Final Exam Review

Economics with Financial Literacy

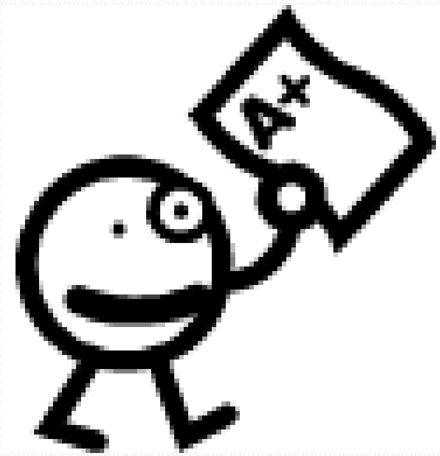
Essentials

Apply these concepts to real life

Module 1	Module 2	Module 3	Module 4	Module 5	Module 6
• Opportunity cost • ROTTEN • TRIBE • Equilibrium • Functions of money • Features of Money	• Credit • Types of taxes • Budget changes • Fixed and variable costs • Investment type • Investments and age to invest	• Factors of production • Market structures • Business organization types • Apply PPC graph • Marginal cost analysis	• Fiscal policy monetary Policy • Expansionary tools • Contractionary tools • Business cycle • Price ceiling • Price floor • Rent control • Federal Reserve Structure	• Trade barriers • Free trade • Outsourcing • Economists and theories • Adam Smith • Types of economies • Economic Systems • Emerging, Developed, Developing	• Externalities • Flow Diagram • Economic relationships

DON'T FORGET TO USE YOUR MODULE PRE-TESTS AS STUDY GUIDES

JUST OPEN YOUR COMPLETED PRE-TESTS AND YOU WILL SEE ALL THE CORRECT ANSWERS HIGHLIGHTED!!!!



Basic Economic Concepts

- Economics is about <u>choice</u> and how we get the things that we need. Your economic situation, in the future, will depend on the career you choose and the extent of your wants and needs.
- <u>Scarcity</u> means that we must all make choices. We have unlimited wants and needs, but a limited about of resources such as time and money.
- <u>Opportunity cost</u> is what we sacrifice to get something else. Ask yourself the question, "What opportunity am I missing out on by choosing something else?" It is the choice that always comes in second!
- If you are undecided about a choice, create a T-chart and list the costs and benefits. This should help you make a decision.
- The basic economic questions are:
- 1. what to produce
- 2. how will it be produced
- 3. for whom will it be produced

Demand

- Demand is the quantity of a product that consumers are willing to buy at a given price.
- If demand increases, the demand curve will shift to the right. If demand decreases the demand curve will shift to the left, “left is less”.
- In all graphs Quantity goes along the bottom of your graph and Price goes up! Just remember, prices always go up!

TRIBE

(What makes the whole demand curve shift? It depends on what the tribe of people are buying!)

- T – tastes and preferences; do consumers want what you are selling?
- R – related items; if the demand for peanut butter goes up, the demand for jelly will go up also.
- I – income; what is the average income of your customers? The more money they have, the more they will spend.
- B – buyers; how many people live within a 5 mile radius of your store? Less people equals less customers
- E – expectation of price; when oil is expected to rise, everyone fills their gas tanks and demand increases.

Supply (how much is going to be produced?)

- Supply is how many goods and services will be available at a given price.
- When supply increases, the supply curve will shift to the right, if it decreases it will shift to the left "left is less".
- S"up"ply curves go up from bottom left to top right.

