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Introduction to Business

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Economic Activity in a Changing World

Chapter Objectives

After completing this chapter, you will be able to:

▶ Section 3.1 U.S. Economic History

- **Describe** the four types of economic shifts the United States has experienced.
- **Describe** what is shown by GDP, unemployment rate, rate of inflation, and national debt.

▶ Section 3.2 The Business Cycle

- **Explain** how individuals and the government influence the economy.
- **Describe** the four stages of the business cycle.

Ask

AN EXPERT

Understanding Financial Risk

Q: I am a drummer in a band. I can't decide if I should buy a new drum set now, or wait until next year when we go on the road. Should I buy now, or wait until next year and hope prices don't go up?

A: Financial risk is always a factor when making major purchasing decisions. You have identified one risk—inflation. Prices may go up, but they also may come down. If you need a loan to buy the drum set, changing interest rates represent another risk. You also have liquidity risk. If the band breaks up, how long will it take you to sell your drums so you can pay off your loan? Some risks can be evaluated mathematically, others cannot.

Mathematics You can calculate the effects of price and interest rate fluctuation on purchases. For example, if a drum set costs \$7,500, and the interest rate for one year is 7 percent, the total cost will be $(0.07 \times \$7,500) + \$7,500 = \$8,025$. Calculate the total cost with interest for each of the scenarios in the comparison chart and determine the least expensive option.

CONCEPT **Comparison Charts** A chart can help in comparing different scenarios of price and interest rates.

Price	Interest Rate
\$7,500	7%
\$7,450	8%
\$8,200	5%



Ilene MacDonald/Alamy

● **Ups and Downs** A market economy has its ups and downs. **How is the business cycle similar to a roller-coaster ride?**

U.S. Economic History

Reading Guide

Before You Read

Think of some factors that affect the health of the U.S. economy.

Read to Learn

- Describe the four types of economic shifts that the United States has experienced.
- Describe what is shown by GDP, the unemployment rate, rate of inflation, and national debt.

The Main Idea

Throughout the years, the U.S. economic system has changed. Each change affected what was produced and how people were employed. To gauge the health of our economic system, we use a variety of economic indicators.

Key Concepts

- The Changing U.S. Economy
- Measuring Economic Activity

Vocabulary

Key Terms

gross domestic product (GDP)
standard of living
inflation
deflation
budget deficit
national debt
budget surplus

Academic Vocabulary

You will find these words in your reading and on your tests. Make sure you know their meanings.

shifts
emphasis
sum
period

Graphic Organizer

Use a timeline like this one to indicate the changes in the U.S. economy from the 1700s to the 2000s. Mark the timeline to designate the following eras: Agricultural, Industrial, Production of Services, and Information Technology.



Go to connectED.mcgraw-hill.com to print out this graphic organizer.

The Changing U.S. Economy

Sometimes major **shifts** in certain growth areas can change the **emphasis** of the U.S. economy. The United States has experienced four major economic shifts.

During the early 1600s, the colonists bartered, or traded, goods and services. This created our service-based economy. In the 1700s, farming was a common way of life. This formed the agriculture-based economy. In the mid-1850s, the Industrial Revolution enabled the advent of big machines for producing goods. This started the industry-based economy. The 1900s saw the rapid movement of information, with the invention of the computer. This created the information-based economy. Computers have transformed the ways that goods and services are produced, delivered, and sold.

While we live in the information age, we also still rely upon aspects of the other types of economies. Agriculture, industry, services, and information all contribute to the health of the U.S. economy.

As You Read

What changes have you seen in the economy in your lifetime?

Business Case Study *Reader and Case Study*

Innovate for Good

Businesses think big to combine financial success with sustainability

Can businesses be responsible stewards of the planet while still remaining profitable and competitive?

Yes, says the World Economic Forum (WEF), which recently issued a report highlighting 16 companies that are doing exactly this. These “new sustainability champions” include companies from India, Brazil, Costa Rica, and other emerging markets. They represent industries including banking, fishing, solar energy, water technology—and even cement production, one of the largest contributors to global warming.

These companies combine superior financial performance with sustainable, innovative business practices. Shree Cement in India, for example, developed the world’s most energy-efficient process for making cement. Chinese air-conditioning manufacturer Broad Group invented a device

to measure air pollution that fits inside a cell phone.

These companies have three things in common. They use innovation to turn challenges into opportunities. They are guided by a vision for sustainability. And they work to change the world around them to improve the way business is done.

