economic policies, although they don't come to blows as in the cartoon. ***Why do economists differ?***

baby boomers people born in the United States during the historically high birthrate years from 1946 to 1964

Skills Handbook
*See page **R41** to learn about **Evaluating Information.***

Economics and Politics Today

MAIN Idea Current conditions shape the views of economists and policy makers.

Economics and You Have you ever perceived an issue to be a certain way and then found out later that it was completely different? Read on to learn why economists' views change as well.

Choosing which economic policies will work best is difficult. When economists offer proposals that sometimes seem contradictory, it makes choosing even more difficult. These differences of opinions among economists, however, are smaller than most people realize.

Economic Politics

In the 1800s, the science of economics was known as "political economics." After a while, economists broke away from the political theorists and tried to establish economics as a science in its own right.

In recent years, the two fields have merged again. This time, however, they have done so in a way better described as "economic politics." Today, politicians are concerned largely with the economic consequences of what they do. Most of the major debates in Congress are over spending, taxes, and other budgetary matters.

Why Economists Differ

Economists who choose one policy over another normally do so because they think that some problems are more critical than others. For example, one economist might think that unemployment is the crucial issue, while another believes that inflation is. Yet if we surveyed all economists on the best way to deal with one specific problem, their recommendations would be much more consistent.

Another reason economists differ is that most economic theories are a product of the times. The unemployment and other problems that occurred during the Great Depression influenced a generation of demand-side economists. Because the government sector was so small during the 1930s, supply-side policies designed to make government's role even smaller probably would not have helped much then.

Later, from the 1960s through 1980s, the monetarists gained influence because of the slow decline of discretionary fiscal policy. Then, by the 1980s, the ideological rejection of "big government" created a generation of supply-siders who thought that the key to economic growth was a smaller government.

By 2010 and beyond, the large population of retired **baby boomers**, who were born between 1946 and 1964, will have its own unique problems. The problems facing this group may well prompt another generation of economists to focus on a whole new set of issues. In the end, then, the views of economists are very much affected by the problems of the current moment.

Council of Economic Advisers

Generally, economists and politicians work together fairly closely. To help keep track of the economy, the president has a

Hands-On Chapter Project

Step 3

Effects of Government Stabilization Policies

Step 3: The Changing Nature of Economic Policy. Student groups will identify and categorize the differing views of economists over time.

Directions: Have students return to their project groups. Instruct each group to use library or reliable Internet resources to identify 10 different economists—one to represent each decade from the 1920s through the current decade. Inform students that each of their selected economists must have published a major economic work in the decade that he or she represents. For example, John Kenneth Galbraith with *The Affluent Society* (1958) and *The New Industrial State* (1967) could represent either the 1950s or 1960s. Ask each group to create a database for their 10 economists. Categories for these databases should include name, decade, major publications, economic theory (can be summarized into a paragraph), and major events that likely influenced the economists' views.

Describing Ask students to write a short paper discussing how economic theories change over time. **OL**

(Chapter Project continued in Visual Summary.)

Council of Economic Advisers, a three-member group that reports on economic developments and proposes strategies. The economists are the advisers, while the politicians direct or implement the policies. In its role as "the president's intelligence arm in the war against the business cycle," the council gathers information and makes recommendations.

The president listens to the economists' advice but may not be willing or able to follow it. For example, if the president **advocates** a balanced budget, the economic advisers may recommend raising taxes to achieve this goal. If one of the president's campaign pledges was not to raise taxes, however, the president might reject the advisers' suggestion and let a deficit develop.

Increased Public Understanding

Despite disagreeing on some points, economists have had considerable success with the description, analysis, and explanation of economic activity. They have developed many statistical measures of the economy's performance. Economists also have constructed models that are helpful with economic analysis and explanation. All of these tools are necessary if we are to understand the opportunity costs of the trade-offs we must make when we select one policy over another.

In the process, economists have helped the American people become more aware of the workings of the economy. This awareness has benefited everyone, from the student just starting out to the politician who must answer to the voters.

S Today economists know enough about the economy to prevent a depression like the one in the 1930s. It is doubtful that economists know enough—or can persuade others that they know enough—to avoid minor recessions. Even so, they can devise policies to stimulate growth, help disadvantaged groups when unemployment rises or inflation strikes, and generally make the American economy more successful.

