Introduction vi

UNIT I: ECONOMICS: THE SCIENCE OF CHOICE

Chapter 1: What Is Economics? 2
Personal Finance: Budgeting 16

Chapter 2: Economic Models 22
Personal Finance: Principles of Purchasing 38
Personal Finance: Consumerism 41

Chapter 3: Value and Demand 44
Personal Finance: Insuring Your Home, Auto, and Life 58

Chapter 4: Supply and Prices 64
Personal Finance: The Christian and Debt 80

UNIT 2: ECONOMICS OF THE NATIONS

Chapter 5: What Is the Economic Problem? 86
Personal Finance: The Consumer and Debt 102

Chapter 6: Economic Systems 106
Personal Finance: Types of Consumer Credit 122

UNIT 3: ECONOMICS OF THE BUSINESS FIRM

Chapter 7: Forms of Business Ownership 128
Personal Finance: Sources of Consumer Credit 142

Chapter 8: The Stock Market 146
Personal Finance: Creditworthiness 160

Chapter 9: Market Structure and Competition 164
Personal Finance: Cash Management 180

UNIT 4: ECONOMICS OF THE FINANCIAL MARKET

Chapter 10: Money and the Financial Market 186
Personal Finance: Opening and Maintaining a Transaction Account 202

Chapter 11: Central Banking 208
Personal Finance: Ways to Save 228

UNIT 5: ECONOMICS OF THE GOVERNMENT

Chapter 12: Measuring the Wealth of the Nation 234
Personal Finance: Understanding How Interest Works 252

Chapter 13: The Business Cycle and Unemployment **256**
Personal Finance: Savings Instruments *274*
Chapter 14: Inflation **278**
Personal Finance: Estate Planning *294*
Chapter 15: Fiscal Policy **300**
Personal Finance: Retirement Planning *318*
Glossary **322**
Index **331**
Photo Credits **337**

INTRODUCTION

Choices and consequences—each day you make choices, and each one has consequences. Many of those choices, and their consequences, seem rather insignificant. Others, though, even some you may have judged of little importance, can have considerable immediate and future impact—sometimes far more than you could have anticipated. The study of the short- and long-term effects of people's choices is a part of economics: the science of how and why people make the choices they do.

The purpose of this textbook is to provide you with a working knowledge of basic economic principles and to introduce you to factors that economists have identified as influences on your choices. This knowledge will assist you in understanding current economic issues and will help prepare you for the economic questions and challenges you will face on whatever path God leads you. This book takes a conservative approach to economic philosophy. It is not intended to be an exhaustive study of classical capitalist economics, but rather, its design is to give you the basic tools, the "nuts and bolts," of economics, such as fundamental laws and models. Your study will include such basic concepts as utility, opportunity benefit, opportunity cost, subjective value, and the laws of demand and supply. You will learn about economic systems, seeing both their strengths and weaknesses. You will be exposed to the economic workings of business firms and financial markets and to the business cycle. And by studying the concepts of GDP, unemployment, trade, inflation, and taxation, you will learn how an economy functions in today's world and how it affects you as an individual in that economy.

As you learn these concepts, you will be challenged to look at them from a biblical worldview. This will often require that you evaluate your own choices and assess their consequences. People are made in the image of God. The choices they make are not neutral. Economics is full of things that are good and bad, right and wrong, just and unjust. Being a Christian who glorifies God in all areas of his life means being someone who can apply the Bible to all kinds of economic realities in order to choose what is good, right, and just.

The Bible has a lot to say about economics. While it doesn't use most of the economic terms discussed in this textbook, it does tell us that "the eyes of man are never satisfied" (Prov. 27:20). It tells us about the basic nature of man. It tells us what we should and should not pursue (Luke 12:30, 31). The Bible also has a lot to say about money—where it comes from, how we should use it, and even how we should feel about it. Some ideas in economics contradict Scripture or encourage people to act unbiblically. You need to be able to recognize these and avoid them. Whatever your economic positions, you are a Christian first of all. To that end we have tried to consistently direct you to the Bible and biblical thinking.