ROTTEN

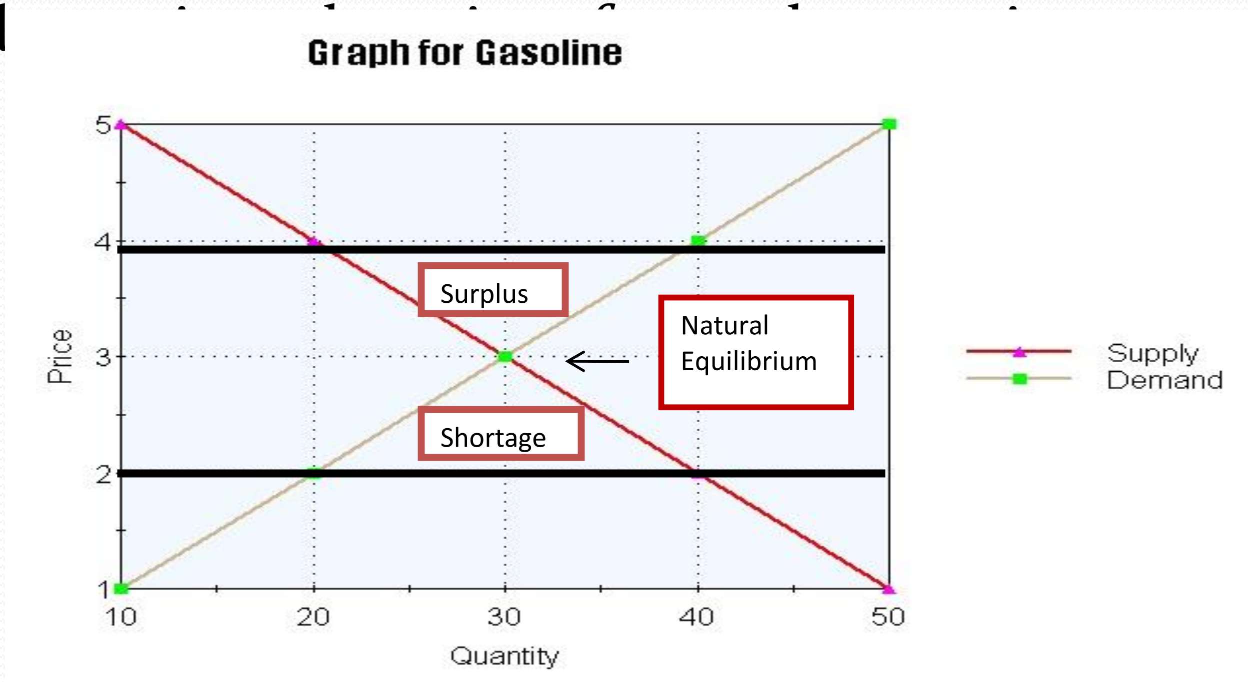
(Events that affect supply; it's ROTTEN that they always run out of the best products at Christmas)

- R – resources; cost and availability.
- O – other goods prices; how much are other supplies charging?
- T – taxes; if tax incentives are provided, supply will increase. If the taxes are higher, the supply will decrease and the curve shifts to the left.
- T – technology; if new technology makes the product/service cheaper to produce the supply will go up.
- E – expectations of the supplier; a planned increase in the supply of roses right before Valentines Day.
- N – number of competitors. As more competitors enter the market, each supplier will supply less, the curve will shift to the left.

Supply and Demand

(they meet and have a picnic at “equilibrium point”)

- The equilibrium point is where supply and demand meet; this d … given time.



If the equilibrium price is too low ($2.00) there will be a shortage. If the equilibrium price is too high ($4.00) there will be a shortage.

Green Definitions

- Currency – paper money and coins.
- Money – includes currency, credit cards, debit cards, rice, and anything of value.

“Money is a matter of functions four—a medium, a measure, a standard, a store.”

- Medium – money can be used for exchange
- Measure – money can be used to determine the value of an item
- Standard – money has one standard that we all follow
- Store – money holds or “stores” it’s value

Characteristics of Money (ADDPSS)

- Accepted – people are willing to accept
- Divisible – it can be divided into smaller parts
- Durable – long lasting
- Portable – you can carry it around
- Scarce – it doesn't go on trees (sorry)
- Stable in value – The value of money does fluctuate, but overall it remains stable.

Top 10 financial skills for teens

1. Balance a checkbook
2. Budget money
3. Finance college
4. Establish credit
5. Determine wants vs. needs
6. Deal with debt
7. Pay taxes
8. Consider all costs
9. Save for the future
10. Stretch a dollar

Want or Need?

- Needs – food, clothing, shelter, job
- Wants – expensive food, expensive clothing, expensive shelters and a different job.

Is this a want or need?

- Cell phone
- Car
- I-pod
- Computer
- Bicycle

Budget Categories (are these wants or needs?)

- Car payment
- Gas
- Car insurance
- Cell Phone
- Food
- Movies
- Rent
- Personal Care
- Clothing
- Savings
- Gifts

The of Law of Diminishing Marginal Utility

- The first chocolate bar you eat will taste better than the second, third, etc. The amount of “utility” of a good or service diminishes as you acquire more of the same item. Can you think of more examples?