✓Reading Check **Interpreting** What is the role of the Council of Economic Advisers?

Economics ONLINE
Student Web Activity Visit the *Economics: Principles and Practices* Web site at glencoe.com and click on *Chapter 15—Student Web Activities* for an activity on the Council of Economic Advisers.

Council of Economic Advisers three-member group that devises strategies and advises the president of the United States on economic matters

SECTION 3 Review

Vocabulary

1. **Explain** the significance of monetary policy, baby boomers, and Council of Economic Advisers.

Main Ideas

2. **Explaining** Why have structural fiscal policies replaced discretionary fiscal policies?
3. **Describing** What actions did the Fed take in response to the recession of 2001?
4. **Describing** Use a graphic organizer like the one below to describe the different types of fiscal policy.

Types of Fiscal Policy		
Type	Description	Example
Discretionary		
Passive		
Structural		

Critical Thinking

5. **The BIG Idea** Why do economists have differing views over which policy is most effective in producing stability and economic growth?
6. **Drawing Conclusions** Why do some people blame the Fed for the recession of 2001?
7. **Analyzing Information** Why might monetary and fiscal policy conflict during an election year?
8. **Analyzing Visuals** Look at the cartoon on the previous page. Why do you think economists care so strongly about their views?

Applying Economics

9. **Fiscal and Monetary Policy** Suppose that Congress passes a massive tax cut during an election year even though inflation is very high. What actions might the Fed take in response? Explain your answer.

S Skill Practice

Problems and Solutions

Ask: Do you think the United States could enter another Great Depression today? Why or why not? *(Students answering "no" may point out that economists now have a better understanding of how the economy works. Students answering "yes" may suggest that events overseas could trigger a depression.)* **OL**

✓Reading Check **Answer:** It gathers information, reports on economic developments, and proposes strategies to the president.

Assess

Use the Interactive Tutor Self-Assessment CD-ROM to review Section 3, and then assign the Section 3 Review as homework or as an in-class activity.

Close

Identifying Central Issues

Ask students to write a short paper explaining the central issues in this section. **OL**

Review SECTION 3

Answers

1. All definitions can be found in the section and the Glossary.
2. time lag between recognizing a problem and acting on it; Congressional gridlock; economic legislation is now often driven by ideology
3. lowered interest rates on a monthly basis to stimulate the economy
4. **Discretionary:** description—must be implemented by Congress, the president, or a governmental agency; example—federal expenditures to build a highway. **Passive:** description—occurs automatically when economy changes; example—unemployment insurance. **Structural:** description—designed to strengthen the economy over a period of time; example—Social Security
5. They have differing views on the most pressing economic problems.
6. Some believe that the Fed contributed to the 2001 recession by raising interest rates too much in 2000.
7. Politicians may implement certain economic policies to win votes, while at the same time the Fed may implement a contradictory policy that addresses another economic concern.
8. Answers will vary, but students should recognize that economists believe that economic policies affect millions of people.
9. The Fed would likely contract the money supply to reduce inflation.

CASE STUDY

Teach

S Skill Practice

Drawing Conclusions **Ask:** **What does the success of the Geek Squad suggest about Best Buy's product line?** *(Possible answer: The products Best Buy sells are complicated; when they break or do not function properly, the average person is not able to solve the problem without help.)* **OL**

Analyzing the Impact

Answers:

1. It is a business model that determined the lifestyle of Best Buy's most profitable customers. It helped Best Buy target the customer groups that would maximize company revenues.
2. by employing a tech support team (the Geek Squad) that provides emergency service and support for Best Buy customers

Additional Support

CASE STUDY

Best Buy Gets Better

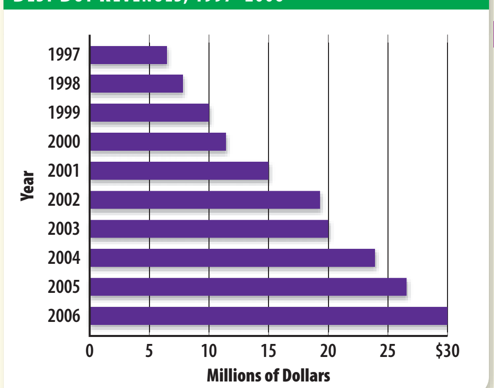
Too Big, Too Fast

In 1996 Best Buy found itself in a predicament. Despite astounding growth over a three-year period, the company had not changed the way it did business. As a result, its stock tumbled and profits dwindled. The company switched gears, opting for a smaller array of products, a new pricing strategy, and new store layouts.

