CHAPTER 1

Exploring the World of Business and Economics

INSTRUCTOR MANUAL RESOURCES

1.1 A WORD FROM THE AUTHORS

This chapter accomplishes three important tasks. First, it sets the stage for the remainder of the course and provides reasons why students should study business. Second, it provides an overview of the economy, competition, and different types of economic systems. Finally, it links events in American history to the present American business system. These concepts are essential to a basic understanding of the American economic system as a whole.

We begin Chapter 1 with a discussion of why students should study business and a definition of *business.* Then we explore the major types of economic systems. Next, we consider how a nation's economy and productivity are measured. An examination of the major types of competition follows. Finally, we discuss the historical development of business in the United States and the challenges that businesses can expect to encounter in the future.

1.2 TRANSITION GUIDE

New in Chapter 1: Exploring the World of Business and Economics

- A new Inside Business feature describes the history of Amazon and how it developed and marketed the Kindle.
- Current economic problems and how they affect both businesses and consumers are included in the introductory paragraph for this chapter.
- New URL information for the student Web site is provided in the first section of Chapter 1.
- A new Figure 1.1 shows how attaining more education can increase annual salary amounts for the average worker.
- The Jump-Starting Your Career feature has been deleted.
- A new Career Success feature describes how employees can use online networking to click their career into high gear.
- New information on the characteristics that employers look for when hiring employees is presented in the section "To Be a Successful Employee."
- A new section entitled "To Improve Your Management Skills" is included in the first part of Chapter 1.
- New examples of companies (Lehman Brothers, AIG, and mortgage lenders Freddie Mac and Fannie Mae) that fudged their sales and profit amounts are included in the "Business Profit" section.
- New material from the General Mills Social Responsibility Report is included in the section "Business Profit."
- A new Entrepreneurial Success feature describes how an entrepreneur built a successful small business by marketing hand-crafted items on the Web.
- The Entrepreneurial Challenge feature has been deleted.
- Current data for gross domestic product and real gross domestic product are included in the section "Important Economic Indicators That Measure a Nation's Economy."

- Figure 1.6 has been revised to reflect the current data for gross domestic product and real gross domestic product presented in the text.
- New information on the unemployment rate and how it affects the economy and consumers is included in the section “Important Economic Indicators That Measure a Nation’s Economy.”
- A new Spotlight feature shows historical and 2010 unemployment rates.
- New information about the amount of the national debt is provided in the section “The Business Cycle.”
- New updated price information for a bushel of wheat is supplied in the section “The Equilibrium, or Market, Price.”
- Figure 1.7 has been revised to reflect the current price of wheat presented in the chapter content.
- The definition of monopoly has been revised.
- Figure 1.8 has been revised to include the green movement, economic crisis, iPod, and netbooks.
- The material in the section “Business Development in the 1900s” has been revised and shortened.
- More information about the service economy is included in the section “A New Century: 2000 and Beyond.”
- The Business of Green feature has been deleted.
- A new Sustaining the Planet feature “How the Sun and Earth Help Frito-Lay” is included in the section “The Current Business Environment.”
- A revised list of questions that businesses must answer in the future is included in the section “The Challenges Ahead.”
- A new Return to Inside Business feature about Amazon is provided at the end of the chapter.
- A new Video Case 1.1 is entitled “Entertainment Means Profits for Nederlander Concerts.”
- A new Case 1.2 describes how Caterpillar operates in a very competitive industry.

1.3 QUICK REFERENCE GUIDE

Instructor Resource	Location
Transition Guide	IM, p. 2
Learning Objectives	Textbook, p. 2; IM, p. 5; PowerPoint Slide 1-2
Brief Chapter Outline	IM, pp. 5–6
Guide for Using PowerPoint Slides	IM, p. 7 Reproduced in Print IM
General Chapter Teaching Tips	IM, p. 8
Comprehensive Lecture Outline	IM, pp. 9–36
At Issue: Capitalism—Yes or No?	IM, p. 23
Career Success *Clicking Your Career into High Gear*	Textbook, p. 6
Entrepreneurial Success *Rob Kalin's Etsy Success*	Textbook, p. 13 Questions and Suggested Answers, IM, p. 15
Sustaining the Planet *How the Sun and Earth Help Frito-Lay*	Textbook, p. 28
Inside Business: How Amazon Kindles Business Success	Textbook, p. 3
Return to Inside Business	Textbook, p. 30 Questions and Suggested Answers, IM, p. 42
Marginal Key Terms List	Textbook, p. 32
Review Questions	Textbook, p. 32 Questions and Suggested Answers, IM, pp. 42–45
Discussion Questions	Textbook, p. 32 Questions and Suggested Answers, IM, pp. 46–47
Video Case 1.1 (Entertainment Means Profits for Nederlander Concerts) and **Questions**	Textbook, p. 33 Questions and Suggested Answers, IM, pp. 47–48
Case 1.2 (Caterpillar Helps the World Build) and **Questions**	Textbook, pp. 33–34 Questions and Suggested Answers, IM, p. 48
Building Skills for Career Success	Textbook, pp. 34–35 Suggested Answers, IM, pp. 49–51
IM Quiz I & Quiz II	IM, pp. 52–54 Answers, IM, p. 55
Class Exercise: Giving examples of competitive situations	Suggested Answers, IM, p. 55
Additional Class Exercises	IM, p. 56
Debate Issue: Should there be less government involvement in the United States economic system?	Premium PowerPoint Slide 1-25
Chapter Quiz (in PowerPoints)	Premium PowerPoint Slides 1-54 to 1-56 Answers, IM, p. 55; Premium Slides 1-57 to 1-59

1.4 LEARNING OBJECTIVES

After studying this chapter, students should be able to:

1. Discuss what you must do to be successful in the world of business.
2. Define *business* and identify potential risks and rewards.
3. Define *economics* and describe the two types of economic systems: capitalism and command economy.
4. Identify the ways to measure economic performance.
5. Outline the four types of competition.
6. Summarize the factors that affect the business environment and the challenges that American businesses will encounter in the future.

1.5 BRIEF CHAPTER OUTLINE

I. Your Future in the Changing World of Business
- A. Why Study Business?
  1. For Help in Choosing a Career
  2. To Be a Successful Employee
  3. To Improve Your Management Skills
  4. To Start Your Own Business
  5. To Become a Better Informed Consumer and Investor
- B. Special Note to Students

II. Business: A Definition
- A. The Organized Effort of Individuals
- B. Satisfying Needs
- C. Business Profit

III. Types of Economic Systems
- A. Capitalism
- B. Capitalism in the United States
  1. Households
  2. Businesses
  3. Governments
- C. Command Economies
  1. Socialism
  2. Communism

IV. Measuring Economic Performance
- A. The Importance of Productivity in the Global Marketplace
- B. Important Economic Indicators That Measure a Nation’s Economy
- C. The Business Cycle

V. Types of Competition

A. Perfect Competition
   1. The Basics of Supply and Demand
   2. The Equilibrium, or Market, Price

B. Monopolistic Competition

C. Oligopoly

D. Monopoly

VI. American Business Today

A. Early Business Development

B. Business Development in the 1900s

C. A New Century: 2000 and Beyond

D. The Current Business Environment

E. The Challenges Ahead

1.6 GUIDE FOR USING POWERPOINT SLIDES

Basic PPT Slide Number(s)	**Premium PPT Slide Number(s)**	**Title/Description**
1	1	Chapter Opener
2	2	Learning Objectives
3–4	3–4	Chapter Outline begins
5	5	*Figure 1.1* Who Makes the Most Money
6	6	Chapter Outline continues
7	7	Tips for Studying Business
8	8	Definition of Business
9	9	*Figure 1.2* Combining Resources
10–12	10–12	Chapter Outline continues
13	13	*Figure 1.3* The Relationship Between Sales Revenue and Profit
14	14	Chapter Outline continues
	15*	Paths to E-Profits
15–18	16–19	Chapter Outline continues
19	20	*Figure 1.4* Basic Assumptions for Adam Smith's Laissez-Faire Capitalism
20	21	Chapter Outline continues
21	22	*Figure 1.5* The Circular Flow in Our Mixed Economy
22–23	23–24	Chapter Outline continues
	25*	Debate Issue: Should there be less government involvement in the United States economic system?
24	26	Chapter Outline continues
	27*	Consumer Price Index
25–26	28–29	Chapter Outline continues
27	30	*Figure 1.6* GDP in Current and in Inflation-Adjusted Dollars
28–33	31–36	Chapter Outline continues
34	37	*Figure 1.7* Supply Curve and Demand Curve
35–37	38–40	Chapter Outline continues
38–39	41–42	*Figure 1.8* Time Line of American Business
40–41	43–44	Chapter Outline continues
	45*	U.S. Manufacturing Employment
	46*	A Few of the Fastest Growing Occupations
42–48	47–53	Chapter Outline concludes
	54–56*	Chapter Quiz
	57–59*	Answers to Chapter Quiz

**Indicates Premium Slide (provides coverage that supplements text content)*

1.7 GENERAL CHAPTER TEACHING TIPS

- This chapter contains three class activities that can be completed in 10–15 minutes. They are designed to be used with groups, but they can also be done with partners or individually. The first one, the Fun Quiz, is useful as an icebreaker on the first day of class. Two other exercises deal with resources and supply and demand issues. They focus on a potential student business, "GarageWorks!" Instructor notes/answers are provided for each exercise. The appropriate place to use these exercises is noted in the Comprehensive Lecture Outline. A fourth activity is a crossword puzzle, which could be used to review the chapter in teams.
- There are specific examples, discussion starters, and teaching tips interspersed throughout the Comprehensive Lecture Outline to help you relate the theoretical material to student interests.
- Note the names of your school and several local organizations as examples of different kinds of organizations that exist in your town. These examples will help make the material immediately relevant and realistic for your students.
- Although the text definition of *business* includes the notion of making a profit, point out to students that not-for-profit organizations exist (discussed in Chapter 4) and are run just as carefully as for-profit businesses. Note the similarities and differences among the kinds of resources used by profit-seeking and not-for-profit organizations. For example, both an airline and a university may buy food in bulk, but they have different revenue sources to pay for that food.
- The questions raised in the section "The Challenges Ahead" can be categorized into several themes that include the globalization of business, ethical issues, continual change, and the importance of technology. Point out for students the different boxed features that appear throughout the text and pick up on these themes: Going for Success, Career Success, Entrepreneurial Success, Ethical Challenges and Successful Solutions, and Sustaining the Planet.
- If your school or a neighboring one offers the MBA degree or has an executive MBA program, students might be interested in a summary of program requirements.
- Note that most top MBA programs will not accept students directly out of an undergraduate program. Instead, they require that the student get an undergraduate degree and then work at least two years in a meaningful job before entering graduate school.
- Mention the names of large companies headquartered in your area or firms that hire large numbers of graduates from your school.

1.8 COMPREHENSIVE LECTURE OUTLINE

Inside Business: How Amazon Kindles Business Success

At the time of publication, perhaps the biggest threats to the nation's economy were the problems associated with the depressed housing, banking, and financial industries. With record home foreclosures, troubled banks on the verge of failure, and stock values dropping, Congress passed the Economic Stabilization Act, a $700-billion bailout plan created to stabilize the nation's economy and restore confidence in the banking and financial industries. While politicians, economists, business leaders, and the general public still debate the merits of a federal rescue plan, one factor became very apparent. Something had to be done to correct what some experts described as the nation's worst economic problems since the Great Depression.