How to Choose a Career

- Education requirements
- Salary/benefits
- Job responsibilities
- Working conditions
- Opportunities for advancement
- Costs of this career
- Benefits of this career

Money and the Government

- The government needs money to operate. They get their money from taxes.
- Direct taxes go directly to the government
- Indirect taxes are collected by someone else and then sent to the government. Gasoline taxes are an example of an indirect tax.

Tax Systems

- Proportional (flat tax) – everyone pays the same percentage on their income.
- Regressive – as your income goes up, the proportion of your income that goes toward taxes goes down.
- Progressive – the more money you make, the more you have to pay in taxes.

Investing Options

(the higher the return, the higher the risk , “no pain, no gain”.)

- Stocks – risky but can have a large return on your money
- Mutual funds – a fund made up of many different stocks.
- Bonds – Government bonds are very safe, but have a very low rate of return.
- Savings accounts - safe

(FDIC – Federal Deposit Insurance Corporation – insures your deposit up to $250,000)

- Money Market Funds – safe investment if in a bank
- Gold – fairly safe, hard asset.

Definitions

- Diversify – spread out among many investments
- Asset allocation – how your investments are distributed
- Compound interest – interested is calculated daily on the new account balance
- Dividends – payments to shareholders when a company makes a profit
- Exchange rate – how much you need of one currency to buy another currency.
- Stock market index – an index based on the value of a conglomeration of stocks.

Credit

- There are many different types of credit
  - Credit cards – balances represent debt owed to a creditor
  - Mortgages – a type of home loan
  - Installment loans
  - Service credit
- The most important thing to think about when taking out a loan or credit is the interest rate
- When you buy with credit, although you get the item right away, you pay more for it over time
  - It is always cheaper to pay with cash
- Treat your credit like your skin – it is always with you. ☺

Budgeting

- A budget is a plan that tracks income and expenses
- In a good budget, your income should exceed your expenses
  - When figuring your income, only figure in your Net Income (Gross Income – Taxes)
  - To figure out your Net Income…
    - Gross Income x Tax Rate = Taxes
    - Gross Income – Taxes = Net Income
    - $25,000 x 10% = $2500
    - $25,000 - $2500 = $22,500
- Two types of costs – variable and fixed – it is always easier to cut your variable (changing) costs

Entrepreneurs

- Entrepreneurs have helped shaped American society through taking risks.
  - Americans from diverse backgrounds not only helped to contribute to the development of the US, but continue to help shape our society.
- Important Entrepreneurs
  - James Cash Penney – department stores
  - George Washington Carver – agriculture innovations
  - Margaret Rousseau – invented penicillin
  - An Wang – pioneer in digital technology
  - Madame C.J. Walker – beauty products
  - Howard Shultz – Starbucks
  - Samuel F.B. Morse – telegraph
  - Joseph Unahue – food distributor

Factors of Production

- Land – natural materials needed for production
- Labor - The human work that goes into the business— physical and mental skills
- Capital - The tools humans create to make the business more efficient— financial, and physical
- Entrepreneurship – a component of labor – it is the assumption of all risks to make a business work – responsible for making decisions in the business
- Be able to give examples of each of the factors for the final exam.

Business Structures

- Sole Proprietorship – least expensive and easiest to start; one owner; owner keeps all profits
- Partnership – two or more owners; share risks; share profits; can share work hours;
- Limited Liability – owners have protection of their personal assets (personal property and investments)
- Corporation – most expensive to start; owned by stockholders; often used in order to expand a business

Market Types

- Monopoly – least business competition, one seller in the market; high barriers to entry, difficult to become and stay the sole producer of a good or service; sometimes occurs naturally, firm behavior that abuses the position, such as setting **extremely** high prices, is illegal in the United States; owners can set prices, but consumers have no choices
  - Vertical (buy up all of the levels of production) and Horizontal (similar businesses combine) consolidation are used to gain more control over the product market
- Oligopoly – market is dominated by few firms who can exert control over the market for their products, often working together to determine price and production quantity.
  - Collusion – firms will work together to set prices
- Monopolistic competition – relatively few barriers to entry; many sellers with differentiated product (lots of clothing manufacturers)
- Pure competition - easy entry into the market; equal product information for sellers and buyers; firms are constantly trying to determine how their competitors and consumers will behave. – this is the most competitive form – perfectly elastic demand curve (vertical line) – sellers have little or no price control – most of the products within a market are the same (apples 2 apples)