Customer Focus

In addition, Best Buy turned to a business model called Customer Insight that determined the lifestyles of its most profitable customers. The five segments Best Buy identified include wealthy professionals desiring the best technology products, young males seeking the latest technology and accessories, fathers looking for technology to improve entertainment, mothers on the lookout for gadgets to enrich their children, and small-business owners who use technology to increase their profits. Best Buy began targeting these groups, increasing revenues from $7.8 million in 1997 to more than $30 million in 2006.

Best Buy Revenues, 1997–2006



Source: Best Buy annual reports

Geek Squad

Best Buy still faced strong competition from other technology retailers such as Circuit City. Enter, the Geek Squad. This army of 2,500 "agents" provides emergency services 24 hours a day, seven **S** days a week, 525,600 minutes a year to fix computers, printers, and networks for individual customers and businesses alike. The ability to provide full technology service and support for the products sold in stores helped Best Buy win back customers and shareholders.

Analyzing the Impact

1. **Summarizing** What is Customer Insight, and how did it help change the way Best Buy does business?
2. **Drawing Conclusions** How did Best Buy differentiate itself from other technology retailers?

Activity: Interdisciplinary Connection

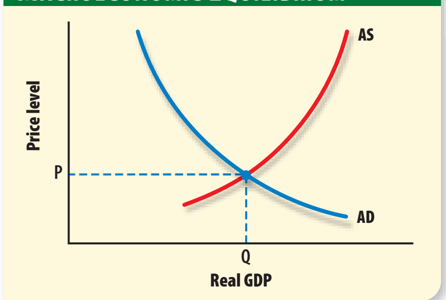
Daily Life Have students find a Best Buy advertisement, such as the ones commonly inserted into newspapers. Ask students to identify at least three products in the advertisement that a customer from each of the five target segments listed in this feature might buy (for example, a notebook computer might appeal to a wealthy professional desiring the best technology products; a high-definition TV might appeal to a young male seeking the latest technology). Instruct students to cut out the pictures of the products and create a collage that illustrates buying preferences of the five customer segments targeted by Best Buy. **OL**

Visual Summary

STUDY TO GO **Study anywhere, anytime!** Download quizzes and flash cards to your PDA from glencoe.com.

Aggregate Supply and Demand In order to understand the economy as a whole, we need to study aggregate supply and demand. The economy reaches macroeconomic equilibrium when aggregate supply and demand are equal at a given price level.

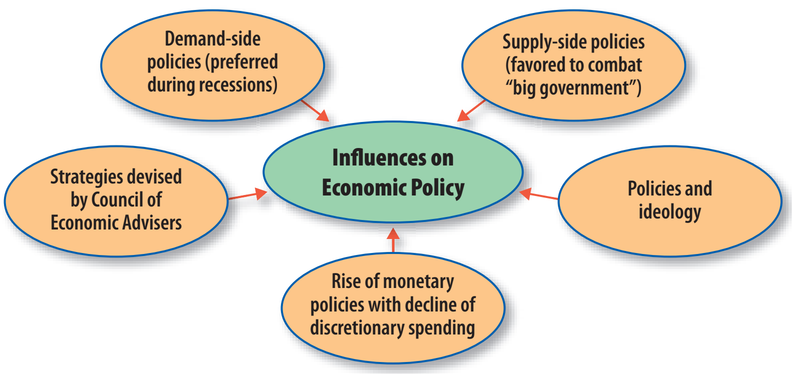
MACROECONOMIC EQUILIBRIUM



Stabilization Policies The government can pursue three different policies to stabilize and grow the economy.

Demand-Side Policies	Supply-Side Policies	Monetary Policies
• Stimulate consumption of goods and services (demand) • Introduced by John Maynard Keynes • Government's role is to offset changes in investment-sector spending • Includes automatic stabilizers	• Stimulate production of goods and services (supply) • Smaller role for government • Lower taxes • Difficult to predict results	• Focuses on money supply • Money supply to grow at a steady rate to match growth of real GDP and production • Difficult to time policy

Influences on Economic Policies Several factors influence economic policies.