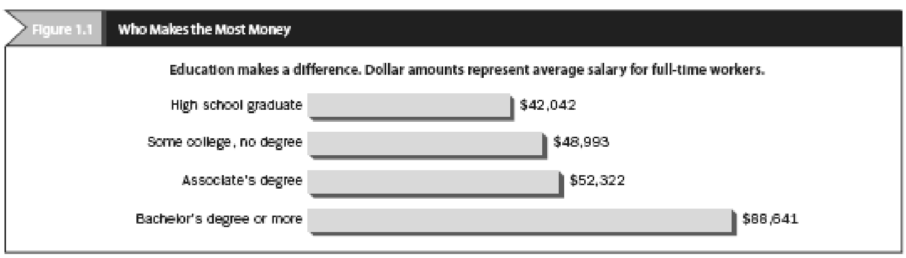
Despite these problems, our economic system will survive. In fact, our economy continues to adapt and change to meet the challenges of an ever-changing world. Our economic system provides an amazing amount of freedom that allows businesses that range in size from the small corner grocer to Apple to adapt to changing business environments. Within certain limits, imposed mainly to ensure public safety, the owners of a business can produce any legal good or service they choose and attempt to sell it at a price they set. This system of business, in which individuals decide what to produce, how to produce it, and at what price to sell it, is called *free enterprise.*

ICEBREAKER ACTIVITY

Fun Quiz: *This 10-minute icebreaker quiz can be completed in a group or individually. See the "Classroom Exercises" section at the end of this chapter for details and a handout.*

I. YOUR FUTURE IN THE CHANGING WORLD OF BUSINESS. To experience success, you must adapt to change in order to take advantage of the opportunities that are out there. To do so, you must bring something to the table that makes you different from the next person. Ask yourself: What can I do that will make employers want to pay me a salary? What skills do I have that employers need?

Figure 1.1



Source: The 2010 Statistical Abstract of the U. S. Web site at http://www.census.gov (accessed March 26, 2010). Salary amounts were obtained from Table 687.

A. **Why Study Business?** Once you have an education and knowledge, no one can take it away. To begin with, there are economic benefits. (See Figure 1.1.) Further, there are at least five reasons why you should study business.

1. **For Help in Choosing a Career.** This business course will introduce you to a wide array of employment opportunities. One thing to remember as you think about what your ideal career might be is that a person's choice of a career is ultimately a reflection of what he or she values and holds most important.

***Teaching Tip:** Ask students what careers they think might be the most in demand in the next 10 years. Link to the Bureau of Labor Statistics Occupational Outlook Handbook website for detailed information (http://www.bls.gov/oco/home.htm). Some of the fastest growing careers are in health and veterinary care, biomedical engineering, network systems, and data communication fields.*

2. **To Be a Successful Employee.** To get a job in your chosen field and to be successful at it, you will have to develop a plan, or road map, that ensures you have the skills and knowledge the job requires. This course, your instructor, and all the resources available at your college or university can help you acquire the skills and knowledge you will need for a successful career.
3. **To Improve Your Management Skills.** To be an effective manager, you must be able to perform four basic management functions: planning, organizing, leading and motivating, and controlling. To successfully perform these management functions, managers must possess three very important skills: interpersonal skills, technical skills, and conceptual skills.
4. **To Start Your Own Business.** Some people prefer to work for themselves, and they open their own businesses.
   a) To be successful, business owners must possess many of the same skills that successful employees have.

***Discussion Starter:** Ask students what the chief motivation is for starting a business—money or independence? Independence wins. Which is more important—creativity or self-discipline? Discipline wins.*

b) It also helps if your small business can provide a product or service that customers want.

c) Unfortunately, approximately 70 percent of small businesses fail within the first seven years. Typical reasons for business failures include undercapitalization, poor business location, poor customer service, unqualified or untrained employees, fraud, lack of a proper business plan, and failure to seek outside professional help.

5. **To Become a Better Informed Consumer and Investor.** By studying business, you will become a more fully informed consumer, which means that you will be able to make more intelligent buying decisions and spend your money more wisely. This same basic understanding of business will also make you a better informed investor.

Teaching Tip: *Ask students if they are more likely to use price to determine quality if they have no knowledge or understanding of a product. Point out that low-priced private label brands are more likely to be purchased by people with more education than by those with less.*

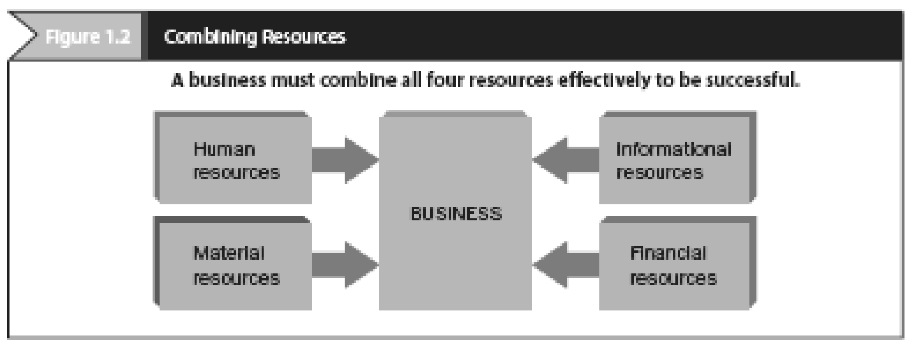
B. **Special Note to Students.** This business course doesn't have to be difficult. All the features in each chapter have been evaluated and recommended by instructors with years of teaching experience. In addition, business students have critiqued each chapter. A number of student supplements to the text will help you explore the world of business, as well as the website that accompanies this edition.

II. BUSINESS: A DEFINITION. *Business* is the organized effort of individuals to produce and sell, for a profit, the goods and services that satisfy society's needs. To be successful, a business must be organized, satisfy needs, and earn a profit.

Discussion Starter: *Ask students to state the three components of the definition of business: (1) it must be organized, (2) it must serve a need, and (3) it must earn a profit. You will probably need to help with the answers. Once you have the three components, ask them to give examples of outstanding companies in each area. For example, consumer products companies such as Procter & Gamble certainly seem to be well organized, serve a need, and make good profits. IBM is another example. Looking at profit relative to the need served can get good discussion flowing early.*

A. **The Organized Effort of Individuals.** For a business to be organized, it must combine four kinds of resources: material, human, financial, and informational. (See Figure 1.2.)

Figure 1.2



1. Material resources include the raw materials used in manufacturing processes, as well as buildings and machinery.
2. Human resources are the people who furnish their labor to the business in return for wages.

3. The financial resource is the money required to pay employees, purchase materials, and generally keep the business operating.
4. Information is the resource that tells the managers of the business how effectively the other resources are being combined and used.
5. Businesses are usually classified as one of three types.
   a) Manufacturing businesses process various materials into tangible goods.
   b) Service businesses produce services.
   c) Marketing intermediaries buy products from manufacturers and then resell them.

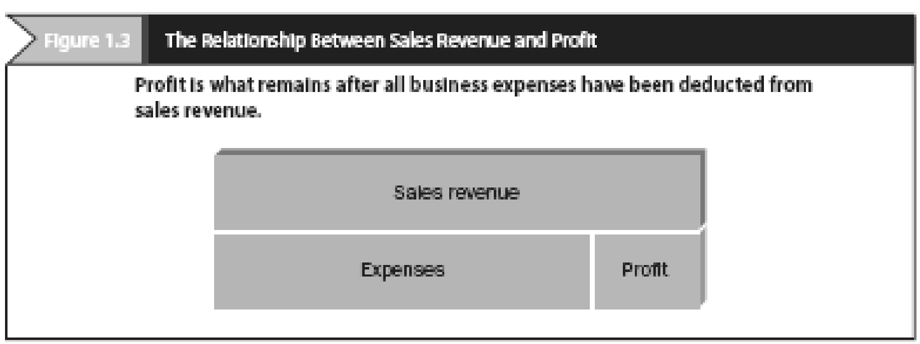
CLASS ACTIVITY

Resource Exercise: *This is a good place to use the 10- to 15-minute group exercise entitled "What Do I Need?" See the "Classroom Exercises" section at the end of this chapter for details and a handout.*

B. **Satisfying Needs.** The ultimate objective of every firm is to satisfy the needs of its customers. When the business understands its customers' needs and works to satisfy those needs, it is usually successful.

C. **Business Profit.** *Profit* is what remains after all business ex-

Figure 1.3



Using the Boxed Inserts

Entrepreneurial Success:

Rob Kalin's Etsy Success

Suggested Question 1. What basic business principle did Rob Kalin employ to make Etsy a success?

The ultimate objective of every firm is to satisfy the needs of its customers. When a business understands its customers' needs and satisfies those needs, it is usually successful. Rob Kalin discovered that there weren't satisfactory online outlets to market his handmade furniture. As he was creating his own Web site, he expanded his sights to include other handmade items such as jewelry, art, vintage items, and craft supplies. Clearly, there was a need for a Web site where artisans, customers, and vendors of handmade merchandise could connect with each other to buy and sell their products. Etsy provided an online marketplace and quickly grew to a $200-million business.

Suggested Question 2. What resources did Rob Kalin use to organize his business?

Rob Kalin utilized four resources in organizing his business: material, human, financial, and informational. Material resources included hardware and software to build the Etsy Web site as well as the merchandise which was bought and sold over the Internet. Human resources consisted of friends and classmates who helped him initially in handling technical operations and Etsy's employees which currently number 70. Beyond his own funds, financial resources consisted of a $50,000 investment from one of his furniture customers and investments from the cofounders of the photo-sharing site, Flickr. Informational resources were both internal with his employees and external among suppliers, vendors, and customers primarily online.

Negative profit, which results when a firm's expenses are greater than its sales revenue, is called a loss. The term *stakeholders* is used to describe all the different people or groups who are affected by the policies, decisions, and activities made by an organization. While stockholders and business owners generally believe that profit is the most important goal for a business, many stakeholders may be just as concerned about a firm's social responsibility record.

The profit earned by a business becomes the property of its owners. Profit is the reward business owners receive for producing goods and services that consumers want and for assuming the risks of ownership. One of these is the risk of not being paid (employees, suppliers, and lenders must be paid before the owners). Another is the risk of losing whatever was invested in the business.

Teaching Tip: *Apple has been monumentally successful with its iPhone product. Ask students what need the iPhone meets? What makes it different from other cellular phones? What other recent products can they name that meet an existing need well?*

III. TYPES OF ECONOMIC SYSTEMS. *Economics* is the study of how wealth is created and distributed.

1. By "wealth" we mean anything of value. "How wealth is distributed" simply means "who gets what." The way in which people deal with these two issues determines the kind of economic system, or *economy,* that a nation has.
2. Economics is usually studied from two perspectives:
    a) *Microeconomics*—The study of the decisions made by individuals and businesses.
    b) *Macroeconomics*—The study of the national economy and the global economy.
3. *Factors of production* are the resources used to provide goods and services. There are four such factors.

a) Land and natural resources—Elements in their natural state that can be used in production, such as crude oil, forests, minerals, land, water, and even air.

***Teaching Tip:** Ask students what resources in addition to oil and gas are in limited supply. Obviously, limitations create problems—but what opportunities might they also represent?*

b) Labor—Human resources such as managers and employees.

c) Capital—Money, facilities, equipment, and machines used in the operation of organizations.

d) Entrepreneurship—The willingness to take risks and the knowledge and ability to use the other factors of production efficiently. An *entrepreneur* is a person who risks his or her time, effort, and money to start and operate a business.