Active Learning

Brainstorm in small teams about businesses in your community that you have seen advertising themselves as “green” or “sustainable.” Call one or more of these businesses and ask about their philosophy of sustainability, as well as about specifics of their practices. Brainstorm ways the business could use innovation to be even more sustainable. Present your ideas to the class.



Unsung Heroes

Each nation's economy has had its unsung heroes and heroines. One hero of the Industrial Revolution might have been French-born Joseph Jacquard, who conceived the Jacquard loom, a system for the mass production of woven fabrics. *Who are the unsung heroes or heroines of our information age?*

As You Read

Economic indicators are figures that measure economic performance. What figures do you use to measure events or performances in your everyday life?

Measuring Economic Activity

Baseball fans know that batting averages, strikeouts, RBIs, and ERAs are figures used to measure a player's performance. Figures are also used to measure economic performance. These figures are called *economic indicators*. They measure things such as how much a country is producing, whether its economy is growing, and how it compares to other countries.

Gross Domestic Product

One way of telling how well an economy is performing is to measure how many goods and services it produces. The total value of the goods and services produced in a country in a given year is called its **gross domestic product (GDP)**. GDP is one of the most important indicators of the status of an economy. To calculate the GDP, economists compute the **sum** of goods and services sold to businesses, consumers, the government, and other countries. The United States has a very high GDP compared to other countries.

Standard of Living

Another important measure of a country's economic health is its standard of living. The **standard of living** is the level of material comfort as measured by the goods and services that are available. The more goods and services produced per person, the higher the standard of living.

The United States has a high standard of living largely because of its productive workforce. The standard of living refers to the amount of goods and services people can buy with the money they have. In the free-enterprise system, the wealth created by businesses benefits the entire community because businesses pay taxes and provide jobs.

? ETHICS in Business

Environmental Awareness

- **Critical Reading** Life is full of important decisions. Think about the kinds of decisions that you make as you read the question below. You are a purchasing agent for a large furniture manufacturer. You have received several bids from lumber companies for a supply of teak, a very dense and decay-resistant type of wood. The lowest bid comes from a lumber company that has been known for not placing a strong emphasis on local environmental concerns, especially resource depletion, when it cuts down trees.
- **Decision Making** How does the lumber company's reputation affect your decision? Explain your answer.



● A Changing Economy

Our economy has been affected by many developments. The development of information technology has transformed the ways goods and services are produced.

What other changes have affected the U.S. economy?

Unemployment Rate

The *unemployment rate* measures the number of people who are able and willing to work but cannot find work during a given **period**. Changes in the unemployment rate show whether an economy is picking up or slowing down.



Identify What does the unemployment rate measure?

Rate of Inflation

Another important measure of economic strength is the rate of inflation. **Inflation** is a general increase in the price of goods and services. With inflation, one's buying power decreases because it costs more to buy goods and services.

Inflation has many causes. It can occur after a war because scarce resources were transferred to the war effort. Inflation can be caused by increases in the costs of raw materials, expenses, and salaries. Inflation can also occur when the government allows too much money to circulate in the economy.

When the supply of goods is greater than demand, deflation can result. **Deflation** is a general decrease in the price of goods and services. When an economy produces more goods than people want, sellers have to lower prices and cut production. As a result, people have less money to buy goods, so the demand continues to go down.

mediaphotos/Getty Images



Worker Shortage

In recent years, Japan has found that it does not have enough workers. Corporations have had to react by retaining their skilled laborers. Toyota Motor Corporation is preparing for a shrinking workforce by offering one-year contracts to top employees who turn 60. Japan's largest untapped source is its women. *What steps do you think Japan might take to ease its current labor shortage?*

National Debt

Countries can run up large debts. The main source of income for a government is taxes. Governments use tax money to pay for programs such as defense, education, and Social Security. When the government spends more on programs than it collects in taxes, the difference in the amount is called a **budget deficit**. To pay for the difference, governments borrow money from the public, banks, and even other countries. The total amount of money a government owes is its **national debt**. If the debt gets too large, a nation can become dependent on other nations or unable to borrow more money. This is the case in many developing nations.

Sometimes, a government's revenue can exceed its expenditures. When a government's revenue exceeds its expenditures during a one-year period, it has a **budget surplus**. The United States experienced several years of budget surpluses in the late 1990s. The government often uses a surplus to cut taxes, reduce the national debt, or increase spending for certain programs.

Section 3.1

After You Read



Review Key Concepts

1. When did the service-based economy begin?
2. What do economic indicators measure?
3. What is the difference between a budget surplus and a budget deficit?