Regardless of whether they are accountants, entrepreneurs, plumbers, teachers, or surgeons, Christians need to understand basic economic principles. In the United States we operate mainly under principles of free-market capitalism. While we support this system, we must also recognize its weaknesses. Although it works best when unregulated, because of man's sin nature, regulations are necessary. Balance resulting from sound judgment is the key.

Christians must also take heed that they live the economic principles they espouse. While opposing governmental interventions and efforts to redistribute the nation's wealth, they must not ignore their personal responsibility to help those in need. Showing love through giving manifests the character of God (John 3:16). Christians ought to be known as caring, generous people.

Luke 12:48 teaches that "unto whomsoever much is given, of him shall be much required." As you are exposed to a biblically based approach to economics, you will become accountable to appropriate what you learn. The real test will be if and how your choices change.

AT THE MARGIN

In economics the term *margin* refers to "value added." Economists often use the phrase *at* (or *on*) *the margin*. In keeping with this economic phraseology, this book contains material at the margin that is intended to add value to your understanding of the concepts and principles it presents. Such material includes definitions, explanatory notes, and biblical applications.

UNIT ONE

ECONOMICS: THE SCIENCE OF CHOICE

CHAPTER 1
WHAT IS ECONOMICS? — 2

Personal Finance: Budgeting —16

CHAPTER 2
ECONOMIC MODELS — 22

Personal Finance: Principles of Purchasing — 38
Personal Finance: Consumerism — 41

CHAPTER 3
VALUE AND DEMAND — 44

Personal Finance: Insuring Your Home, Auto, and Life — 58

CHAPTER 4
SUPPLY AND PRICES — 64

Personal Finance: The Christian and Debt — 80

CHAPTER FOUR

SUPPLY AND PRICES

4A SUPPLY — 65

4B DETERMINING PRICES — 71

In 2004 in the span of less than two months' time, four severe hurricanes made landfall in Florida. Ranging in intensity from category 2 to 4, hurricanes Charley, Frances, Ivan, and Jeanne caused catastrophic damage throughout much of the state. The fury of these storms severely damaged homes, cut off electric power for days or weeks, and left debris that hindered the movement of equipment and personnel needed for repairs and reconstruction. As a result of the widespread destruction, the demand for equipment and building materials—such as chain saws, gasoline-powered electric generators, and especially plywood—skyrocketed. Also, without electricity for air conditioning or refrigeration, there arose an enormous demand for ice to cool drinks on hot days and to preserve food. Keeping workers cool and fed so that they could rebuild required abundant resources.

However, because of the great demand for certain products, the prices of those products rose significantly immediately following each storm. Plywood sold at prices that were double the pre-storm amounts. For displaced residents, motels offered rooms at double the advertised rates. People began to complain of unfair pricing,

saying that just when they were in their greatest need, suppliers would raise the prices of essential goods and make it difficult to obtain them. The legislature passed laws against these practices, and thousands of Floridians called a special hotline to report instances of alleged price gouging.

Unfortunately, the laws that guaranteed consumers pre-hurricane prices also hindered the rebuilding process. As you will see in this chapter, high prices are the means whereby the market indicates to suppliers that it needs more supplies. High prices also provide the incentive for those producers to make additional goods and services available. When the state government enforced a limit on the prices that sellers could charge for their products, it eliminated an incentive for individuals and businesses to bring to the market greater quantities of necessary goods, such as plywood, generators, and ice.

High demand for certain products during hurricane season causes the prices of those products to rise.

One might respond that under emergency circumstances, it is the role of the government to provide these necessary goods to consumers. While the government certainly has a role to play in such situations, there is ample evidence that it cannot provide goods to consumers as quickly and efficiently as the free market. Moreover, when the government provides goods to consumers, it ultimately must increase taxes on all citizens to pay for those goods. In the end, therefore, consumers always pay, either directly or indirectly, for what the government supplies.