***Extra Example:** We often think of China in terms of inexpensive labor. Yet, China is slowly losing work to countries like Bangladesh, Vietnam, and Cambodia as Chinese labor unrest has led to big pay raises for many factory workers. This is particularly true for workers who produce cheaper, labor-intensive goods like casual clothes, toys, and simple electronics that do not require literate or skilled workers .While the $117 to $147 per month minimum wage earned by garment workers in China's coastal industrial provinces sounds low compared to most Western nations, workers in the same industry in Bangladesh earn about $64 a month.*

***Source:** Vikas Bajaj, "Bangladesh, with Low Pay, Moves in on China,"* NYtimes.com*, July 16, 2010, http://www.nytimes.com/2010/07/17/business/global/17textile.html?src=busln, accessed July 17, 2010.*

4. A nation's economic system significantly affects all the economic activities of its citizens and organizations. A country's economic system provides answers to four basic economic questions.
   a) What goods and services—and how much of each—will be produced?
   b) How will these goods and services be produced?
   c) For whom will these goods and services be produced?
   d) Who owns and controls the major factors of production?

Teaching Tip: *Ask the students to regard the classroom as an economic unit. The goods produced are papers, discussions, and exam results. How are these goods produced? For whom? And most importantly, who has ownership?*

A. **Capitalism.** *Capitalism* is an economic system in which individuals own and operate the majority of businesses that provide goods and services. Adam Smith in his book, *Wealth of Nations,* published in 1776, argued that a society's interests are best served when the individuals within that society are allowed to pursue their own self-interest.
   1. Adam Smith created the concept he called the *invisible hand*, which describes how a business owner's personal gain benefits others (through the product that is produced or through the wages that are paid to workers) and a nation's economy (through increased GDP, taxes, exports, etc.).

2. Adam Smith's capitalism is based on four fundamental issues. (See Figure 1.4.)

Figure 1.4

   a) First, the creation of wealth is properly the concern of private individuals, not of government.
   b) Second, private individuals must own the resources used to create wealth, and the owners of resources should be free to determine how these resources are used.
   c) Third, Smith contended that economic freedom ensures the existence of competitive markets that allow both sellers and buyers to enter and exit as they choose. The freedom to enter or leave a market at will has given rise to the term *market economy* (sometimes referred to as a free-market economy)—an economic system in which businesses and individuals make the decisions about what to produce and what to buy; the market determines how much is sold and at what prices.
   d) Finally, in Smith's view, the role of government should be limited to providing defense against foreign enemies, ensuring internal order, and furnishing public works and education.

With regard to the economy, government should act only as rule maker and umpire.

Teaching Tip: *Ask students to debate whether federal, state, and local governments are properly involved in regulating business.*

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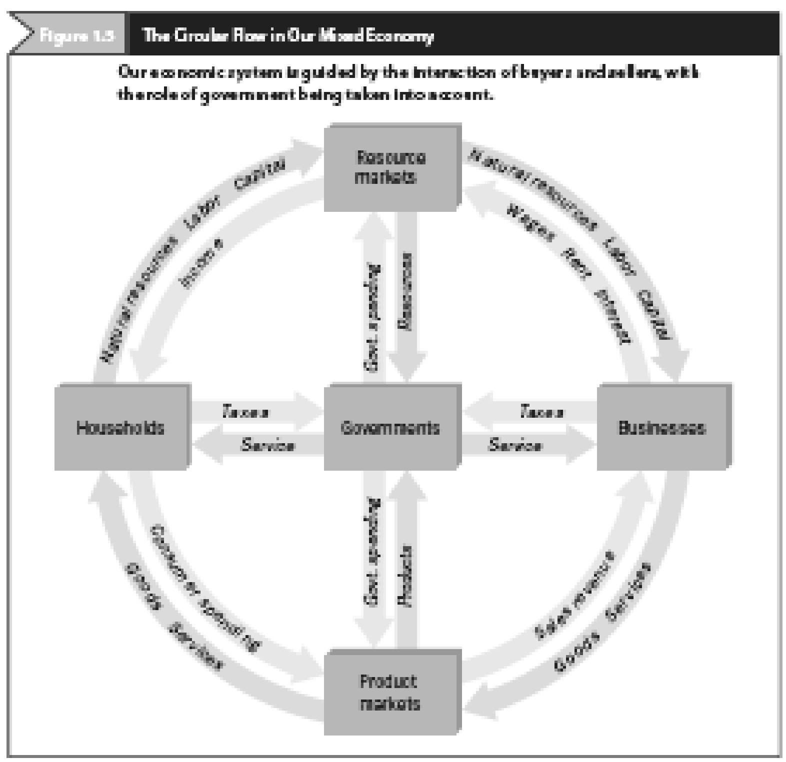
3. Smith believed that each person should be allowed to work toward his or her own economic gain, without government interference. The French term "laissez faire" describes Smith's system; loosely translated it means "let them do" (as they see fit).

B. **Capitalism in the United States.** The U.S. economy is a *mixed economy* because it exhibits elements of both capitalism and socialism. In today's economy, the four basic economic questions are answered by three groups. (See Figure 1.5.)

Figure 1.5



1. **Households.** Households are consumers of goods and services, as

well as owners of some of the factors of production. Approximately 70 percent of U.S. production consists of products for personal consumption.

WHAT PEOPLE ARE SAYING

Private enterprise is an economy open to new ideas, new products, new jobs, new men.

—William Benton

a) As "resource owners," the members of households provide businesses with labor, capital, and other resources.

b) As "consumers," household members use their income to purchase the goods and services produced by business. Approximately 70 percent of our nation's total production consists of *consumer products:* goods and services purchased by individuals for personal consumption.

2. **Businesses.** Like households, businesses are engaged in two different exchanges. They exchange money for natural resources, labor, and capital, and they use these resources to produce goods and services. Then they exchange their goods and services for sales revenue.

3. **Governments.** Government provides a variety of services that are considered important but either (a) would not be produced by private business firms or (b) would be produced only for those who could afford them (e.g., national defense, police/fire protection, education, and construction of roads and highways).

C. **Command Economies.** A *command economy* is an economic system in which the government decides what will be produced, how it will be produced, for whom available goods and services will be produced, and who owns and controls the major factors of production. Two types of economic systems serve as examples of command economies.

1. **Socialism.** In a socialist economy, the key industries are owned and controlled by the government. Depending on the country, private ownership of smaller businesses is permitted to varying degrees. What to produce and how to produce it are determined in accordance with national goals.
2. **Communism.** In a communist economy, almost all economic resources are owned by the government. The basic economic questions are answered through centralized state planning, which also sets prices and wages. Emphasis is placed on the production of goods the government needs rather than on the products that consumers might want. Karl Marx was the father of communism.

Extra Example: *On July 15, 2010, Congress approved a sweeping expansion of federal financial regulation in response to the 2008 financial crisis that let to the worst recession since the Great Depression. For much of the previous century, encouraged by the nation's economic growth, the government had allowed financial companies to become larger, less transparent, and more profitable. Unfettered markets had been seen as the key to prosperity. This legislation was controversial, reflecting the tension between free markets and governmental supervision.*

Source: *"Financial Oversight Bill Signals Shift on Deregulation,"* NYTimes.com*, July 16, 2010, http://dealbook.blogs.nytimes.com/2010/07/16/financial-oversight-bill-signals-shift-on-deregulation/, accessed July 17, 2010.*

At Issue

The American economy is primarily a free-market economy. It is based on several building blocks, including the private ownership of property and the free interchange of the forces of supply and demand. Is the capitalistic system of producing goods and services the best economic system?

For Capitalism	Against Capitalism
1. The capitalist economic system has survived the test of time (more than 225 years) and for most of that time has produced the highest standard of living in the world.	1. The capitalist economy has produced the greatest volume of consistent waste of any economy in human history.
2. People decide what products to buy when they "vote" in the marketplace with their dollars. These individuals are the best judges of what to make, how much to make, and how it should be distributed.	2. People acting as independent and separate decision makers do not allow any opportunity for a more centralized planning system of utilization of scarce and necessary resources.
3. Capitalism offers the freedom to select careers, products, services, etc., not available in other economies.	3. Capitalism as originally defined by Adam Smith in 1776 does not exist given the presence of so many huge corporations and an increasing amount of government intervention.

Discussion Starter: *Ask students to compare their experiences with the U.S. Postal Service (USPS) with FedEx and UPS. At first glance, the latter two may seem more efficient—but then remind them that the USPS processes 584 million pieces of mail on an average day at a relatively low cost.*

Source: *http://www.usps.com/communications/newsroom/postalfacts.htm, accessed July 17, 2010.*

IV. MEASURING ECONOMIC PERFORMANCE

A. **The Importance of Productivity in the Global Marketplace.** One way to measure a nation's economic performance is to assess its productivity. *Productivity* is the average level of output per worker per hour. An increase in productivity results in economic growth.

Discussion Starter: *Arguably the world's most watched sporting event is the World Cup of Soccer that occurs every four years. One study suggests the German economy, Europe's largest, loses more than $8 billion in productivity, about 0.27 percent of gross domestic product, during the month-long tournament. Surveys in Britain predict output losses there of $1.5 billion to $2.3 billion. Even in the United States, the World Cup is the fourth-biggest "productivity sapper," based on a nonscientific ranking of top sporting events carried out by Challenger, Gray & Christmas, a workplace consultancy based in Chicago. The NCAA men's basketball tournament ranked No. 1 and was followed by NFL fantasy football pools and the Super Bowl.*

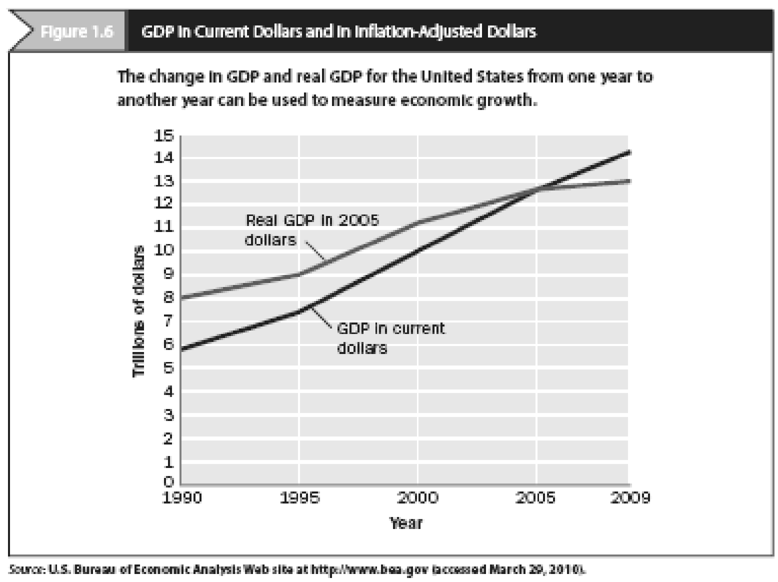
Source: *David Rising, "World Cup Causes Net Loss in Productivity,"* The Spokes-Man Review*, July 11, 2010, http://www.spokesman.com/stories/2010/jul/11/world-cup-causes-net-loss-in-productivity/, accessed July 17, 2010.*

Ask the students how much they think March Madness costs the United States in lost productivity. Answer: Estimates for 2010 ran as high as $1.8 billion.

B. **Important Economic Indicators That Measure a Nation's Economy.** A nation's *gross domestic product (GDP)* is the total dollar value of all goods and services produced by all people within the boundaries of a country during a one-year period.