Academic Skills

4. **Mathematics** Suppose a recent study shows the U.S. Gross Domestic Product (GDP) is \$11.5 trillion. The study also shows that personal spending accounts for 70.4 percent of the total GDP. How much is personal spending in dollars?

CONCEPT Number and Operations: Percents

A percent is a ratio comparing a number to 100. It can also be represented as a fraction, with 100 as the denominator. To find a decimal equivalent, divide the percent by 100. Multiply that decimal by the total amount to determine the dollar amount that it represents.



For math help, go to the Math Appendix.



Go to connectED.mcgraw-hill.com to check your answers.

The Business Cycle

Reading Guide

Before You Read

Think about the ups and downs local businesses experience in a market economy.

Read to Learn

- Describe the four stages of the business cycle.
- Explain how individuals and government influence the economy.

The Main Idea

In a market economy, there is an economic cycle, which includes four stages: prosperity, recession, depression, and recovery. These are also the four stages of the business cycle. In the last few decades, we have experienced the economic cycle a number of times.

Key Concept

- Guiding the Economy
- Four Stages of the Business Cycle

Vocabulary

Key Terms

business cycle
prosperity
recession

depression
recovery

Academic Vocabulary

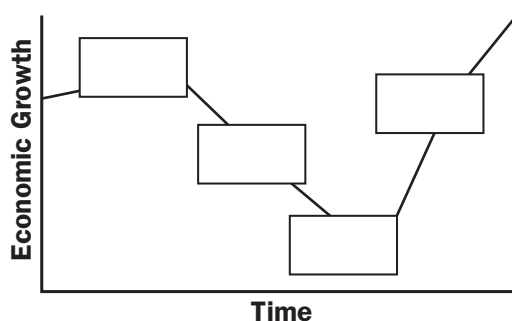
You will find these words in your reading and on your tests. Make sure you know their meanings.

enormous
policy

purchase
decline

Graphic Organizer

On a figure like the one below, label each of the four boxes with the appropriate stage of the business cycle.



Go to connectED.mcgraw-hill.com to print out this graphic organizer.

Guiding the Economy

The U.S. economy is shaped by a mix of public and private forces. Individuals have an **enormous** role on the market for goods and services. Congress and the President enact laws that impact fiscal **policy**. Whenever tax money is spent, it has an effect on the economy. These expenditures are often planned to guide the economy. The Federal Reserve, informally called “the Fed,” is a government agency that guides the economy by regulating the amount of money in circulation, controlling interest rates, and controlling the amount of money loaned. State and local governments may also take steps to influence their local economies.

As You Read

One country's economy can affect other countries. How does the economy of your community affect you and your family?

Four Stages of the Business Cycle

Economies go through ups and downs. This can happen for many reasons, including wars, foreign competition, changes in technology, and changes in consumer wants. Over long periods of time, these changes form patterns. For example, the U.S. economy went through slumps in the 1930s, the 1950s, the 1970s, and the early part of 2000. These slumps in economic activity with increased unemployment were followed by new waves of increased productivity and rises in GDP. The rise and fall of economic activity over time is called the **business cycle**. There are four stages of the business cycle—prosperity, recession, depression, and recovery. **Figure 3.1** illustrates the business cycle.

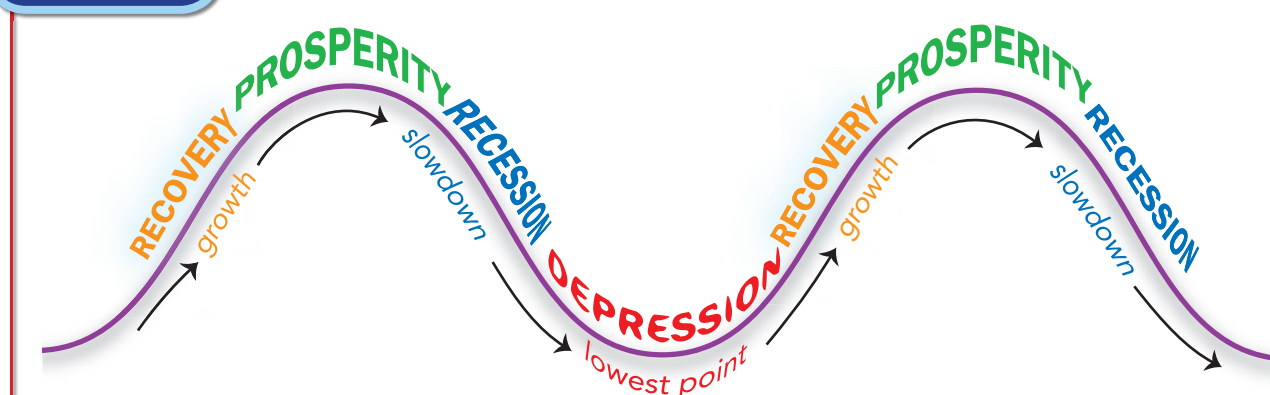
In a global economy, one country's economy can affect other trading partners. If a nation is in a period of economic expansion, it may **purchase** goods and services from other countries, promoting expansion in those countries.