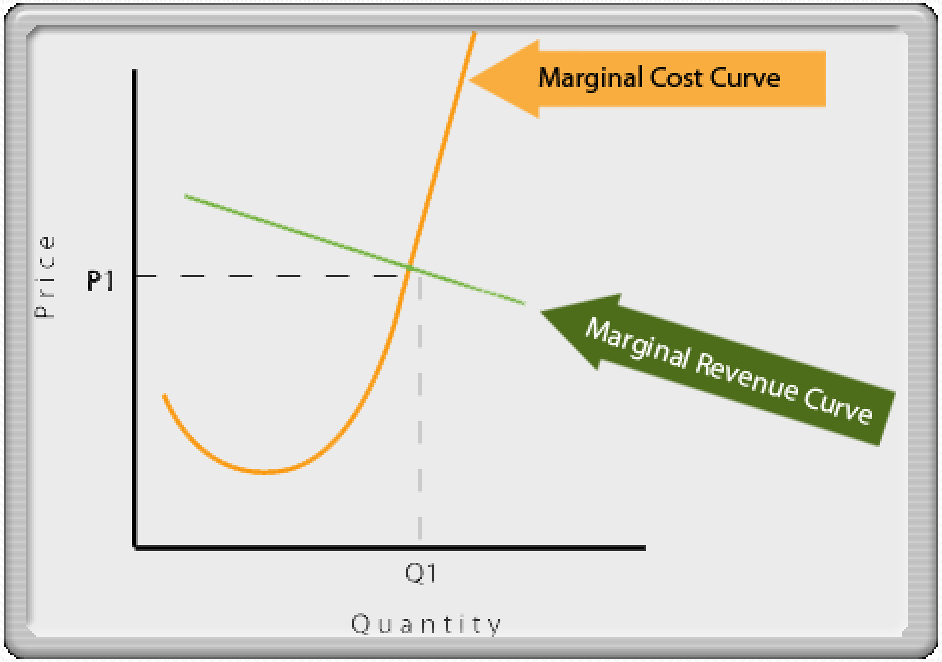
Non-price Competition

- Purpose is to distinguish their product from other company's products
- Mostly used in the Monopolistic Competition Market
- Examples
  - Advertising – make wants feel like a need, targets fears, social values, and rituals
  - Improving product quality
  - Improving customer service

Marginal Cost Analysis

- Marginal cost = the cost to produce 1 extra unit of a good or service
- Marginal Cost Analysis helps a firm to determine the most efficient price and quantity production levels
- First step is to determine fixed and variable costs for specified quantities of a product
- Business revenue is collected through product sales

Marginal Cost Analysis



Where the two lines meet is the most profitable place to produce.

Law of Diminishing Marginal Returns – at some point, adding resources will result in less output per additional unit of product. This causes the shape of the Marginal Cost curve.

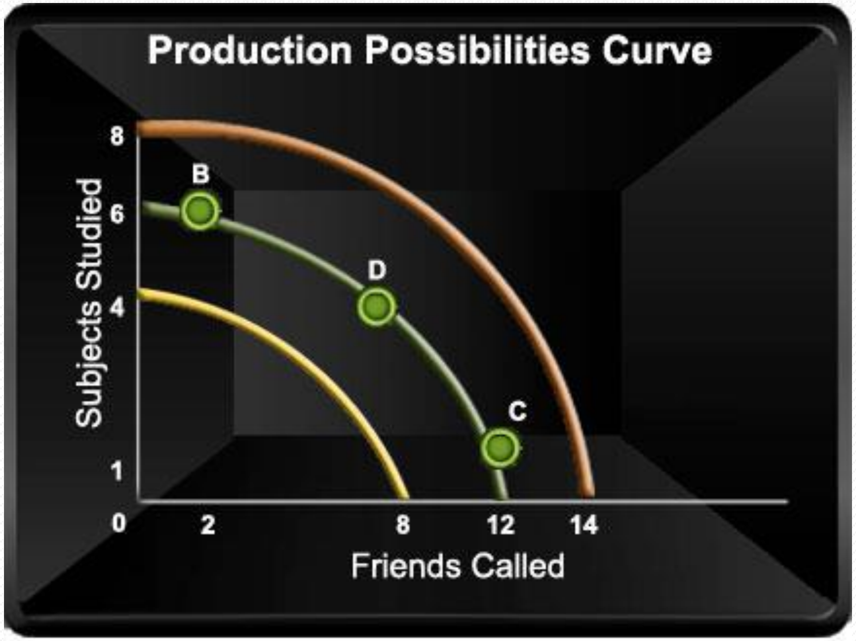
Go back and review how to figure out the Marginal Cost and Marginal Revenue. Remember it is the difference between the amount you have and the next unit produced.