1. This GDP figure facilitates comparisons between the United States and other countries because it is the standard used in international guidelines for economic accounting.
2. To make accurate comparisons of GDP figures for two different years, we must adjust the figures for inflation or deflation. *Inflation* is a general rise in the level of prices. *Deflation* is a general decrease in the level of prices. "Real" gross domestic product is the total dollar value, using inflation-adjusted figures, of all goods and services produced by a nation. (See Figure 1.6.)
3. There are other economic measures that can be used to evaluate a nation's economy such as the *unemployment rate*. (See Table 1.2 in the text.)

Figure 1.6



WHAT PEOPLE ARE SAYING

Communism: Nobody's got nothing, but everybody's working.

—Fred Allen

C. **The Business Cycle.** A nation's economy fluctuates rather than grows at a steady pace every year. These fluctuations are generally referred to as the *business cycle;* that is, the recurrence of periods of growth and recession in a nation's economic activity. Generally, the business cycle consists of four states: the peak (sometimes referred to as prosperity), recession, the trough, and recovery.

1. During the peak period, the economy is at its highest point, unemployment is low, total income is relatively high, and consumers are willing to buy products and services. Businesses often expand and offer new products and services.
2. Generally, economists define a *recession* as two or more consecutive three-month periods of decline in a country's gross domestic product. Unemployment rises during a recession, and total buying power declines. Economists define a *depression* as a severe recession that lasts longer than a recession.
3. The third phase of the business cycle, the "trough" of a recession or depression, is the phase in which the nation's output and unemployment bottom out and reach their lowest levels. To offset the effects of recession and depression, the federal government uses both monetary and fiscal policies.
    a) *Monetary policies* are the Federal Reserve's decisions that determine the size of the supply of money in the nation and the level of interest rates.
    b) The government can also use *fiscal policy* to influence the amount of savings and expenditures by altering the tax structure and changing the levels of government spending. Although the federal government collects over $3 trillion in an-

nual revenues, the government often spends more than it receives, resulting in the *federal deficit.*

c) The total of all federal deficits is called the *national debt.*

4. The last economic state is recovery. Recovery is the movement of the economy from depression or recession to prosperity; a greater demand for products and services results.

V. TYPES OF COMPETITION. Business *competition* is essentially a rivalry among businesses for sales to potential customers. Economists recognize four different degrees of competition, ranging from ideal, complete competition to no competition at all. These are perfect competition, monopolistic competition, oligopoly, and monopoly. (See Table 1.3 in the text.)

CLASS ACTIVITY

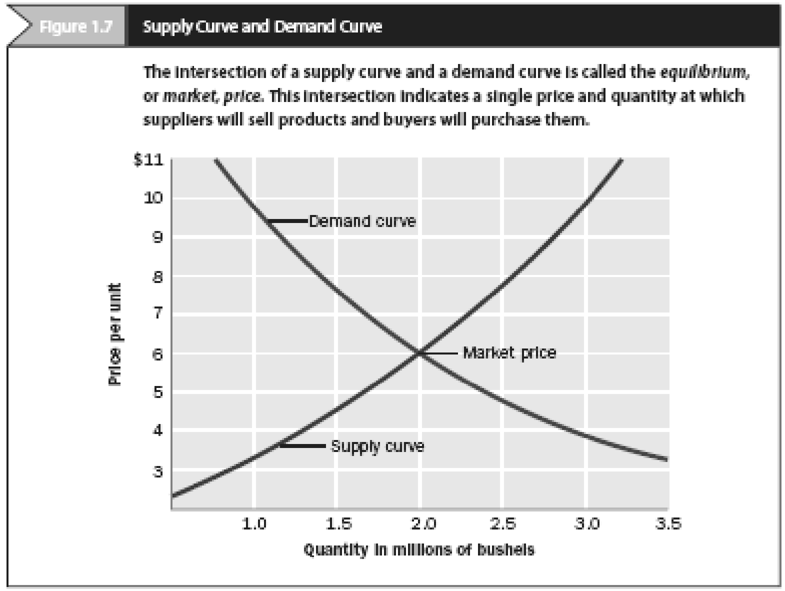
GarageWorks! Exercise: *This is a 10-minute group activity that will build on the earlier resource exercise to illustrate supply and demand. See the "Classroom Exercises" section at the end of this chapter for details.*

A. **Perfect Competition.** *Perfect competition* is a market situation in which there are many buyers and sellers of a product, and no single buyer or seller is powerful enough to affect the price of that product. In perfect competition, buyers and sellers must accept the going price.

1. **The Basics of Supply and Demand.** The *supply* of a particular product is the quantity of the product that producers are willing to sell at each of various prices. The *demand* for a particular product

is the quantity that buyers are willing to purchase at each of various prices. (See Figure 1.7.)

Figure 1.7



2. **The Equilibrium, or Market, Price.**

   Under pure competition, the *market price* of any product is the price at which the quantity demanded is exactly equal to the quantity supplied. Market prices are affected by anything that affects supply and demand.

B. **Monopolistic Competition.** *Monopolistic competition* is a market situation in which there are many buyers along with a relatively large number of sellers. The various products available in this market are similar and intended to satisfy the same need. However, each seller attempts to make its products different. *Product differentiation* is the process of developing and promoting differences between one's products and all similar products.

C. **Oligopoly.** An *oligopoly* is a market situation (or industry) in which there are few sellers. These sellers are quite large and must make sizable investments to enter into their markets. Because there are few sellers, the market actions of each can have a strong effect on competitors' sales and prices.

D. **Monopoly.** A *monopoly* is a market (or industry) with only one seller. A firm in a monopoly position must consider the demand for its product and set the price at the most profitable level. A *natural monopoly* is an industry that requires a huge investment in capital and within which any duplication of facilities would be wasteful. Many public utilities are still classified as natural monopolies, but competition is increasing in many industries.

1. In addition to natural monopolies, another type of legal monopoly —sometimes referred to as "limited monopoly"—is created when the federal government issues a copyright, patent, or trademark.
2. Except for natural and limited monopolies, federal antitrust laws prohibit both monopolies and attempts to form monopolies.

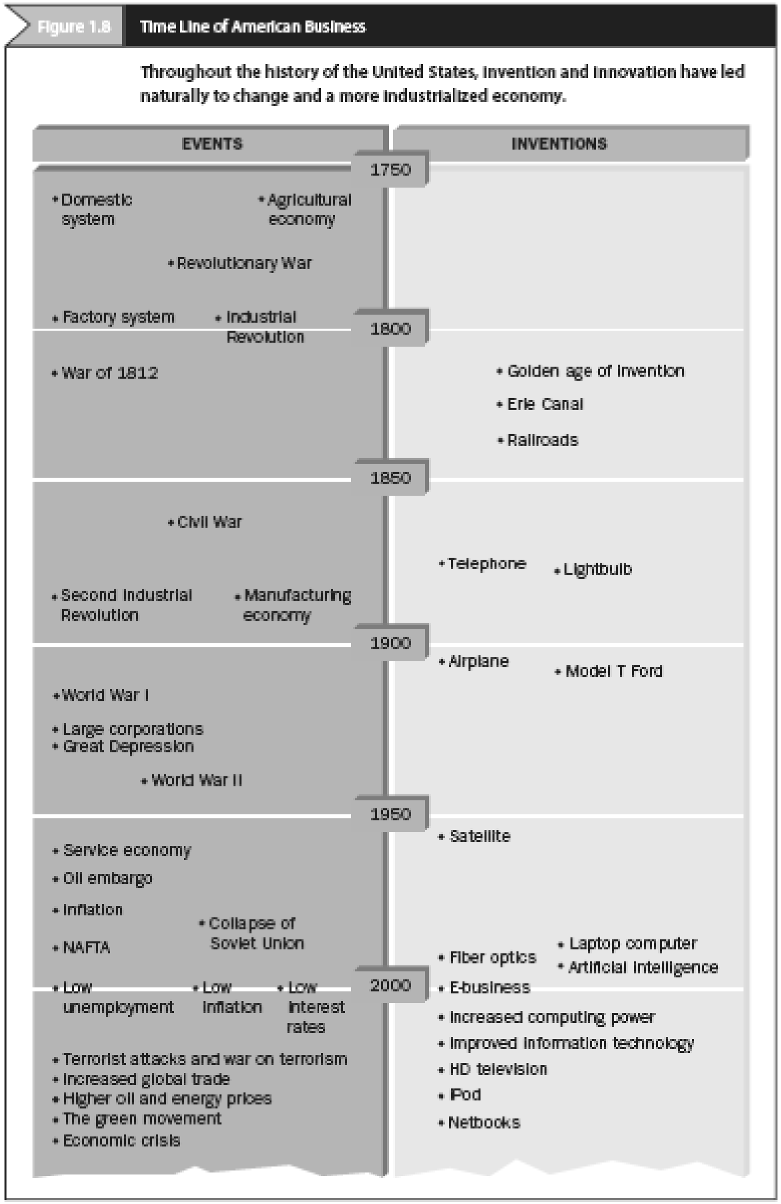
Teaching Tip: *Ask students to debate whether monopolies are always bad or if they should be permitted on occasions. For example, most European and Asian companies are larger than many American companies, and many are government owned or subsidized. For example, many national airlines such as Air France and Boeing's European competitor Airbus receive government subsidies. You could make an argument that we need very large companies to effectively compete in the global marketplace.*

VI. AMERICAN BUSINESS TODAY. Refer to Figure 1.8 for an overall view of our nation's history, the development of our business system, and some major inventions that influenced the nation and our business system.

A. **Early Business Development.** Almost all families lived on farms, and the entire family worked at the business of surviving.

1. The early colonists used *barter*—a system of exchange in which goods or services are traded directly for other goods and/or services without using money.

Figure 1.8



2. The *domestic system* was a method of manufacturing in which an entrepreneur distributed raw materials to various homes, where families would process them into finished goods.
3. In 1790, Samuel Slater, an Englishman, set up a textile factory in Rhode Island to spin raw cotton into thread. Slater's ingenuity resulted in America's first use of the *factory system* of manufacturing, in which all the materials, machinery, and workers required to manufacture a product are assembled in one place.
4. A manufacturing technique called *specialization* was used to improve productivity. Specialization is the separation of a manufacturing process into distinct tasks and the assignment of different tasks to different workers.
5. The years from 1820 to 1900 were the golden age of invention and innovation in machinery.
6. At the same time, new means of transportation greatly expanded the domestic markets for American products.

B. **Business Development in the 1900s**

1. Industrial growth and prosperity continued well into the twentieth century. Henry Ford's moving automotive assembly line refined the concept of specialization and helped spur on the mass production of consumer goods.
2. Fundamental changes occurred in business ownership and management. No longer were the largest businesses owned by one individual; instead, ownership was in the hands of thousands of corporate shareholders.

3. The Roaring Twenties ended with the sudden crash of the stock market in 1929 and the near collapse of the economy. The Great Depression that followed in the 1930s was a time of misery and human suffering.
4. After Franklin D. Roosevelt became president in 1933, the federal government got deeply involved in business for the first time by implementing programs to get the economy moving again.
5. The economy was on the road to recovery when World War II broke out in Europe in 1939. The 1940s, 1950s, and 1960s witnessed both increasing production and a rising standard of living. *Standard of living* is a loose, subjective measure of how well off an individual or a society is, mainly in terms of need satisfaction through goods and services.
6. Major events that shaped the nation's economy occurred during the period of 1940 to 2000:
   - World War II, the Korean War, and the Vietnam War.
   - Rapid economic growth and higher standard of living during the 1950s and 1960s.
   - The social responsibility movement during the 1960s.
   - A shortage of crude oil and higher prices for most goods in the mid-1970s.
   - High inflation, high interest rates, and reduced business profits during the early 1980s.
   - Sustained economic growth in the 1990s.