Reading Check

Identify What are the four stages of the business cycle?

Figure 3.1 — **Business Cycle Model**



The Business Cycle The repeated rise and fall of economic activity over time is called a business cycle. **Does every business cycle have all four of these stages?**

Prosperity

When unemployment is low, production of goods and services is high, new businesses open, and there is prosperity. **Prosperity** is a peak of economic activity. This condition spreads throughout the economy. Wages are usually higher, so workers have more income. There is a greater demand for goods to be produced. More people can buy houses, which creates more work for builders. People also want to buy more goods from other countries, which benefits those countries as well.

Recession

During a **recession**, economic activity slows down. Businesses produce less, so they need fewer workers. As the unemployment rate increases, people have less money to spend. Without a steady source of income, unemployed workers consume fewer goods and services. The general drop in the total production of goods and services makes GDP decline.

In a recession there are downturns in many industries. A downturn in one industry can affect others. For example, a recession in the auto-making industry can lead to a recession in businesses that make parts for cars. When this happens, it is called the ripple effect. Because of the ripple effect, downturns in major industries can bring on a recession.

As You Read

When an economy enjoys prosperity, there is a greater demand for goods. What new technologies were developed in the last few decades as a result of good economic conditions?

Science/TechTRENDS

Jobs in Your Future

Job opportunities result from the relationships between the population, the labor force, and the demand for goods and services. Population changes influence the demand for goods and services. When the population changes, the size and makeup of the labor force change as well.

The Bureau of Labor Statistics recently released a report stating that nearly all the 30 fastest-growing occupations between now and 2022 are related to health care and construction. These occupations include home health aides, industrial psychologists, supervisors, and trade workers.

Web Quest

Locate Web sites where you can research population trends between now and 10 years from now. Make some predictions about how the demand for goods and services will change over the next 10 years.

● **Different Scenes for Different Stages of the Business Cycle** When workers go on strike, they usually want more wages or benefits. **At what stage of the business cycle would this type of event most likely occur?**



Depression


During a depression there is high unemployment and low production of goods and services. A **depression** is a deep recession that affects the entire economy and lasts for several years. It can be limited to one country but usually spreads to related countries. During a depression, many people are out of work, and fewer goods and services are produced. There is also a lot of unused manufacturing facilities. Fortunately, depressions are rare.

The stock market crash on October 29, 1929, or “Black Tuesday,” marked the beginning of the Great Depression. Between 1929 and 1933, GDP fell from approximately \$103 billion to \$55 billion—a **decline** of nearly 50 percent. At the same time, the number of people out of work rose nearly 800 percent—from 1.6 million to 12.8 million. During the worst years of the Depression, one out of every four workers was jobless. Even workers who had jobs suffered. The average manufacturing wage, which had reached 55 cents an hour by 1929, plunged to five cents an hour by 1933.

Many banks across the country failed. The FDIC did not exist at the time, so depositors were not protected. To prevent panic withdrawals, the federal government declared a “bank holiday” in March 1933. Every bank in the country closed for several days, and many never reopened. The money supply fell by one-third. Currency was in such short supply that towns, counties, chambers of commerce, and other civic bodies resorted to printing their own money.



Describe What happens to the economy during a depression?



“Depressionproof”
During the Great Depression, millions of people lost their homes and livelihoods. However, a large percentage of middle-class Americans were able to keep their jobs. These people were in professions considered “depressionproof.”
What professions do you think are more secure during a depression, and why?

Recovery

During a recovery, production starts to increase. A **recovery** is a rise in business activity after a recession or depression. People start going back to work and have money to purchase goods and services. The new demand for goods and services stimulates more production, and the GDP grows. Recovery leads back to prosperity as new businesses open and existing businesses increase productivity.

A recovery can take a long time or it can happen quickly. In 1939, the United States was only beginning to recover from the depression when World War II began. During the war, the United States recovered much faster because of the demand for war production.