Supply and Demand of Labor

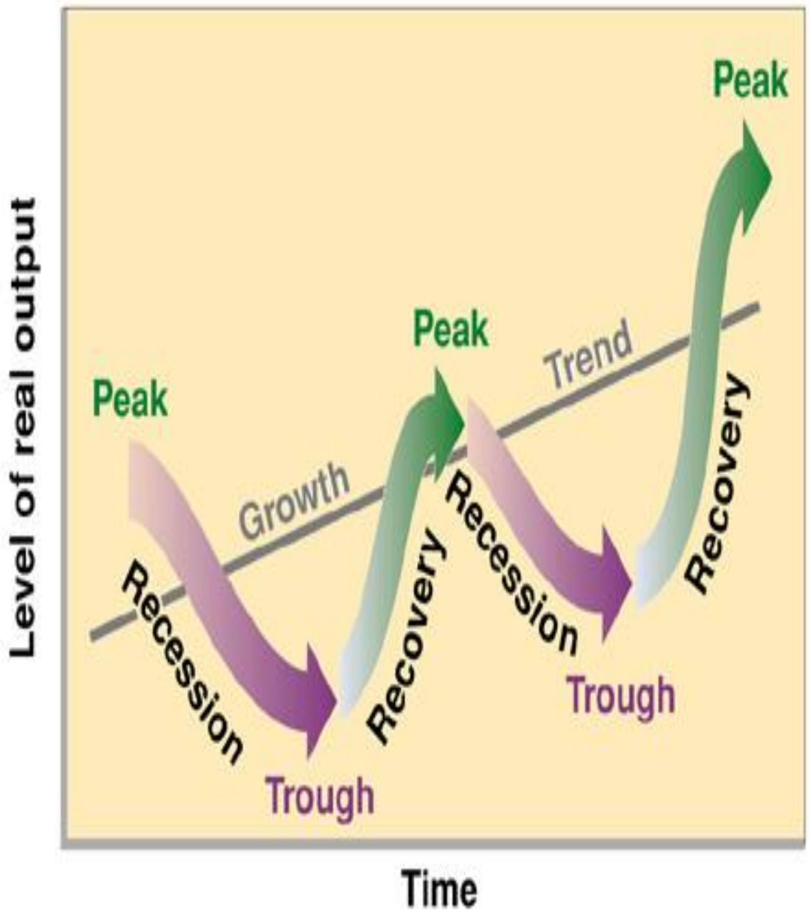
- Works just like regular supply and demand – except the suppliers are the workers (laborers) and the demanders are the employers (owners of firms)
- If demand for a product decreased, the owner of the company might fire some workers to reduce the amount being produced and thus decrease supply to meet equilibrium
- Companies will continue to hire or fire workers until the additional profit is less than the costs of the workers
- The supply and demand for a certain job helps determine that jobs wages – or earnings of labor
- By cutting labor costs, the owner can increase profits

Investing in your Business

- Capital Investments – help to increase productivity – new technology
- Production Possibility Curve – PPC – shows how much of a product can be produced using limited resources



The Business Cycle



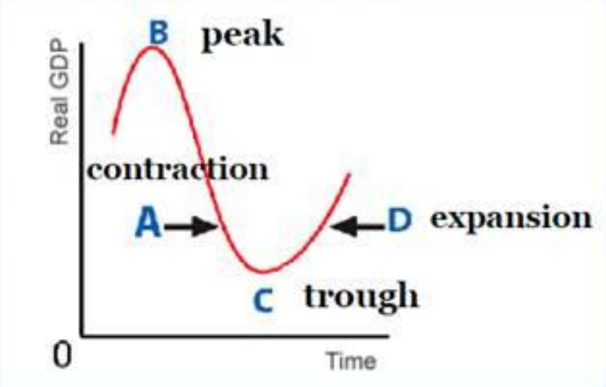
- Inflation – too much spending, prices rising
- Unemployment – people out of work who are still looking for work
- Contractions – shrinking economy, can lead to a recession
- Expansion – growing economy – leads to recovery
- Stagflation – high unemployment and high inflation