C. **A New Century: 2000 and Beyond.** According to economic experts, the time period from 2000 to 2010 might be characterized as the best of times and the worst of times rolled into one package.

1. On the plus side, technology became available at an affordable price. *e-Business* became an accepted method of conducting business. The growth of service businesses and increasing opportunities for global trade has changed the way American firms do business. A service economy is an economy in which more effort is devoted to the production of services than to the production of goods.
2. On the negative side, there is still a certain amount of pessimism surrounding the economy.

D. **The Current Business Environment.** Business is the organized effort of individuals to produce and sell, for a profit, the goods and services that satisfy society's needs. Business is affected by the following environments:

1. *The Competitive Environment.* Successful firms compete with competitors by satisfying customer needs.
2. *The Global Environment.* There are winners and losers from globalization. Consumers win because they have more product choices and lower prices. On the negative side, many people have and will lose their jobs because of lower offshore wages or due to technological innovation.

3. *The Technological Environment.* Changes in manufacturing equipment, communication with customers, and distribution of products are examples of how technology has changed business practices.

Discussion Starter: *Technology is changing how businesses hire as well. For example, a June 2010 study by* Jobvite *revealed that 73.3 percent of surveyed companies turn to social networking sites to recruit and hire new employees. Nearly 60 percent of companies surveyed for the study also reported having successfully hired a new employee found through social networking websites like LinkedIn and Facebook. In light of these facts, consider your current social networking sites—are you putting your best foot forward? Or are there things you may not want future employers to know about you?*

4. *The Economic Environment.* Managers and business owners do not have unlimited resources to pay for all the business activities they want to fund. This is especially important if the nation's economy drops precipitously or an individual firm's sales and profits are declining.

E. **The Challenges Ahead.** When our business system works well, it provides jobs for those who are willing to work, a standard of living that few countries can match, and many opportunities for personal advancement. But our system is far from perfect. It also gave us the Great Depression of the 1930s and the economic problems of the 1970s, the late 1980s, and the economic crisis that began in the fall of 2007.

The challenges to the U.S. economic system over the next decade are many. Some of the issues to be resolved include the following:

1. How can we create a more stable economy and create new jobs for the unemployed?
2. How can we regulate banks, savings and loan associations, credit unions, and other financial institutions to prevent the type of abuses that led to a banking crisis?
3. How do we reduce the national debt and still maintain a healthy economy and stimulate business growth?
4. How can we make American workers more productive and American firms more competitive in the global marketplace?
5. How can we preserve the benefits of competition and small business in our American economic system?
6. How can we encourage economic growth and at the same time continue to conserve natural resources and sustain our environment?
7. How can we meet the needs of two-income families, single parents, older Americans, and the less fortunate who need health care and social programs to exist?
8. How can we meet the challenges of managing culturally diverse workforces to address the needs of a culturally diverse marketplace?
9. How can we defeat terrorism and resolve conflict with Iran, North Korea, and other countries throughout the world?

The answers to these questions are anything but simple. Yet they directly affect our own future, our children's future, and the future of our nation.

Within the American economic and political system, the answers are ours to provide.

WHAT PEOPLE ARE SAYING

A sound economy is a sound understanding brought into action. It is calculation realized; it is the doctrine of proportion reduced to practice; it is foreseeing contingencies and providing against them; it is expecting contingencies and being prepared for them.

—Hannah More

1.9 POWERPOINT SLIDES

1.10 TEXTBOOK ANSWER KEYS

1.10a Return to Inside Business

Amazon

1. **Of the environments that affect the business world, which have had the most significant effect on Amazon?**

   The technological environment has been very important to Amazon's success. As the text indicates, founder Jeff Bezos relied on cutting-edge technology to establish a business that would satisfy customers' needs for wide selection, good service, and low prices. Students may also say that the competitive environment has played a role in Amazon's success by spurring the company on to new innovations and new products, such as the Kindle.

2. **During a recent year, Amazon's earnings topped $900 million. Why do you think this online retailer is profitable? What actions must management take to continue to earn record profits?**

   Students may offer a number of explanations for Amazon's profitability. For example, some may say that Amazon keeps costs low by using technology to deliver good service, provide personalized recommendations, and expand into new types of merchandise without the expense of building and maintaining physical stores. To continue to earn record profits, Amazon will need to maintain its entrepreneurial spirit, keep its competitive edge, improve productivity, and anticipate and meet customers' needs. Students may suggest other actions as well.

1.10b Review Questions

1. **What reasons would you give if you were advising someone to study business?**

   There are five compelling reasons for studying business described in this chapter.

   a. To help you choose a career

   a. To help you be a successful employee

   b. To help you improve your management skills

   c. To help you start your own business

   d. To help you become a better informed consumer and investor

2. **What factors affect a person's choice of careers?**

   Deciding what kind of career you want to devote your life to can be both daunting and puzzling, especially when you don't know what all the possibilities are. Choices range from small, local businesses owned by one individual to large corporations with offices and facilities in countries around the globe. There are also employment opportunities with federal, state, county, and local governments and with not-for-profit organizations. One thing to remember when choosing a career is that a person's choice of a career is ultimately a reflection of what he or she values and holds most important. What you choose to do with your life will be based on what *you* feel is most important.

3. Describe the four resources that must be combined to organize and operate a business. How do they differ from the economist's factors of production?

The four resources are (1) material resources, which include raw materials used in the manufacturing process as well as buildings and machinery; (2) human resources, who are the people that furnish their labor to the business in return for wages; (3) financial resources, which is money used to pay employees, purchase materials, and keep the business operating; and (4) information, which tells the managers of the business how effectively the other resources are being combined and used. Economists refer to the factors of production as the resources used to produce goods and services. They are land and natural resources, labor, capital, and entrepreneurship.

4. Describe the relationship among profit, business risk, and the satisfaction of customers' needs.

The business that is able to successfully satisfy customers' needs is said to be the business that will realize the greatest profit potential. Profit is also the payment that business owners receive for assuming the risks of ownership. These risks include not being paid and losing whatever they have invested into the business.

5. What are the four basic economic questions? How are they answered in a capitalist economy?

The four basic economic questions are (1) what goods and services and how much of each to produce, (2) how to produce, (3) for whom to produce, and (4) who owns and controls the factors of production. In a capitalist economy, the first question is answered by consumers as they spend their money. The second question is answered by producers as they compete for sales and profits. The third question is answered by those who have the money to buy the product. The fourth question is answered by who provides the land and natural resources, labor, capital, and/or entrepreneurship. The distribution of goods and services, therefore, depends on the current prices of economic resources, goods, and services and who can afford to buy them.

6. Explain the invisible hand of capitalism.

The "invisible hand" was a term created by Adam Smith to describe how an individual's personal gain benefits other citizens and a nation's economy. For example, a small business owner who sells shoes not only prospers from selling his shoes but also provides a benefit to the workers he pays to produce his shoes. Ultimately, the small-business owner contributes to the nation's economy by providing employment, paying taxes, and providing exports, etc.

7. Describe the four basic assumptions required for a laissez-faire capitalist economy.

1. The creation of wealth is the concern of private individuals, not of government.
2. Private individuals must own the resources used to create wealth and should be free to determine how these resources are used.
3. The existence of competitive markets gives sellers and buyers the right to make decisions about what to produce and what to buy, and the market determines how much is sold and at what prices.

4. Government's role should be limited to providing defense against foreign enemies, ensuring internal order, and furnishing public works and education.

8. Why is the American economy called a mixed economy?

Our economy is a mixed economy because it exhibits elements of both capitalism and socialism.

9. Based on Figure 1.5, outline the economic interactions between business and households in our business system.

See Figure 1.5. In the circular flow that characterizes our business system:

a. Households are the resource owners and provide businesses with natural resources, labor, and capital. Households are also consumers who use their income to purchase the goods and services produced by businesses. Today's households purchase approximately two-thirds of our nation's total production.

b. Businesses purchase households' natural resources, labor, and capital and use these resources to produce goods and services that are exchanged for sales revenue. This revenue is exchanged once again for households' resources.

10. How does capitalism differ from socialism and communism?

Capitalism is a market economy (sometimes referred to as a free-market economy). The basic economic questions are answered by private business owners who control the factors of production. Socialism and communism, on the other hand, are controlled by government planning and government ownership. Decisions are made by government planners and, in many cases, the wants and needs of the government are more important than those of consumers.

11. How is productivity related to the unemployment rate?

As productivity increases, fewer workers are needed to produce a given level of goods and services. If demand doesn't increase, management may decide to reduce their workforce in order to generate more profit. This situation will result in higher unemployment. In this case, increased productivity is good for employers but not good for unemployed workers seeking jobs in a very competitive work environment

12. Define gross domestic product. Why is this economic measure significant?

Gross domestic product (GDP) is the total dollar value of all goods and services produced by all people within the boundaries of a country during a one-year period.

GDP as an economic measure is important because it is a measure of a nation's economic output. It facilitates comparisons between the United States and other countries, since it is the standard used in international guidelines for economic accounting. GDP allows observers to determine, over several time periods, the extent of economic growth.

13. How is the producer price index related to the consumer price index?

The producer price index (PPI) measures prices of goods at the wholesale level. The consumer price index (CPI) measures the prices consumers typically pay for a specific good. Since changes in the PPI reflect price increases or decreases at the wholesale level, the PPI is an accurate predictor of both changes in the CPI or prices that consumers will ultimately pay when they purchase goods and services.

14. What are the four steps in a typical business cycle? How are monetary and fiscal policies related to the business cycle?

The four steps in a typical business cycle are the peak (sometimes called prosperity), recession, the trough, and recovery (sometimes called expansion). The federal government uses both monetary and fiscal policies to offset the effects of recession and depression. The government uses monetary policies to determine the size of the supply of money in the nation and the level of interest rates. Through fiscal policies, the government can influence the amount of savings and expenditures by altering the tax structure and changing the level of government spending.

15. Choose three of the economic measures described in Table 1.2 and describe why these indicators are important when measuring a nation's economy.

While student answers will vary depending on the term they choose, you may want to review the material in Table 1.2. Each of the following seven terms are defined: balance of trade, bank credit, corporate profits, inflation rate, national income, new housing starts, and prime interest rate.

16. Identify and compare the four forms of competition.

The four forms of competition are pure competition, monopolistic competition, oligopoly, and monopoly.

Under pure competition, there are many buyers and sellers of a product, and no single buyer or seller is powerful enough to affect the price of that product. Under monopolistic competition, there are many buyers and a relatively large number of sellers who differentiate their products from the products of competitors. An oligopoly is a market situation in which there are few sellers, so the market actions of each seller have a strong effect on competitors' sales. A monopoly is a market with only one supplier of the product.

17. Explain how the equilibrium, or market, price of a product is determined.

Under pure competition, the market price of any product is the price at which the quantity demanded is exactly equal to the quantity supplied.

18. Four different environments that affect business were described in this chapter. Choose one of the environments and explain how it affects a small electronics manufacturer located in Oregon. Why?

The four different environments are (1) the competitive environment, (2) the global environment, (3) the technological environment, and (4) the economic environment. A small electronics manufacturer in Oregon would most likely find itself in a highly *competitive environment* where there are many buyers along with a relatively large number of sellers. To successfully compete in this environment, a small electronics manufacturer might differentiate its product from the competition by providing unique product features, an attention-getting brand name, unique packaging, services such as free delivery, or a lifetime warranty.

