



Sharp / Register / Grimes

# Economics of Social Issues

Nineteenth Edition

**This  
International  
Student Edition  
is for use  
outside of  
the U.S.**

McGraw-Hill International Edition



# Contents

## Preface v

### 1

#### **Alleviating Human Misery: The Role of Economic Reasoning 2**

- World Poverty and Economics 4
  - Our Insatiable Wants* 4
  - Our Limited Means* 5
  - The Capacity of the Economy to Produce* 6
  - Assessing Well-Being Using GDP* 12
- Causes of Poverty and Requisites of Economic Growth 19
- Can Governments Help? 21
  - Governments of LDCs* 21
  - Governments of DCs* 22
- Summary 23

### 2

#### **Economic Systems, Resource Allocation, and Social Well-Being: Lessons from China's Transition 28**

- Economic Systems 31
  - Pure Market Economy* 31
  - Pure Command Economy* 32
  - Mixed Systems* 32
- Resource Allocation in a Market Economy 33
  - Market Structure* 33
  - Market Forces* 35
  - Competitive Market Equilibrium and Social Well-Being* 43
- Resource Allocation in a Command Economy 46
  - Centralized Planning* 47
  - Problems with Centralized Planning* 49
- The New Chinese Economy 52
  - China's Transition to a Market-Oriented Economy* 52

*China's Transition to Markets: What Are the Facts?* 55

*Problems of Transition in China* 57

Summary 60

### 3

#### **Government Control of Prices in Mixed Systems: What Are the Actual Outcomes? 66**

- Price Ceilings and Floors 70
- Rent Controls 71
  - Demand* 71
  - Supply* 73
  - Price* 73
  - The Effects of Rent Controls* 74
- Minimum Wages 76
  - Market Demand for Labor* 76
  - The Demand for Labor by One Employer* 78
  - Market Supply of Labor* 81
  - The Labor Market* 83
  - The Effects of the Minimum Wage* 84
- Summary 89

### 4

#### **Pollution Problems: Must We Foul Our Own Nests? 94**

- What Is Pollution? 97
  - The Environment and Its Services* 97
  - Recycling of Wastes and the Concept of Pollution* 97
  - Common Forms of Pollution* 98
- Markets, Resource Allocation, and Social Well-Being: A Recap and Extension 100
  - Demand, Marginal Private Benefit, and Marginal Social Benefit* 101
  - Supply, Marginal Private Cost, and Marginal Social Cost* 103
  - The Market and Social Well-Being* 104

Economics of Pollution 105  
    *Why Polluters Pollute* 105  
    *Pollution and Resource Allocation* 106  
    *The Appropriate Level of Pollution Control* 110  
What Can Be Done about Pollution? 112  
    *Direct Controls* 112  
    *Indirect Controls* 113  
    *Creation of Pollution Rights Markets* 115  
Summary 116

## 5 Economics of Crime and Its Prevention: How Much Is Too Much? 122

What Is Crime? 125  
    *Immorality?* 125  
    *Illegality?* 125  
    *Classification of Criminal Acts* 126  
The Costs of Crime 127  
Different Types of Goods and Services 128  
    *Private Goods and Services* 129  
    *Semiprivate Goods and Services* 129  
    *Public Goods and Services* 130  
    *The Free-Rider Problem* 130  
    *Government Production of Public Items* 131  
The Economics of Crime Prevention  
Activities 131  
    *The "Optimal" Level* 131  
    *Allocation of the Crime Prevention Budget* 134  
    *Changing the Legal Status of Goods and  
Services* 135  
    *Causes of Criminal Activity* 138  
Summary 141

## 6 The Economics of Education: Crisis and Reform 146

The Crisis in K–12 148  
K–12 as a Purely Private Market 150  
Potential Shortcomings of a Purely Private  
Market for K–12 155  
    *Positive Externalities in Consumption* 155  
    *Lost Social and Cultural Cohesion through  
Segregation* 161  
    *What of Equal Opportunity?* 162

Proposals for Reform in the Current  
K–12 System 163  
    *School Choice and Vouchers* 163  
    *Class-Size Reductions and Other School  
Resource Issues* 170  
    *Reform Proposals: A Postscript* 172  
Summary 173

