

AMERICAN FREE ENTERPRISE

Promoting Growth and Stability

- ① How do you track economic health?
 - Gross Domestic Product (GDP)
 - The total value of all final goods and services produced in an economy
 - Business cycles
 - A period of expansion and contraction lasting a significant amount of time
 - Government tries to prevent drastic economic ups and down (boom and bust cycles) through its policies

Technology and Productivity

- ⦿ Increasing productivity (shifting the production possibilities frontier) ensures that the American standard of living continues to increase. How?
 - Work ethic
 - Technological progress
- ⦿ Government's role?
 - Fund research and development
 - Government research
 - Patents—the exclusive right to produce and sell a new product for 20 years
 - US Constitution Article 1, Section 8 gives Congress the power to do this

Public Goods

- ⦿ Public good: a shared good or service for which it would be inefficient or impractical
 - 1) to make consumers pay individually, and
 - 2) to exclude nonpayers
- ⦿ The number of users does not reduce the benefits to any one user
- ⦿ Examples:
 - National parks
 - Monuments
 - Dams
 - Highways

Public Goods and Cost

- ⦿ When a good or service is public:
 - The benefit to each individual is less than the cost that each would have to pay if it were provided privately, and
 - The total benefits to society are greater than the total cost
- ⦿ The market would never provide the good
 - Why not?

- ⦿ Because there is no profit motive to do so

Market Failures

- ⦿ Market Failure:

- A situation in which the market, on its own, does not distribute resources efficiently

Imagine that you are an executive
at a company that builds roads—
group activity



Externalities

- ◎ Externality:
 - An economic side effect of a good or service
- ◎ Positive Externalities
 - Someone buys an old, rundown house and fixes it up
 - Externality: Neighbors receive higher property values and a better view

⦿ Negative Externalities

- Part of the cost of producing a good or service are paid for by someone other than the producer
- Examples:
 - A paper mill dumps harmful chemicals into a river. Downstream cities pay to install equipment to clean up the chemical at the water treatment plant—the full cost of producing the paper is paid—in part—by the community

Government Response

- ⦿ When externalities are present, there is a market failure
- ⦿ Government's role:
 - Encourage the creation of positive externalities
 - Education, for example
 - Limits negative externalities
 - Acid rain is part of the cost of producing power by burning coal
 - Damage occurred to communities downwind from the powerplant
 - Costs of the electricity were paid by persons other than the producer

Response to Externalities

- ⦿ Government requires cars to have a catalytic converter that limits emissions
- ⦿ Environmental Protection Agency offers incentives to companies that put scrubbers on their power plants