During a recovery, some businesses innovate—meaning that they bring out new goods and services. These innovations can be different from what the businesses previously produced. They could also be different from what their competitors make. If the innovation is popular with consumers, sales increase dramatically, per unit costs decrease, and profitability increases. Businesses grow and economic activity soars.

Section 3.2

After You Read

Review Key Concepts

1. What is the stage that follows a recession or depression?
2. What is the difference between a recession and a depression?
3. Why may innovation play an important role in the recovery stage of the business cycle?

Academic Skills

4. **English Language Arts** The business cycle is often described using terms that describe how large bodies of water behave. Two of those terms are *ebb and flow* and *ripple effect*. Write a few sentences about each of these terms. Explain what they mean and why they are good metaphors for different aspects of the business cycle.
5. **English Language Arts** The words listed below are all synonyms, or closely related in meaning. They all can be used to describe negative movement in the business cycle. Notice that some of the words imply a more serious fall in the economy than others. Rewrite the list so that the words are, in your best judgment, ordered from least serious to most serious. Then write a few sentences explaining why you ordered the words as you did.

recession	slump	depression
decline	downturn	



Go to connectED.mcgraw-hill.com to check your answers.

Chapter 3 Review and Activities

Section 3.1 Summary

U.S. Economic History Throughout the years, our economic system has evolved and changed. In colonial times, the United States had begun its service-based economy. The 1700s saw the rise of the agriculture-based economy. The Industrial Revolution in the 1850s brought about the industrial economy, characterized by the large-scale manufacturing of goods. During the latter part of the 20th century, the information technology economy revolutionized the business world. To measure the health of our economic system, we use a variety of economic indicators, including GDP, unemployment rate, rate of inflation, and national debt.

Section 3.2 Summary

The Business Cycle In a global economy, one country's economy can affect the economy of its other trading partners. The Fed adjusts monetary policies to try to level out the ups and downs of the economy. An economic cycle includes four stages: prosperity, recession, depression, and recovery. Prosperity is the peak of economic activity. Recession is a slowdown in economic activity. Depression is a deep recession that affects the entire economy and lasts for several years. A recovery is a rise in business activity after a recession or depression. Fortunately, the United States has not had a depression since the 1930s.

Vocabulary Review

1. On a sheet of paper, use each of these key terms and academic vocabulary terms in a sentence.

Key Terms

gross domestic product (GDP)	budget surplus
standard of living	business cycle
inflation	prosperity
deflation	recession
budget deficit	depression
national debt	recovery

Academic Vocabulary

shifts	enormous
emphasis	policy
sum	purchase
period	decline

Review Key Concepts

2. Describe the four types of economic shifts the United States has experienced.
3. Describe what is shown by GDP, unemployment rate, rate of inflation, and national debt.
4. Explain how individuals and the government influences the economy.
5. Describe the four stages of the business cycle.

Critical Thinking

6. Would the cars made in this country by a foreign-owned company be included in GDP? Why or why not?
7. Which would be included in GDP: babysitting at home or working at a day-care center?
8. Why are people who are unemployed but not looking for work not included in the unemployment figures?
9. Why is inflation especially difficult for retired people?
10. Why might deflation be a bad thing?
11. Suppose you go to a store to buy a soda but notice the price is 20 cents higher than it was last week. Other prices are unchanged. Is this an example of inflation? Why or why not?
12. In which stage or stages of the business cycle would there be more personal bankruptcies? More business formations?
13. Explain why the standard of living is higher in the United States than in many other countries.

Write About It

14. Many economists believe that some unemployment is necessary because many of the unemployed are between jobs. Write an essay explaining why this might be true.
15. To pay for expenses, the federal government issues bonds. Many of these bonds are bought by foreign countries. Write a paragraph indicating whether you think this is good or bad for America.
16. Write a letter to your school counselor that explains how understanding the unemployment rate can be beneficial to you as you look for a job.
17. Assume the current inflation rate is 3 percent. Write an e-mail to your teacher explaining how that might help you decide where to put your savings.
18. Write a summary of the pros and cons of your starting a new business in the prosperous stage of the business cycle.
19. The unemployment rate in your community has increased considerably because of the closure of two firms. Write a letter to the editor of the newspaper explaining what steps you might take in your business as a result.

Technology Applications

Web Pages

20. You want to do business on the Internet. You know what kind of business you want to open. Use the Internet to research several businesses that might be considered your competition. Write a report that evaluates their Web sites. Print pages from each Web site and include them in your report.