## 7 Poverty and Discrimination: Why Are So Many Still Poor? 178

Poverty in Terms of Absolute Income  
Levels 181  
    *What Is Poverty?* 182  
    *Who Are the Poor?* 183  
Poverty in Terms of Income Distribution 185  
    *Income Inequality* 187  
The Economic Causes of Poverty 188  
    *Determinants of Resource Prices and  
Employment* 188  
    *Determination of Individual or Family  
Income* 189  
    *Determinants of Income Distribution* 189  
    *The Effects of Discrimination on Income* 191  
Evidence of Discrimination in Our  
Economy 192  
    *Wage Discrimination* 193  
    *Employment Discrimination* 194  
    *Occupational Discrimination* 194  
Government Attempts to Alleviate  
Poverty 195  
    *The Old Federal Welfare System* 196  
    *Problems with the Old Welfare System* 198  
    *Welfare Reform and the New System* 199  
Using Tax Policy to Fight Poverty 201  
    *The Earned Income Tax Credit* 202  
    *The Negative Income Tax Proposal* 204  
What Can Be Done about  
Discrimination? 205  
    *Reduce Tastes for Discrimination* 205  
    *Reduce Market Imperfections* 206  
    *Reduce Discrimination in Development of Human  
Capital* 207  
    *Reduce Occupational Segregation* 207  
Summary 208

**8****The Economics of Monopoly Power:  
Who Does What to Whom? 214**

## The Economics of Monopoly Power 217

*What Is Monopoly Power?* 217*Outputs and Prices* 219*Entry Restrictions* 228*Nonprice Competition* 231

## Should We Fear Monopoly Power? 231

*Outputs and Prices* 232*Entry Restrictions and Resource Allocation* 233*Nonprice Competition* 234*What of Bigness?* 234The Peculiar Case of Natural  
Monopoly 236*When Should Government Regulate**Business?* 239*Regulation and Corporate Responsibility* 241

## Summary 242

**9****The Economics of Professional Sports:  
What Is the Real Score? 248**

## The Professional Sports Business 250

*Organizational Structure* 251*Teams and Players* 251*Economic Analysis and Professional Sports* 252

## The Product Market 253

*Cooperation among Teams* 253*Cartels* 253*Coordinated Behavior* 255*Pricing and Output for Broadcast Rights* 256*The Number and Location of Teams* 259*The Stadium Controversy* 260

## The Resource Market 261

*The Employment of Players* 261*Monopsony* 262*Wages and Employment in a Monopsony* 263*Free Agency* 266*Labor Disputes* 267*Do Professional Athletes Earn Their Pay?* 269*Illicit Drugs and Professional Sports* 270*The Case of Major League Soccer* 271

## Summary 273

**10****Competition in the Global Marketplace:  
Should We Protect Ourselves from  
International Trade? 278**The Controversy over International  
Trade 280*The Protectionist Viewpoint* 281*The Free Trade Viewpoint* 282

## The Economics of the Global Marketplace 282

*How Trade Takes Place* 282*Production and Consumption Possibilities* 283*The Principle of Comparative Advantage* 286*How International Trade Is Financed* 287*International Trade Restrictions* 290

## Analysis of the Controversy 296

*Protection from Cheap Foreign Goods* 296*Outsourcing of Service Jobs* 297*Payments Problems* 298*Protection of Key and Infant Industries* 300*Protection of the Environment and Human Rights* 300

## Today's Global Trade Environment 301

*The World Trade Organization* 302*Common Markets* 302

## Summary 306

**11****Economic Growth: Why Is the Economic  
Road So Bumpy? 312**

## The Concept of Economic Growth 315

*What Is Economic Growth?* 315*The Rate of Growth* 315Short-Run Fluctuations in Economic  
Growth 319*What Are Business Cycles?* 319*Theories of the Business Cycle* 321

## The Determinants of Economic Growth 324

*Availability of Economic Resources* 324*Productivity Factors* 327

## The Recent Slowdown in Growth 329

*Contributing Factors* 329*The 2001 Recession* 331*The 2007 Peak and Beyond* 333*Where Do We Go from Here?* 334