1.10c Discussion Questions

1. **In what ways have the economic problems caused by the recent crisis in the banking and financial industries affected business firms? In what ways have these problems affected employees and individuals?**

   The recent crisis in the banking and financial industries has had a significant negative impact on business firms not only in the United States but worldwide. Financial giants such as Lehman Brothers and Bears Stearns have either gone out of business or been taken over by competitors. AIG, the largest insurance company in the world, received a $45-billion-dollar bailout from the U.S. government so that the company could meet its financial obligations. Washington Mutual, the largest bank in Washington, D.C., has failed. The stock market in the United States fell nearly 38 percent in six months. This has resulted in a lack of confidence in the U.S. economy, a significant reduction in consumer spending, and a severe tightening of credit from banks. Businesses of all sizes have seen their investments lose value, are finding it difficult to borrow money to meet their short-term business needs, and are experiencing lower demand for their goods and services. The effect on individuals has been equally difficult. Workers are losing their jobs and are unable to find new ones. Individuals in every economic class have seen their savings decline in value and in some cases evaporate. Retirees are being forced to reenter the workforce because their savings have been depleted. Few if any Americans have not been affected by this economic downturn.

2. **What factors caused American business to develop into a mixed economic system rather than some other type of economic system?**

   The shrinking size of the globe, the intervention of foreign competition, the Great Depression, World Wars I and II, and the ever-increasing age of our population (among other factors) have contributed to our mixed economic system.

3. **Does an individual consumer really have a voice in answering the basic economic questions?**

   Yes, each individual votes in the competitive marketplace with his or her dollars.

4. **Is gross domestic product a reliable indicator of a nation's economic health? What might be a better indicator?**

   Currently, gross domestic product is the measure used by the nations of the world. A system that measures only those goods and services that contribute *directly* to the standard of living of the nation's citizens might be better.

5. **Discuss this statement: "Business competition encourages efficiency of production and leads to improved product quality."**

   If there are several products of the same type, the consumer will purchase the products of better quality. Businesses are thus forced to improve their products constantly to maintain or enlarge their share of the market.

6. **In our business system, how is government involved in answering the four basic economic questions? Does government participate in the system or interfere with it?**

   The government is involved in answering the four basic economic questions with regard to promoting public welfare. The question of what goods and services will be produced is answered when government provides goods and services that would not be produced by private enterprise or that would otherwise be too expensive for the average citizen. The question of how these goods and services will be produced is answered by government through taxation that is necessary to pay for goods and services society needs. The question of who will receive these goods and services is answered by the government through programs such as national defense, police and fire protection, education, and construction of roads and highways. The question of who owns the major factors of production is answered by government ensuring that all factors of production are available and shared by businesses involved in a capitalistic society.

Student answers will vary on whether government participates in or interferes with the system.

7. **Choose one of the challenges listed on page 29 and describe possible ways in which business and society could help to solve or eliminate the problem in the future.**

   Students' answers will vary, depending on the challenge chosen by the student.

1.10d Comments on Video Case 1.1

Suggestions for using this video case are provided in the Pride/Hughes/Kapoor Video Guide, which appears at the end of this manual.

Entertainment Means Profits for Nederlander Concerts

1. **Nederlander Concerts competes for audiences and with other concert arenas and promoters. Do you think it also competes for those audiences with television, movies, CDs, DVDs, streaming video, and sports events? Why or why not? If yes, what implications does this type of competition have for Nederlander's business?**

   There is a sense in which all forms of entertainment, even print media, must compete with each other for audience members' loyalty, time, and dollars, which means Nederlander must continue to meet high standards by booking popular artists, staging exciting and well-produced shows, and creating a memorable entertainment experience at a fair price. Students may discuss whether live entertainment can really compete with recorded entertainment or even streaming video online or simulcast. The spontaneity and thrill of a live performance also includes sharing the audience response, an advantage recorded media events cannot provide.

2. **How many different groups can you think of whose needs Nederlander Concerts must satisfy in order to remain a successful business?**

   Nederlander Concerts must produce enough profit to make its owners happy; it must be run fairly to keep its employees happy; it must cut rewarding deals to satisfy the performers on whom it depends; and it must keep audiences happy by balancing supply and demand—presenting the acts they want at prices they can afford. The company must also work well with the cities whose civic theaters it manages and even consider the communities in which its performances are staged so that noise and traffic, for instance, don't inconvenience its neighbors. Although it is privately owned, Nederlander must also comply with local government regulations covering, for instance, allowable noise levels, employee safety, fire safety, and so on.

3. **Give an example showing how Nederlander Concerts utilizes each of the four factors of production.**

   Nederlander Concerts uses land for its physical buildings—theaters, offices, parking lots—and natural resources for electrical energy, heating, air conditioning, and so on. It uses the labor of its own employees and of the performers it books and their crews and staff. Its capital is in the form of equipment like amplifiers, microphones, lighting and special effects systems, and even the seats in the company-owned theaters. Finally, while the firm is not an entrepreneurship, it operates in a highly creative, fast-changing, and competitive industry, so entrepreneurial skills are needed to book the right acts in the right venues on the right schedule.

1.10e Comments on Case 1.2

Caterpillar Helps the World Build

1. **How is Caterpillar using the factors of production to fuel global growth?**

   As it expands worldwide, Caterpillar uses natural resources such as land for its factories and raw materials for manufacturing earth-moving machinery and other equipment required by business customers and governments. Caterpillar uses labor—employees in its various facilities—to develop, produce, sell, and service the equipment it manufactures for different markets. The company also requires capital (in the form of financing, machinery, factories, and offices) as it expands into additional factories and countries. Finally, Caterpillar makes use of entrepreneurship to compete efficiently and effectively as it leverages the other factors of production for current and future growth.

2. **How would you characterize Caterpillar's competitive situation? What are the implications for how it does business?**

   Caterpillar's competitive situation appears to be monopolistic competition, because it has a number of rivals and serves a large number of customers in the global marketplace. As a result, the company must carefully differentiate its products to distinguish them from similar products made by competitors. Caterpillar does this by ensuring product quality, creating innovative new products to meet customers' requirements and expectations, and enhancing its reputation through ethical and socially responsible behavior. Students may suggest other implications for Caterpillar's business situation, as well.

3. **What factors in the business environment appear to have the most influence on Caterpillar's ability to continue its business success? Explain.**

   One factor that greatly influences Caterpillar's continued business success is the global environment. The company knows how to compete against other multinational corporations, and it is knowledgeable about the needs and concerns of customers in local markets around the world. The economic environment is important to Caterpillar's ongoing success because the company must be ready for higher purchases of earth-moving equipment and similar products during economic expansions while shifting its emphasis to customers in developing nations during recessions. Students may also make a strong case for the influence of the technological environment and the competitive environment.

1.10f Building Skills for Career Success

The journal exercises can be used as informal writing assignments that are checked off or they may be graded. Some instructions you may wish to give for Chapter 1 might include the following:

1. Answer all questions.
2. Check grammar and spelling.
3. Bullet points are acceptable.
4. Be honest in your answers—the purpose of these questions is to help prepare you to be a successful employee.
5. Be as specific as possible.
6. Use the language and concepts from the course whenever possible.
7. Provide examples as appropriate.

1. Journaling for Success

Assume that you are now age 25 and are interviewing for a position as a management trainee in a large corporation. Also assume that this position pays $45,000 a year.

(1) Describe what steps you would take to prepare for this interview.

A thoughtful answer should include a brief discussion of research the student will do as well as a self-assessment relative to what the student might have to offer. A sample answer follows.

The first thing I would do is research the company online. I would want to know:

- its mission statement;
- the products and services it provides;
- total revenue and sales; and
- what its growth areas are.

The second thing I would do is look for recent articles on the company to see what problems it may be having or what opportunities exist.

After looking at its situation, I would make a list of the skills and attributes I possess that it could use. For example, if the company is looking to expand into South and Latin America, my minor in Spanish will be an asset.

(2) Assuming that you get the management trainee position, describe the personal traits or skills that you have that will help you to become successful.

Students have a variety of skills they can discuss in this answer. A thoughtful answer might consider traits or skills that have helped them in school and part-time work, clubs, activities, and athletics.

In their descriptions, students should indicate how each particular trait or skill will help them. For example, being *disciplined* means they will be able to set their own deadlines and make sure that work gets done without prodding, while being a *fast reader* means that they can keep up with new information.

A typical student answer might look like the following:

I am a hard-working person who is not satisfied unless a job is done well. Whether it is a paper I write for school or waiting on a customer at work, I make sure that I cover all the bases. I ask questions to make certain that everything is being done correctly. I am also good at organizing a lot of material. This enables me to work on more than one thing without losing my place or missing deadlines.

(3) Describe the one personal skill or trait that you feel needs improvement. How would you go about improving your weakness?

Some traits students may wish to work with include shyness in groups, giving in to others too easily, or a tendency to get flustered when confronted with stress or difficult deadlines. Some things they could do would be to find books or articles that address those issues or talk to professors who could point them in the right direction. Skills are easier to address than traits, as there are courses, programs, and so forth, that help people with their skills.

A typical student answer might look something like this:

I am not as organized as I would like to be. Occasionally, I lose track of papers and deadlines, which creates issues with professors and bosses. I work hard, and my work is good, but I get stressed when I am disorganized. Specific actions I can take include making lists on my computer and saving them on the hard drive rather than on pieces of paper I can lose. I will also keep a calendar and pen by the phone to write down right away any dates I need to remember.

2. Exploring the Internet

Suggestions for using each *Exploring the Internet* exercise are contained on the Web site for Pride/Hughes/Kapoor at www.cengage.com/introbusiness/pride. By using a Web site, we can also replace outdated material with the most up-to-date material available.

3. Developing Critical-Thinking Skills

The answers will vary depending on the students' ages and interests, how familiar they are with their local car dealerships, and what they know about financing. Competition promotes a wide range of products—in this case, models of automobiles and types of financing—to consumers. Competition affects the prices of the product—automobiles and interest rates—and the types of services offered by dealerships and financial institutions. Competition encourages manufacturers and financial institutions to improve their quality by offering better products and better services to their consumers. Competition impacts the way business is done. For example, competition affects the way salespeople differentiate their automobiles from their competitors' makes and models and the way financial packages are offered to borrowers.

Students should recognize that the auto industry is dominated by a few manufacturers and, therefore, operates as an oligopoly type of competition, which restricts them from setting prices by agreement. The amount and degree of competition are determined by the availability of resources in a community.

4. Building Team Skills

Giving students an opportunity to learn something about their classmates will decrease fears, allow relationships and trust to develop, and help move the class toward being a team. The number of students will determine how much time you can devote to each step in the process.

The instructor's role is to keep track of the time and move the students along. Emphasize that time is a resource in the workplace and that time is money. How time is spent can make a difference in the results achieved. Use time wisely.

5. Researching Different Careers

The answers will vary depending on what information the students are able to find. An entrepreneurial environment spurs creativity and encourages new product development, while an entrepreneurial attitude allows an employee to take risks and try new and different things. Solving difficult problems requires moving outside a perceived set of assumptions; this is where an entrepreneurial attitude helps.

Employees are rewarded in many different ways—from cash to promotions. The philosophy of the company determines how it values entrepreneurship and how employees are rewarded for their efforts.

1.11 QUIZZES I AND II

Quiz I

True-False Questions

Select the correct answer.