In this chapter you will see how supply helps to determine price in a free market and why the free market is more efficient at encouraging the correct supply of necessary goods, even during an emergency. The price of a good is not like an elevator that the government can raise and lower at whim. The market price of anything does not come from a law but from a compromise, an agreement between a buyer and a seller. In the previous chapter, you looked at this compromise from the demand side, or the buyer's point of view. Now you will examine the seller's perspective, or the supply side. Later, you will see how buyers and sellers agree, thereby reaching a market price. You will also learn how and why that market price can change and how a Christian should respond to price changes.

4A SUPPLY

Supply is the amount of goods and services business firms are willing and able to provide at different prices. For economists, business firms include all sellers of goods and services, not just major corporations.

THE LAW OF SUPPLY

As you recall from Chapter 3, the law of demand states that as the price of a good or service falls, other things being held constant, people will demand more of it and vice versa. The **law of supply**, on the other hand, holds that the higher the price buyers are willing to pay, other things being held constant, the greater the quantity of a

Whether their product is sheets of steel or bottles of sports drinks, suppliers will generally produce a greater quantity as the price rises.

Fig. 4-1 Supply Schedule

Price offered per candy bar	Quantity supplied
$1.90	5,000 bars
1.55	4,750
1.00	3,500
.80	1,000
.75	250

product a firm will produce and that the lower the price consumers are willing to pay, the smaller the quantity the supplier will produce.

To explain, let us return to the candy illustration from the previous chapter. This time, however, we will assume that you are not a customer but the owner of Candy City and that it costs you 70¢ to produce each So Good candy bar. Common sense says that if customers are willing to pay only 67¢ per bar, you would be unwilling to produce any because you would lose 3¢ on every bar sold. However, if the price that buyers are willing to pay rises above 70¢, you would be willing to start production, and the higher the price rises above 70¢, the more candy bars you would be willing to produce. Figure 4-1 presents a table with hypothetical data on the quantity of So Good candy bars you would produce at various prices. As a business owner you would recognize such a table as a **supply schedule**.

The information contained in a supply schedule could be more useful to you if it were plotted on a graph called a **supply curve**. Supply curves are positively sloped, meaning that as the price consumers

Fig. 4-2 Supply Curve

Fig. 4-3 Change in Quantity Supplied

will pay rises, suppliers become willing to provide greater quantities and that as the price consumers will pay falls, suppliers tend to produce fewer quantities. Whenever a change in the price consumers are willing to pay causes a change in the number of goods produced and sold, a **change in quantity supplied** has occurred, as seen in Figure 4-3.

CHANGES IN SUPPLY

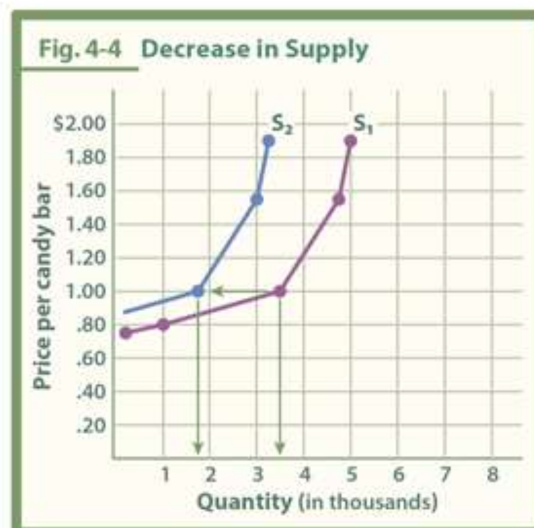
Just as a demand curve may shift to the left or right, a supply curve may shift to reflect **changes in supply**. A leftward shift indicates a **decrease in supply**, a situation in which suppliers produce less of their product at any given price. An **increase in supply**, shown in a rightward shift of the supply curve, demonstrates the willingness of business firms to produce more of their product at any given price. Figures 4-4 and 4-5 illustrate these two situations. Figure 4-4 illustrates a decrease in supply. Candy City shifts from being willing to supply 3,500 candy bars at $1.00 ($S_1$) to being willing to supply 1,750 candy bars at the same price (S_2). In contrast, Figure 4-5 demonstrates a rightward shift of the supply curve. Candy City moves from providing 3,500 bars at $1.00 ($S_1$) to supplying 4,250 at the same price (S_2).