## Summary 336

**12****Money, Banking, and the Financial System: Old Problems with New Twists 342****What Are Banks? 344***Commercial Banks 344**Investment Banks and Insurance Companies 345***What Is Money? 346***Functions of Money 347**The Money Supply (M1 and M2) in the United States 347***The Process of Creating Money 349***Commercial Banks and Other Depository Institutions 349**Banking Regulation 350**Balance Sheet of a Bank 350**The Fractional Reserve Banking System 351**Demand Deposit Creation 351***The Issue of Control 353***The Federal Reserve System 353**Federal Reserve Controls 354**Federal Reserve Targets 355***The Money Supply, Interest Rates, and the Price Level 356***Interest Rates 357**Quantity Theory of Money 359***The Financial Crisis of 2008 359***The Home Real Estate Market 360**Financial Instruments and Accounting Rules 362**Fall 2008 363**The Future 364***Summary 364****13****Unemployment and Inflation: Can We Find a Balance? 368****What Is Unemployment? 370***The Labor Force 371**Unemployment in a Market Economy 373***Analysis of the Unemployment Problem 375***Types of Unemployment 375**Further Dimensions of the Unemployment Problem 376***What Is Inflation? 378***How Is Inflation Measured? 378**Rate of Inflation 380***Economic Effects of Inflation 381***Equity Effects 381**Efficiency Effects 382**Output Effects 382***Economic Analysis of Unemployment and Inflation 383***Circular Flow of Economic Activity 383**Aggregate Demand 384**Aggregate Supply 388**Aggregate Demand and Supply 391**Reasons for Deficient Aggregate Demand 392**Reasons for Weak Aggregate Supply 394***Possible Trade-offs and Policy Options 395***The Phillips Curve 396**Policy Problems 397***Summary 398****14****Government Spending, Taxation, and the National Debt: Who Wins and Who Loses? 402****What Are People Afraid Of? 404***Size of Government 404**Tax Inequities 405***The Problem of Size 405***Government Expenditures 406**Government Receipts 408***Economic Analysis of the Problem of Size 409***An Efficient Level of Government Expenditures 409**Public Goods 409**External Benefits and Costs 410**Income Distribution 412**Summary 412***Tax Principles and Analysis 412***Tax Equity 412**Tax Efficiency 414**Principles of Shifting and Incidence 414***The American Tax System 418***Federal Tax System 419**The Personal Income Tax 420*

<b>The Beginning of a New Century</b>	422
<i>Economic Effects of Government Borrowing</i>	422
<i>Economic Effects of Federal Debt Retirement</i>	423
<i>Recent Tax Reforms</i>	423
<i>The Financial Crisis of 2008</i>	424
<b>Summary</b>	424

## 15

### **Social Security and Medicare: How Secure Is Our Safety Net for the Elderly?** 428

<b>Social Insurance</b>	431
<b>Social Security</b>	432
<i>A Brief History of Social Security</i>	432
<i>The Current Status of Social Security</i>	434
<b>The Economic Effects of Social Security</b>	437
<i>Income</i>	437
<i>Labor Supply</i>	438
<i>Saving and Investment</i>	439
<b>The Future of Social Security</b>	442
<i>The Financial Dilemma</i>	442
<i>Possible Solutions</i>	443

<b>The Market for Health Care:</b>	
<b>A Brief Overview</b>	445
<i>The Nation's Health Dollar: Where It Came         From and Where It Went</i>	445
<i>Health Expenditure Growth</i>	447
<i>Government Role in Health Care Financing</i>	447
<i>The Decline in Importance of Private         Health Insurance</i>	448
<b>The Medicare Program</b>	448
<i>Coverage</i>	448
<i>Financing</i>	450
<i>Provider Payments</i>	450
<b>The Economic Effects of Medicare</b>	451
<b>The Future of Medicare</b>	452
<i>The Financial Dilemma</i>	452
<i>Possible Solutions</i>	453
<i>The Medicare Modernization Act</i>	454
<b>Summary</b>	454

## **Glossary** 459

## **Index** 469