1. T F Free enterprise is a system of business in which individuals decide what to produce and how to produce it.
2. T F Less than 50 percent of small businesses fail within the first five years.
3. T F Business is the organized effort of individuals to produce and sell, for a profit, the products and services that satisfy society's needs.
4. T F Adam Smith argued that the creation of wealth is properly the concern of private individuals, not the government.
5. T F The business cycle consists of two or more consecutive three-month periods of decline in a country's GDP.

Multiple-Choice Questions

Circle the letter before the most accurate answer.

6. A general rise in the level of prices is called
   a. free enterprise.
   b. inflation.
   c. gross domestic product.
   d. depression.
   e. monopoly.
7. A market situation in which there are many buyers and sellers of a product and no single buyer or seller can control the price is
   a. an oligopoly.
   b. a monopolistic marketplace.
   c. a monopoly.
   d. pure competition.
   e. a laissez-faire market.
8. A system of exchange in which goods or services are exchanged without using money is called
   a. a barter system.
   b. free enterprise.
   c. monetary policy.
   d. fiscal policy.
   e. monopolistic competition.

9. The separation of a manufacturing process into distinct tasks is referred to as
   a. barter.
   b. specialization.
   c. a factory system.
   d. a domestic system.
   e. an economy of scale.
10. A method of manufacturing in which all materials, machinery, and workers are assembled in one place is called
    a. the economic system.
    b. the domestic system.
    c. Slater's system.
    d. the factory system.
    e. an oligopoly.

Quiz II

True-False Questions

Select the correct answer.

1. T F The only difference between the definition of business and e-business is that e-business requires that sales be conducted through the Internet.
2. T F Walmart and Target are often referred to as marketing intermediaries.
3. T F Profit is the payment that business owners receive for assuming the considerable risks of ownership.
4. T F Approximately one-third of our nation's total production consists of consumer products.
5. T F A monopoly is a market (or industry) with only one seller.

Multiple-Choice Questions

Circle the letter before the most accurate answer.

6. Which of the following is *not* one of the four resources used by business today?
   a. Material
   b. Informational
   c. Governmental
   d. Financial
   e. Human
7. Today, the U.S. economy is often characterized as a __________ economy.
   a. laissez-faire
   b. command
   c. socialist
   d. mixed
   e. Smithsonian

8. Many economists refer to the average level of output per worker per hour as
   a. productivity.
   b. inflation.
   c. the business cycle.
   d. real GDP.
   e. the trough.

9. Which of the following is *not* one of the four states in a business cycle?
   a. Peak
   b. Recession
   c. Trough
   d. Recovery
   e. Deficit

10. Before leaving England, __________ memorized the plans for a water-powered spinning machine and set up a textile plan in Pawtucket, Rhode Island.
    a. Eli Whitney
    b. Franklin Roosevelt
    c. Samuel Slater
    d. Mark Cuban
    e. Cyrus McCormick

1.12 ANSWER KEY FOR QUIZZES I AND II AND PREMIUM POWERPOINT EXERCISE AND QUIZ

Quiz I

True-False

1. T
2. F
3. T
4. T
5. F

Multiple-Choice

6. b
7. d
8. a
9. b
10. d

Quiz II

True-False

1. T
2. T
3. T
4. F
5. T

Multiple-Choice

6. c
7. d
8. a
9. e
10. c

Class Exercise

1. Pure competition: product—farm produce
   specific firm—grocery store
2. Monopolistic competition: product—toothpaste
   specific firm—grocery, drug, and convenience stores
3. Oligopoly: product—automobiles
   specific firm—automobile dealership
4. Monopoly: product—electric utility
   specific firm—local utility company

Chapter Quiz—Premium PowerPoint Slide 1-54

1. b
2. c
3. b
4. d

5. a

1.13 CLASSROOM EXERCISES

1.13a Homework Activities

- Have students bring or print out an article that shows an example of one of the challenges facing businesses today as discussed at the end of the chapter.
- Have students identify a public company that they are particularly interested in. Have them explain why they are interested in it, and have them make a list of potential sources they will use to research the company for the duration of the course. They should write a brief overview about the company indicating what industry it is in, who its major competitors are, and where the company headquarters are located. With each assignment, students should document their sources of information, as they would with any research project.

1.13b Classroom Activities

- **Fun Quiz.** Using the "So You Think You Know Business?" Fun Quiz as a handout or a PowerPoint, have students form groups of four or five and give them 10 minutes to see if they can come up with the answers. Then, use the answers from the quiz as a basis for discussion. This is an especially good exercise for the first day. It allows students to have a little fun and meet others in the class.
- **Resource Exercise: What Do I Need?** Divide students into groups of three or four. Using the Resource Exercise as a handout or PowerPoint slide, ask the students to develop a list of the various resources they would need to start a part-time garage cleaning business. You may wish to mention here that Michael Dell started his computer business while still in college. This exercise should take no more than 10 to 15 minutes to complete. Instructor guidelines for completing the exercise appear after the handout.
- **Supply and Demand Exercise.** GarageWorks! Hand out the GarageWorks! fee and customer schedule. Have students get into groups of four and decide how much they will charge to clean a garage. How much labor are they willing to supply at each price? And what happens to demand as they raise their prices? This exercise should take about 10 minutes and stimulate a lot of discussion, not only about how much demand there is for services at different prices but also about how much work people are willing to provide at what pay.
- **Productivity Exercise.** This is a simple exercise that can be done in 10 to 15 minutes. Using the handout or slide, ask students to develop a list of techniques or strategies to help increase the productivity of a gardening hobby that has grown into a profitable little business. This exercise can also be used to lead into a discussion of the differences between services and goods. It is also helpful for introducing the subject of sustainability early in the semester.
- **Crossword Puzzle.** Have students form small groups and work together to complete the crossword puzzle at the end of this chapter. Have a small prize for the team that completes the puzzle first.

1.13c Exercise Handouts Follow on Next Pages

"Fun Quiz"

So You Think You Know Business?

(Answer the following questions to see how much you really know.)

1. **Since 1954, only three companies have been No. 1 on America's Fortune 500 list. They are:**

   ___

2. **The best selling clothing brand on the planet is:**

   ___

3. **The air conditioner was developed by Willis Carrier in 1902. Its original purpose was not to cool homes. What was its purpose?**

   ___

4. **Which college football team inspired Gatorade?**

   ___

5. **What fast-food chain founded in 1964 was named for brothers Forrest and LeRoy Raffel?**

   ___

6. **True or False—Reebok is Turkish for "fleet of foot."**

   ___

7. **In what city was America's first stock exchange located?**

   ___

8. **What company today was originally named the Computer-Tabulator-Recorder Company (C-T-R)?**

   ___

9. **With what product did the term "brand name" originate?**

   ___

10. **What did the term "buck" originally refer to?**

    ___

Sources: Adapted from American Business Trivia, www.journalofbusinessstrategy.com/articles/business-trivia.shtml, accessed July 16, 2006; Business & Finance Trivia, http://morevalue.com/FinanceChannnel/Trivia/TriviaEnter.htm, accessed July 17, 2010.

Answer Key to "Fun Quiz"

1. Since 1954, only three companies have been No. 1 on America's Fortune 500 list. They are:
   General Motors
   ExxonMobil
   Walmart

2. The best selling clothing brand on the planet is:
   Levi's

3. The air conditioner was developed by Willis Carrier in 1902. Its original purpose was not to cool homes. What was its purpose?
   To remove humidity from air in printing and food production plants.

4. Which college football team inspired Gatorade?
   University of Florida researchers were looking for a drink to rapidly replace fluids and help prevent dehydration—the drink was tested on the UF Gators football team.

5. What fast-food chain founded in 1964 was named for brothers Forrest and LeRoy Raffel?
   Arby's. The name stands for RB—Raffel Brothers.

6. True or False—Reebok is Turkish for "fleet of foot."
   False—Reebok is an African gazelle.

7. In what city was America's first stock exchange located?
   Philadelphia

8. What company today was originally named the Computer-Tabulator-Recorder Company (C-T-R)?
   IBM

9. With what product did the term "brand name" originate?
   Whiskey. Producers branded their names on the barrels they shipped out.

10. What did the term "buck" originally refer to?
    Deerskins, which were a common method of exchange in frontier days.

Resource Exercise
What Do I Need?

You and three school friends have come up with a new business—GarageWorks! There are many people working in the landscaping, house-cleaning, and even car-cleaning and dog-washing businesses, but you are going to specialize in cleaning and organizing garages for suburbanites. Some are elderly, some are busy—so you will do the heavy work. What resources will you and your friends need? Initially, you will clean four garages a week while in school.

Work with your group members to come up with a short list of needs. This should take no longer than 10 minutes.

Material resources: What do you need to get started?

Human resources: How many people will you need?

Informational resources: What information do you need access to, and how will you know how well you are doing?

Financial resources: How much money do you need to get started?

Answers to Resource Exercise

A partial list might include:

Material resources: What do you need to get started?

- *Access to at least one large car or van to transport people and equipment/ supplies*
- *Cleaning equipment—Heavy-duty sponges, brooms, rags, towels, sprayers, long-handled cleaners for ceilings*
- *Cleaning supplies—Wood cleaners, concrete and metal cleaners, rust remover, garbage bags, etc.*
- *Work shoes/boots and clothes—Aprons? Overalls?*
- *Organizing supplies—Nails, hammers, shelving, etc.*
- *Bins or boxes to hold and transport equipment and supplies*
- *Some place to keep supplies and equipment when not in use*
- *Other?*

Human resources: How many people will you need?
You have four people in your company. Will you always need—or even have—four people? How many hours do you need to do a "typical" job? How much time will you have to spend getting customers? Advertising? Organizing? Getting supplies? Etc. How will you decide who does what?

Informational: What information do you need access to, and how will you know how well you are doing?
Obviously, you need cost data, including the value of time.
It would be helpful to have a potential customer database, whether generated from family, friends, neighbors, or some other source. You may wish to check the Internet or local library to find out which suburb has the most two-earner families on the assumption that they have the least time.

Financial: How much money do you need to get started?
This is a bit of a trick question, as you would have to know the cost of the equipment and supplies, opportunity cost of giving up your current job, how many trips you would make and where in order to calculate gas and car maintenance costs.

Supply and Demand Exercise

GarageWorks! Fee Schedule

You and three friends have a garage-cleaning business. You are all carrying a full study schedule but need to make some extra money. You have handed out a questionnaire to potential customers to determine what they are willing to pay, and the results are as follows:

TotalTotalProfitProfit
Price per Cleaned Garage*CostsProfitper Personper HourNumber of Customers

$150$20$130$32.50$16.25300

$200$20$180$45.00$22.50250

$250$20$230$57.50$28.75225

$300$20$280$70.00$35.00150

$350$20$330$82.50$41.25 70

$400$20$380$95.00$47.50 30

$500$20$480$120.00$60.00 10

***Notes:**

Price per cleaned garage is based on four people working four hours each.
Profit per person is the total profit divided by four people.
Profit per hour is how much each person makes as an hourly wage.
Based on the above schedule, how much are you going to charge? You will have 400 customers if you charge $100, down to 10 customers if you charge $500. Your costs (supplies, etc.) remain constant. Explain your choice.

GarageWorks! Instructor Notes

Most students will quickly see that they will maximize their income by charging the high price of $500. However, there are only 10 people willing to pay that price. Clearly, demand falls as price rises.

Students who choose that price may argue that since the members of GarageWorks! have a full study schedule, they are better off just doing 10 garages and charging the maximum. This is not a full-time business for them. They may also suggest that after they finish the 10 at $500 and wish to do more, they can always lower the price.