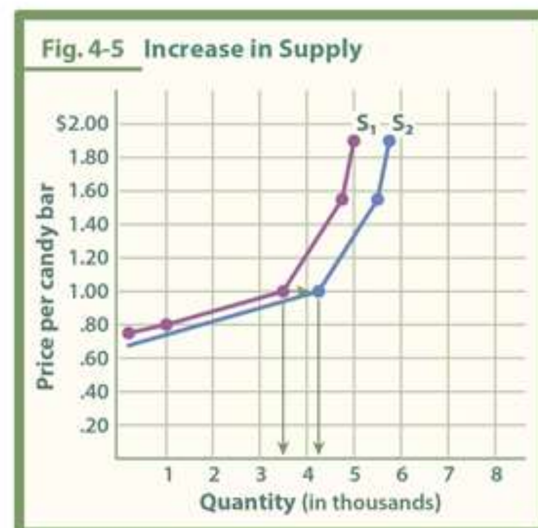
It is understandable why business firms would be willing to provide more or less of a good as customers become willing to pay more or less, but what could cause a business to supply more or less of a product when its price has not changed? Economists have pinpointed three factors that lead to this phenomenon:

1. Changes in technology
2. Changes in production costs
3. Changes in the price of related goods

Changes in Technology

Technological advances are improvements in the tools used to produce goods and services. Recent technological advances include the

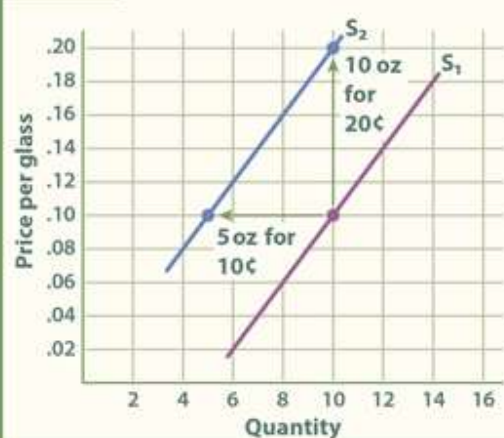




Changes in technology resulted in changes in the form and functions of calculators.

use of computerization and automated production machinery. As manufacturers improve the tools of production, businesses are able to offer more of the product at the same price (or the same amount at a lower price).

Consider the case of the electronic calculator. In the early 1970s a "pocket" electronic calculator (which was in fact very large) had the ability to perform only limited mathematical functions, and it cost around $75. As time passed and the tools of production improved, the components were miniaturized and the quality increased dramatically. As the tools used in producing calculators improved, businesses were able to manufacture them less expensively. The same amount of money that the producers once spent to manufacture a few early calculators now allowed them to make many more of the modernized versions. Supplies increased rapidly, and prices began to drop. For the $75 a person had to pay for a single calculator in 1973, he could now buy fifteen or more.



Changes in Production Costs

Business firms must pay for the natural resources, labor, and capital that go into their products. If a firm's costs rise, it must decrease the quantity of what it provides at the same price. For example, Beth, a business-minded ten-year-old, decided to open a lemonade stand in her front yard. With a hundred-ounce bottle of lemonade costing $1, Beth charged 10¢ per ten-ounce glass (we are ignoring profit for the moment). Her venture was so successful that she had to buy another hundred-ounce bottle the next day, but to her surprise and disappointment, its price had risen to $2. Making some quick mental calculations, she determined that for the same ten-ounce glass she would have to raise her price to 20¢. After Beth changed her sign to reflect the higher price, her business dropped off dramatically. Concluding that the price was out of the reach of her