Government Regulation

- The government will sometimes step in to regulate businesses in an attempt to either monitor safety or to control the economy.
  - Wage and price controls
    - Minimum wage and natural monopolies
    - Can lead to shortages/surpluses
    - Subsidies
- Price ceiling: maximum price (freeze gas price)
- Price floor: minimum price (minimum wage)

Mod 4 – Quick Review – BEING SENT TO YOU RIGHT NOW!

The Business Cycle:



	Unemployment	Inflation
Peak	Low	High
Contraction	Increases	Decreases
Trough	High	Low
Expansion	Decreases	Increases

Fiscal Policy	Monetary Policy
Lead by Congress	Lead by the Federal Reserve
Tools: Taxing and Spending	Tools: Discount rate (DR), Reserve Requirement (RR), Buying and selling bonds in open market operations (OMO).
Contractionary Fiscal Policy: Lower spending or raise taxes	Contractionary Monetary Policy: Increase DR, Increase RR, Sell securities in OMO
Expansionary Fiscal Policy: Increase spending and lower taxes	Expansionary Monetary Policy: Decrease DR, Decrease RR, Buy securities in OMO

The Federal Reserve

- Controls Monetary Policy – or the regulation of the supply of money in circulation
  - Know the details of the Federal Reserve Bank and its operations
- Discount Rate—the interest rate the Federal Reserve charges banks to borrow currency.
- Reserve Requirement—the percentage of a bank's deposits that must be kept as currency and coin in the bank.
- Open Market Operations—the Federal Reserve's frequent buying and selling of government securities, considered the most significant of the three tools.
- Expansionary policy – includes lowering the discount rate, buying bonds, and lowering the reserve requirement
- Contractionary policy – raise discount rate, sell bonds, raise the reserve requirement

Fiscal Policy and Congress

- Fiscal Policy is the use of spending and taxing by Congress to regulate the economy
- Spending has a huge impact because of the volume of spending that the government does
  - Deficit – when spending exceeds taxing
  - Debt – the long term effect of deficit spending
- Expansionary – lower taxes, increase spending
- Contractionary - raise taxes, decrease spending

- You will need to know when/why expansionary or contractionary policy is used by Congress and The Fed.

Economists

- Smith – no government intervention
- Marx - total government intervention
- Keynes – somewhere in the middle

- You should know the details for each of them.

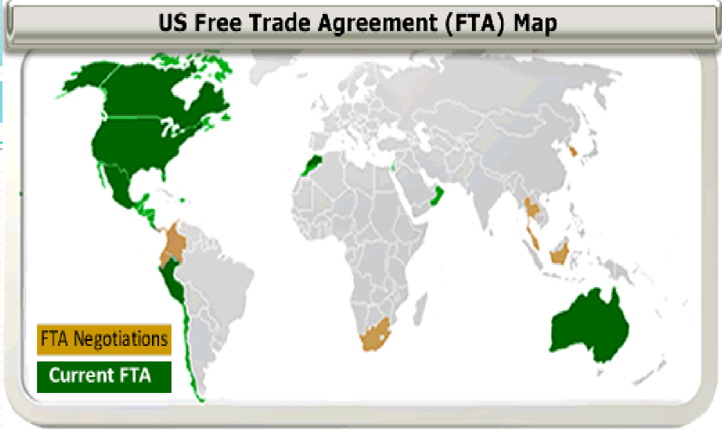
Economics Systems

- Market economy – market in control – no government regulation – supply and demand rules
- Command economy – government in control – total government regulation
- Traditional economy – community, culture, and tradition controls the economy
- Mixed economy – a mix of command and market

Economic goals and the GDP

- Freedom – low regulation
- Efficiency – use of resources
- Growth – rising GDP
- Security – low unemployment