Visual Summary

Analyzing Remind students that both supply-side policies and demand-side policies can impact the macroeconomic equilibrium. **Ask: Which direction would the macroequilibrium point move on the graph if supply-side policies were successful?** *(down and to the right)* **Which direction would the macroequilibrium point move on the graph if demand-side policies were successful?** *(up and to the right)* **OL**

Simulating Provide students with the following scenario: *The United States is experiencing a severe recession. Nationwide unemployment is at 10 percent, but in some regions it stands at 25 percent. Inflation, however, is running at an annual rate of 3 percent. Consumer and business spending are down. GDP has fallen 5 percent over the last 3 quarters, and government revenues have declined.* Have students select an economic policy—demand-side, supply-side, or monetarism—to bring the United States out of the recession. Direct students to write a brief report detailing and justifying the actions they would take. **AL**

Hands-On Chapter Project

Step 4: Wrap Up

Effects of Government Stabilization Policies

Step 4: Complete the Assessment. Students will synthesize what they learned in the first three steps.

Directions: Have students reassemble into their previously established project groups. Have students in each group compile the data they have gathered in the previous steps into a three-ring binder. Ask groups to write a short paper explaining how their findings in this project relate to the Big Idea. Instruct groups to next write an essay predicting which economic policy will likely prevail in the United States over the next decade. Students should explain the reasons for their selection. Have groups add their Big Idea papers and prediction essays to their binders before turning in their work. **OL**

ExamView® Assessment Suite

This easy-to-use software includes extensive question banks and allows you to create fully customized tests that can be administered in print or online.

Review Content Vocabulary

1.–12. Students' paragraphs will vary but should demonstrate understanding of economic stabilization policies.

Review Academic Vocabulary

13.–18. Students' sentences should reflect a clear understanding of the terms and the goals of the three economic policies.

Review the Main Ideas

19. the quantity of real GDP demanded is equal to the real GDP supplied

20. Supply curve: what a firm is willing to produce at various price levels. Aggregate supply curve: output of economy at various price levels; includes prices of everything produced.

21. how to increase real GDP without unduly increasing the price level

22. Increase AS: anything that decreases production costs. Decrease AS: the reverse. Increase AD: anything that increases consumer spending. Decrease AD: the reverse.

23. business investment sector

24. Multiplier: magnified effects of a change in investment spending. Accelerator: change in investment spending caused by a change in total spending.

25. by studying the growth rates of real GDP and productivity

26. deregulate business, cut spending and lower taxes, reduce federal agencies

27. recognition and implementation time lags, gridlock in Congress, and ideological differences among politicians

28. Business fluctuations are continually occurring.

29. Answers should show sound economic reasoning.

30. They disagree about the most severe problem plaguing the economy.

Critical Thinking

31. Expansive could cause inflation. Restrictive could cause a recession.

32. Aggregate refers to whole economy. Simple refers to single good or service.

33. Students may note that demand-side delays policies, supply-side lacks experience, and monetarist may not reduce unemployment.

CHAPTER 15

Assessment & Activities

Review Content Vocabulary

Use all of the terms below to write a paragraph about government policies to stabilize the economy.

1. aggregate supply
2. supply-side policies
3. fiscal policy
4. aggregate demand
5. monetarism
6. automatic stabilizer
7. deregulation
8. accelerator
9. macroeconomic equilibrium
10. monetary policy
11. wage-price controls
12. Keynesian economics

Review Academic Vocabulary

Use the words below to construct three sentences that summarize the goals of demand-side, supply-side, and monetarist economic policies.

13. unduly
14. framework
15. unstable
16. explicit
17. ideology
18. advocates

Review the Main Ideas

Section 1 *(pages 413–417)*

19. **Describe** the circumstances under which prices are consistent with a given level of real GDP.
20. **Explain** the difference between the supply curve of a firm and the aggregate supply curve.
21. **State** the major dilemma that faces economic policy makers.
22. **Identify** the factors influencing the increase or decrease of aggregate supply and aggregate demand by using a graphic organizer like the one below.

Aggregate Supply (AS) and Aggregate Demand (AD)	
Factors that increase AS	
Factors that decrease AS	
Factors that increase AD	
Factors that decrease AD	

Section 2 *(pages 419–427)*

23. **Identify** which component of GDP Keynes labeled as the cause of instability.
24. **Discuss** the effects of the multiplier and the accelerator.
25. **Describe** how monetarists determine the proper growth rate for the money supply.
26. **Explain** how supply-siders would reduce the government's role in the economy.