Business Ethics

Dealing with Ethical Systems

21. You are the president of a biotechnology company that produces vaccines. A foreign government has asked to buy a vaccine to help stop a deadly infectious disease, but the negotiator expects a bribe. Should you look the other way so that you can get the vaccine to people who need it?

Chapter 3 Review and Activities

Applying Academics to Business

English Language Arts

22. Major novelists of the 1920s, a time of prosperity in the United States, and the 1930s, the time of the Great Depression, include John Steinbeck, William Faulkner, F. Scott Fitzgerald, Ernest Hemingway, and John Dos Passos. Find out more about their work and the work of other writers of the period. Make a bibliography of novels that portray everyday life during the 1920s and 1930s. Choose one to read and write a review of it to share with your classmates.

Mathematics

23. The Agriculture sector of the U.S. economy produces $\frac{1}{50}$ of the GDP while the Industry sector produces 18 percent. The rest is produced by the Service sector. What percent of GDP is contributed by the service sector?

CONCEPT Number and Operations:

Comparing Numbers After converting the two numbers $\frac{1}{50}$ and 18 percent so that they are either both percents or both fractions, they can be added together and then subtracted from the whole to find the part contributed by the service sector.

English Language Arts

24. The words Internet, interdependent, and international have the same prefix. Write a sentence in your own words telling what the prefix is and what it means. Give examples of other words that use the same prefix, and write sentences using them. Do the same for productivity and prosperity. Then check your work by looking in a dictionary or other resource.

Mathematics

25. Find unemployment statistics for the years 1933, 1944, 1955, 1966, 1977, 1988, 1999, and the most recent year for which statistics are available. Present the information in a bar graph. Write a few sentences discussing the reasons for the differences shown in the graph.

CONCEPT Data Analysis and Probability:

Bar Graphs Bar graphs are great for making multiple comparisons, showing frequencies, and displaying trends. They are sometimes confused with histograms, which are used to graphically show the distribution of a set of data. In this case, the bar graph will show how unemployment levels rose and fell with the cycles of the economy.

Active Learning

Track News Stories

26. During a two-week period, read the newspaper or watch the national news on television. Pick out three articles or report on three sequences of television news programming that relate to one of the topics discussed in this chapter, such as unemployment, inflation, deflation, and national debt. Write a report or give an oral presentation to the class on your findings.

Business in the Real World

Interview a Businessperson

27. Identify a businessperson in your community who has been in business for several years and experienced a number of business cycles. Interview the business owner to find out how his or her company performed during periods of recession and periods of prosperity. Then write a report summarizing the business owner's responses.

Real LIFE • skills

ASSESSING YOUR SKILLS

28. These skills are needed by all employees: creative thinking, decision making, and problem solving. Give an example of how you have implemented each skill in the last month. Then indicate which skills you believe you are fairly good at doing. Recommend how you can become better at doing the skill or skills in which you need work.

COOL Business CAREERS

FIND YOUR DREAM JOB

29. Locate the Occupational Outlook Handbook Web site. Click on the “OOH Search/A-Z Index” link and enter the job title “economist.” Then write a one-page report about this type of occupation. Conclude your report with a list of things you could do now to prepare yourself to pursue the occupation.

Role Play

ANALYZING ECONOMIC INDICATORS

30. **Situation** You are an intern for a federal bureau that collects and analyzes economic data. You have been asked to research recent economic indicators.

Activity Choose a sector of the economy to measure how well the economy is doing. Give a presentation to the bureau’s economists. Sectors include housing construction, gross domestic product, and retail and food services.

Evaluation You will be evaluated on how well you meet the following performance indicators:

- Research an economic sector.
- Interpret economic data.
- Answer questions about your findings.
- Present clear and relevant information.
- Project your voice, and use correct grammar and English.

Standardized Test Practice

Directions Read the paragraph and answer the question that follows. Write the letter for the answer on a separate piece of paper.

Some reasons for unemployment represent more of a problem for the economy than others. For example, recently graduated students and those who are voluntarily looking for a new job are only temporarily unemployed. Some workers are seasonal workers and only unemployed during part of the year. However, those workers who have lost their jobs because the economy has slowed down may be out of work until the economy recovers.

1. Which best describes the way the paragraph is organized?

- A sequence of events
- B comparison
- C statement and example
- D cause and effect



TEST-TAKING TIP When studying from a textbook, read the chapter summaries. They usually do a good job at summarizing important points.