Other groups may feel that there is a long-term opportunity here and may wish to go with a lower price such as $400 or $350. They may feel there is still enough profit so that the original four members may wish to subcontract to friends on an as-needed basis.

It is unlikely that any groups will consider $150 as a viable price. At $16.25 an hour, opportunity cost would apply.

Service Sector Productivity Brainstorming Exercise Handout

Chapter 1 defines "productivity" as the average level of output per worker. An increase in productivity results in economic growth. The Internet along with automation has increased productivity in recent times. Productivity improvements are more difficult to achieve in the service sector than they are in manufacturing.

Your instructor has assigned your team the following scenario:

Your parents have recently retired and have turned their backyard gardening hobby into a small business growing organic vegetables and herbs. They start their seeds in the winter and plant as the weather allows in spring. Because they are organic, they do not use pesticides. All weeding and pest control is done by hand. The resulting foods are sold either at local farm markets or at a small stand in front of their house.

They are fortunate to live in a semi-rural suburb with little zoning regulation that is still close to urban and suburban areas where residents are willing to pay a premium for such foods. In fact, they are able to charge up to 15 percent more than local supermarkets do for similar organic foods. They have built up a strong clientele and could easily sell 50 percent more vegetables if they had more room and more help. They would love the extra money, but at their age, are not anxious to either buy more land, make huge investments in machinery, or start hiring staff. They also love the interaction with their customers. Clearly, this is a productivity issue.

In the next 10 to15 minutes, develop a list of ways they could increase their productivity. Choose a group member to report the results as directed by your instructor.

Service Sector Productivity Brainstorming Exercise Instructor Notes

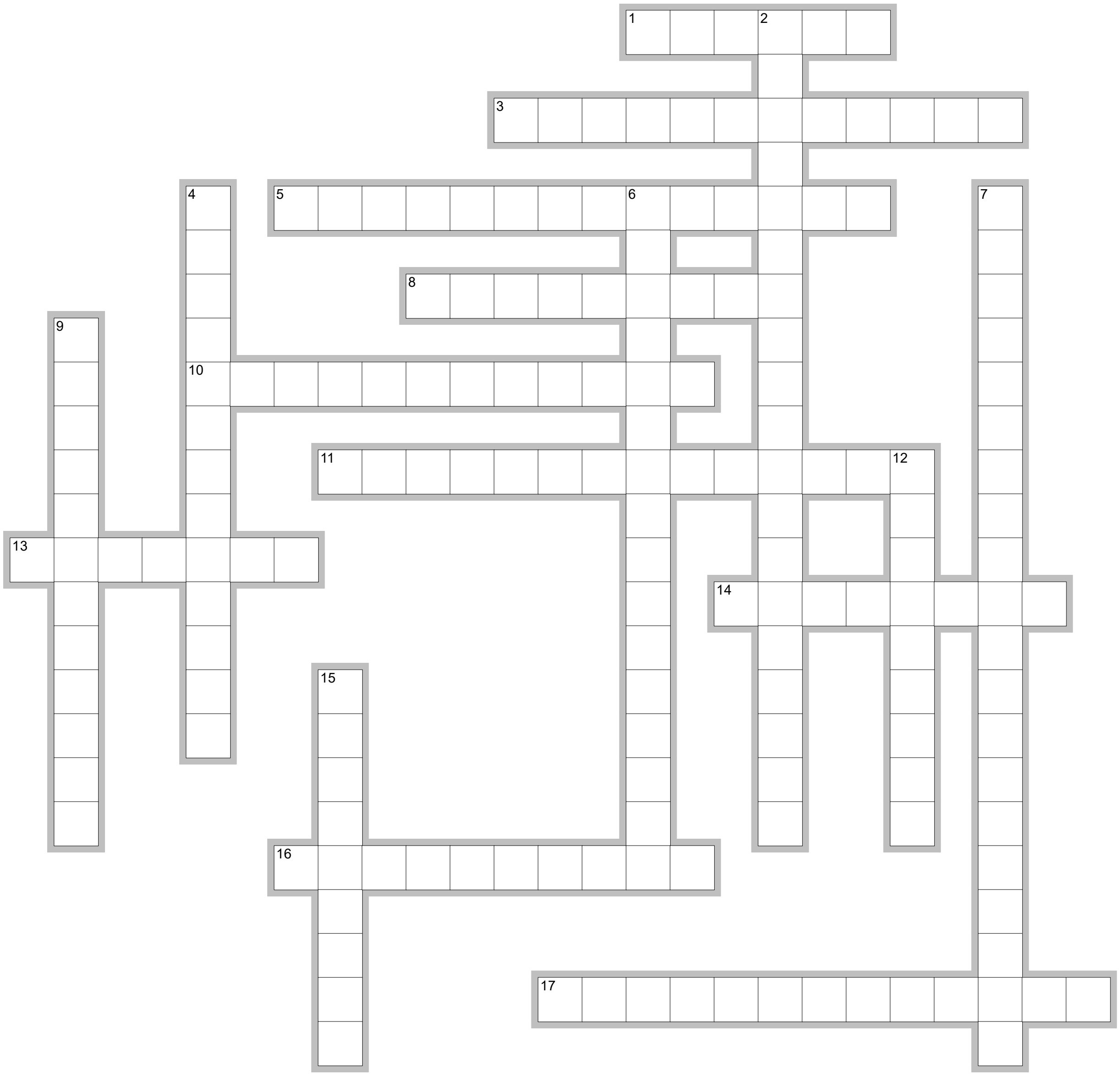
This is a simple exercise, given that there are no employees to be trained or motivated to perform at higher levels. Students should be organized into groups of three or four, with one student designated to report results. This exercise should take no longer than 15 minutes.

Students should be encouraged to discuss any service jobs they may have held and how productivity could have been increased in those jobs. They can then see if those can be adapted for the Mom and Pop Farm scenario. It should be fairly easy for them to suggest items such as the following:

- Establish contact with local agricultural schools for suggestions about time-saving techniques and equipment.
- Research the Internet and journals to see what advances are being made in sustainable farming techniques.
- Investigate the possibility of joining forces with other micro-farmers in the area.
- Consider specializing in a more limited product assortment of vegetables or herbs.
- Grow only the vegetables that provide the highest profit and are the easiest to grow.
- Provide part-time work for middle and high school students on a partnership basis.

This scenario makes it clear that these small-scale gardeners have no interest in growing a major business. As a follow-up, you may ask your students how their answers might change if that were not the case.

1.13d CROSSWORD



Created with EclipseCrossword — www.eclipsecrossword.com

CROSSWORD CLUES

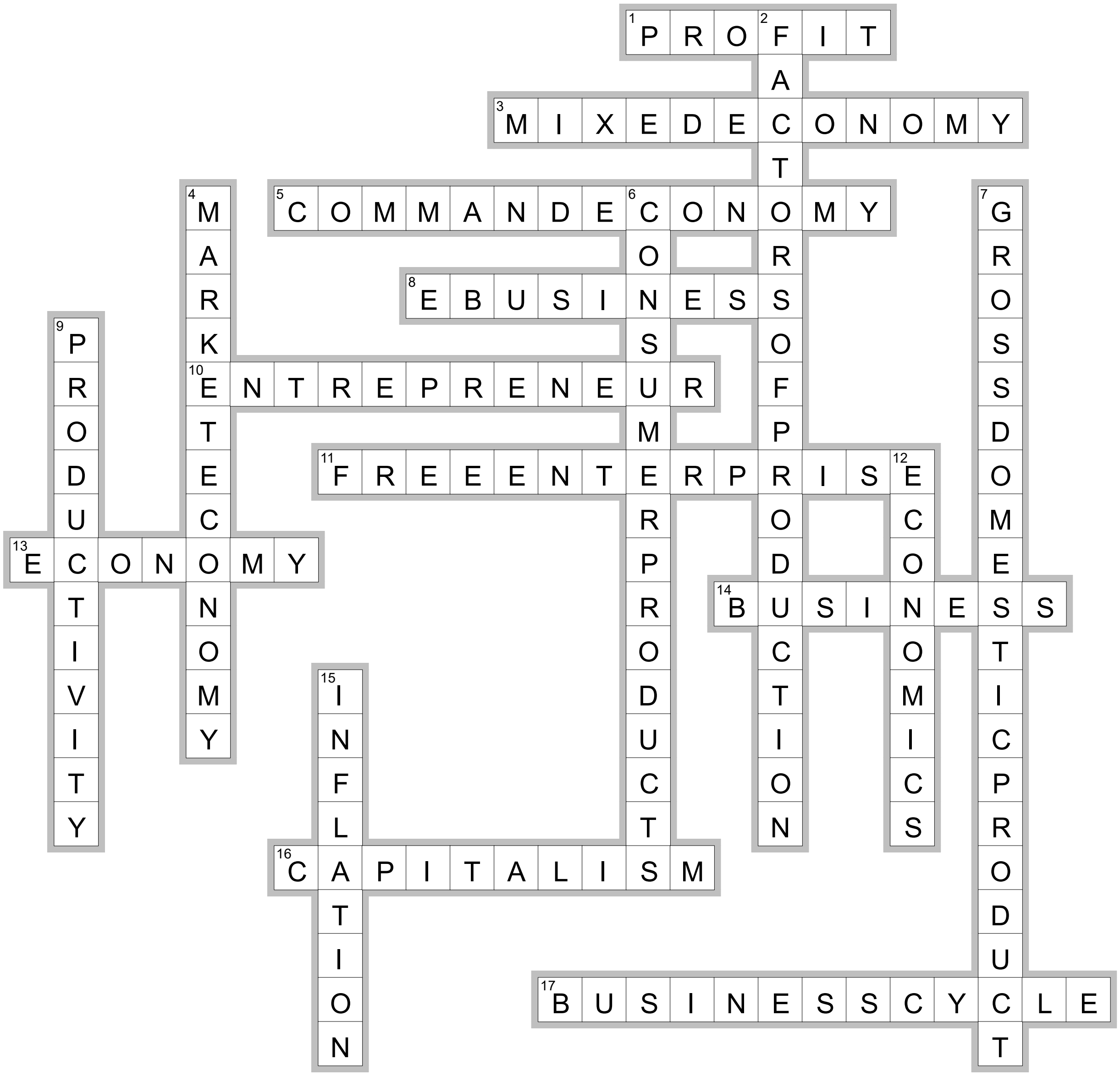
Across

1. What remains after all business expenses have been deducted from sales revenue
3. An economy that exhibits elements of both capitalism and socialism
5. An economic system in which the government decides what will be produced, how it will be produced, who gets what is produced, and who owns and controls the major factors of production
8. The organized effort of individuals to produce and sell, for a profit, the products and services that satisfy society's needs through the Internet
10. A person who risks time, effort, and money to start and operate a business
11. The system of business in which individuals are free to decide what to produce, how to produce it, and at what price to sell it
13. The way in which people deal with the creation and distribution of wealth
14. The organized effort of individuals to produce and sell, for a profit, the products and services that satisfy society's needs
16. An economic system in which individuals own and operate the majority of businesses that provide goods and services
17. The recurrence of periods of growth and recession in a nation's economic activity

Down

2. Land and natural resources, labor, capital, and entrepreneurship
4. An economic system in which businesses and individuals decide what to produce and buy, and the market determines quantities sold and prices
6. Goods and services purchased by individuals for personal consumption
7. The total dollar value of all goods and services produced by all people within the boundaries of a country during a one-year period
9. The average level of output per worker per hour
12. The study of how wealth is created and distributed
15. A general rise in the level of prices

CROSSWORD SOLUTION



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