Section 3 *(pages 429–433)*

27. **Discuss** the difficulty of using discretionary fiscal policy.
28. **Explain** why new problems will arise in the economy, even as old ones are solved.
29. **State** an example of how politics sometimes overrides economic policies.
30. **Describe** how economists sometimes differ in their views about the economy.

Critical Thinking

31. **The BIG Idea** Why and how could monetary policy be destabilizing?
32. **Contrasting** How do aggregate supply and demand differ from simple supply and demand?
33. **Comparing** What are the limitations of demand-side, supply-side, and monetarist economic policies?

Economics ONLINE **Self-Check Quiz** Visit the *Economics: Principles and Practices* Web site at glencoe.com and click on *Chapter 15—Self-Check Quizzes* to prepare for the chapter test.

34. **Analyzing Information** How do the events of the 1980s and the early 2000s support or disprove the central supply-side position about the relationship between taxes, economic growth, and tax revenues? Provide examples in your answer.
35. **Drawing Conclusions** Why are the automatic stabilizers effective fiscal policies that counter business cycles?
36. **Contrasting** Compare the use of discretionary fiscal policy and monetary policy to offset the effects of a short recession. Which policy would you choose? Include reasons to support your choice.

Analyzing Visuals

37. **Synthesizing** Look at Figure 15.4 on page 422. Use what you have learned to explain what policies might make the demand curve shift. What effect does this have on aggregate supply?

Applying Economic Concepts

38. **Monetary Policy** At one time or another, some presidents have complained about the independence that the Fed enjoys when it conducts monetary policy. Do you think this independence is beneficial and should be maintained, or would you prefer that elected officials have more control over monetary policy? Support your answer.
39. **Fiscal Policy** Which fiscal policy do you think the government would use in each of the scenarios described in the table below? Explain your answers.

Scenario	Fiscal Policy	Explanation
Inflation is rising and real GDP is growing strongly		
GDP is down and the unemployment rate has increased by 10 percent		

Interpreting Cartoons

40. Look at the cartoon below. What is the topic of the cartoon? What point is the cartoonist making about the impact of tax cuts and the war in Iraq? How does the cartoonist illustrate this point?

"LOOK, KIDS! THEY'RE DIGGING YOUR SHARE OF THE NATIONAL DEBT!"

Thinking Like an Economist

41. Like demand-side and supply-side policies, monetary policies are designed to promote stable economic growth. The three approaches differ on what should be done to achieve this goal. Assume that real GDP growth was negative during the last quarter. Using Figure 15.5 as an example, construct a similar chart listing the policies that monetarists would follow to help the economy.

Writing About Economics

42. **Expository Writing** Some economists favor policies that stimulate demand, while others favor those that stimulate the supply of goods and services. Still other economists prefer policies based on the growth of the money supply. With which group of economists do you agree? Write a two-page paper outlining the policies and the reason for your choice.

Economics ONLINE

Have students visit the Web site at glencoe.com to review Chapter 15 and take the **Self-Check Quiz.**

34. Answers will vary, but students should use specific examples about tax revenues and economic growth in the 1980s and 2000s to support their answers.
35. They do not require any government action to take effect; thus, no time lags or political differences limit their effectiveness.
36. With discretionary fiscal policy, the government would increase spending to try to deal with the recession. With monetary policy, the Fed would increase the money supply to spur economic activity. Student policy preferences will vary but should be supported by sound economic reasoning.

Analyzing Visuals

37. Changes in taxes, transfer payments, and consumer saving could cause the demand curve to shift. Such changes would cause the aggregate demand curve to intersect with the aggregate supply curve at a different point.

Applying Economic Concepts

38. Answers will vary, but students should demonstrate understanding of the Fed and monetary policy.
39. Row 1: increase taxes; the government will gain a surplus and be able to pay down its debt.
    Row 2: increase spending; this will increase economic activity, creating jobs and GDP growth.

Interpreting Cartoons

40. the national debt; tax cuts and the war in Iraq are increasing the national debt; by showing the Iraq war as blasting a larger hole in an already vast canyon that represents the national debt

Thinking Like an Economist

41. Students' charts should demonstrate a clear understanding of monetarist policies.

Writing About Economics

42. Answers will vary, but students should support their preference with sound economic reasoning.