Barriers to Trade



- Quota - A quota sets a maximum amount of a product for import. With less product available, quantity supplied decreases and price increases.
- Tariff - A tariff is a tax on imported goods. It is added onto the selling price when it enters the country and increases the price of import goods, thus decreasing the quantity demanded. In addition, it provides more tax revenue to the government.
- Regulation - A regulation is a safety and quality standard. It may result in the ban of specific ingredients proven to be hazardous. If a product includes these ingredients, it is not allowed to enter the country. A regulation also serves as a standard for environmental or ethical impact.
- Impact - Impact limits consumer access to goods that are considered to be of poor quality or do not meet social expectations.
- Embargo "Ban" - An embargo is the complete refusal to import a good or even all goods from a particular country. It can create a black market for those goods and hurts the political relationship with the country that has been banned. It could also potentially hurt the economy of one or both countries.
- FTA – Free Trade Agreement; Countries that trade freely with the U.S., beneficial because of the agreement which eliminates all barriers to trade and countries agree to work together economically.

Importance of Inflation

- Inflation is a general rise in prices over time.
- Inflation impacts everyone's economy. Inflation not only affects our personal cost of living, but also business profits, government revenue, exchange rates, and international trade.
- The Consumer Price Index (CPI) is a measure of inflation. The Consumer Price Index is a statistic comparing the cost of a "market basket" of goods and services American households normally purchase to the cost from a prior time. Calculating changes in the CPI produces the inflation rate. If the inflation rate is a negative number, that means overall prices are falling and we call this <u>deflation</u>. Though you might think this is a positive for the consumer, falling prices means businesses are losing profits and they may reduce worker pay. Rather than growing, the economy is shrinking.

Why Inflation Occurs

- Money supply is too high. Have you ever wondered why the government cannot just print more money to help people? Inflation is why. If the economy has too much cash circulating, it simply is not worth as much, and prices will rise.
- Demand exceeds supply. Remember the theory of supply and demand? When consumers want to purchase goods and services but there is not enough to go around, prices will rise. This relates closely to the problem of money supply.
- Cost of production rises. This is another reminder of the principles of supply. If the cost of offering a good or service increases, producers will pass the cost on to consumers. Think about the airline tickets.

Comparative and Absolute Advantage

- Absolute – one country can do something absolutely better than another
- Comparative – one country can do something comparatively better than another
  - It makes no sense to do everything for yourself, so allow others to produce some of the goods that you need and share amongst everyone so that everyone benefits.

Module 6

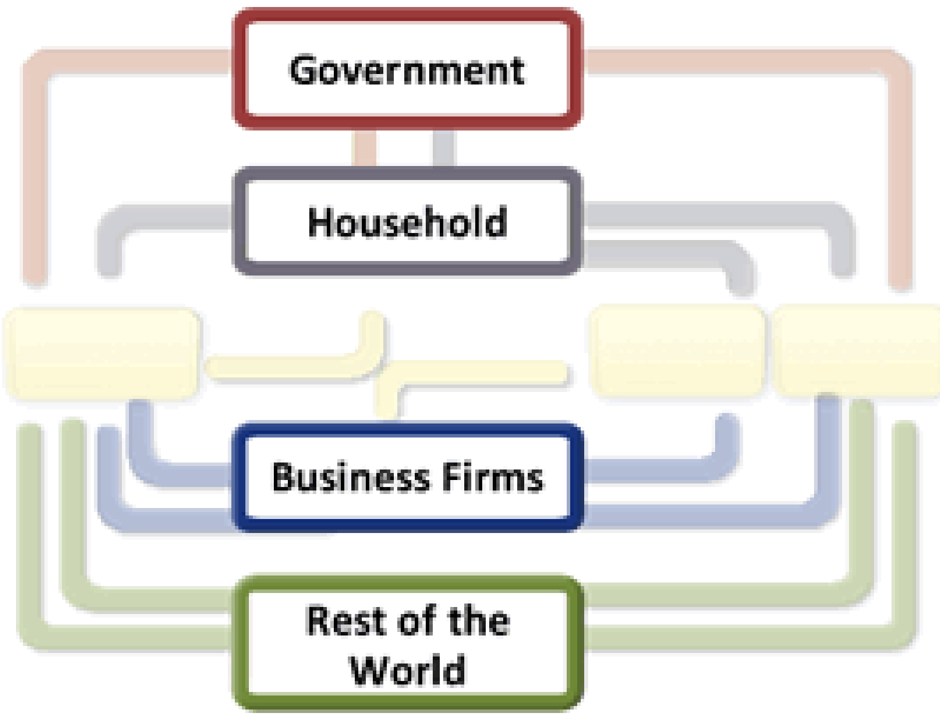
- Steps in a rational decision-making model: =
- Define the situation or problem
- Identify the important criteria to evaluate possible solutions
- Consider all possible solutions or alternatives
- Calculate the consequences of these solutions versus satisfying the criteria
- Choose the best option

The Circular Flow Model

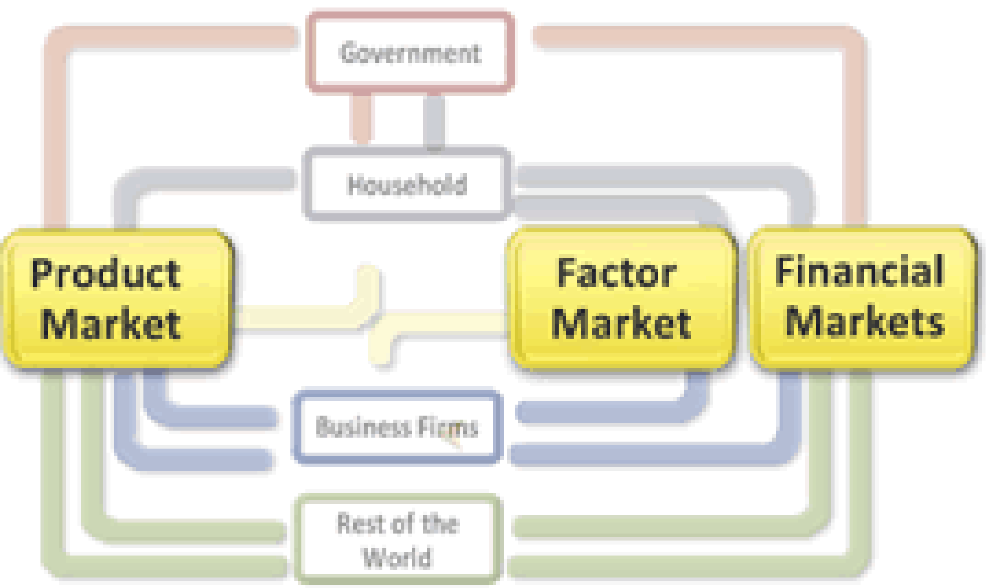
A circular-flow diagram shows the flow of resources between four main players in the economy—households, businesses, the government, and the rest of the world.

The Players

- The government represents any lawmaking body (local, state, or national) that collects taxes and provides services to individuals and businesses.
- Households include individuals like you and those living in the same home.
- Businesses include any company type that earns income from the sale of goods and services.
- The rest of the world represents interaction with all those three groups in foreign countries.



The Circular Flow Model



The Markets

- The four main players interact in three types of markets —factor, product, and financial.
- The product market is the buying and selling of finished goods and services, like your morning latte.
- The factor market is the exchange of the factors of production including components of land, labor, and capital, such as a coffee company purchasing equipment to process coffee beans.
- The financial market refers to the stock market and banking services, including the loans all the other economic players use to meet their goals.

Externalities

- Externalities: We call the effects of our choices on other people "externalities." You do not drive because you wish to pollute the air, but it happens and pollution affects our health and our planet. We can use a decision-making model to help us reduce such negative externalities. Remember to think hard about your choices!
- Externalities are costs and benefits to third parties; we also call them unintended consequences. Almost any choice we make creates externalities that can affect the economy at all levels.

Externalities

- Externalities can be caused by multiple factors, both positive and negative. Explanations include free resources, the commons, and free riders.
- Free resources - Free resources refer to productive ingredients that exist in quantities greater than people need or want for production. People often do not think of the potential impact on others when using free resources.
- Free Riders - An additional cause of externalities is the free-rider problem. The free-rider problem refers to how people can benefit from a good without necessarily paying for the costs of that good.
- The Commons - Another cause of externalities is the use of common goods. A common good is property that everyone owns equally, such as tax-supported land or structures like public parks, schools, or beaches. Everyone helps pay for common goods through taxes and has equal opportunity to use them.

Questions and Clarifications…
Call your teacher if you have questions on any of these concepts