GLOSSARY OF TERMS

The economic model in this project was developed by William R. Waters, Professor of Economics, DePaul University, who has written the following explanations of the key economic terms related to this model and its application in this unit. They are presented in a logical order for comprehension of the concepts they deal with, and in teaching they could be introduced in a similar sequence in lecture and discussion.

ECONOMY The set of institutions in society that aid people in making decisions of: what and how to produce; what people need for their material wellbeing; who will receive what part of production; what proportion of output is to be devoted to consumption for immediate satisfaction and need and how much to investment or capital formation for improvement of their wellbeing in the future.

KINDS OF ECONOMIES A traditional economy is one where decisions are easily made because things are done the way they have always been done. A capitalist or private enterprise economy is one where decisions are made privately. More completely, there is private ownership of the means of production, private enterprise, and private credit to fund enterprise. Socialism is an economy where decisions are made socially, that is, with the wellbeing of the whole society in view. There are public (social) ownership of the factors of production, public (collective) enterprise, and public decision-making about the projects to be funded.

CAPITALISM An economy with these characteristics: private ownership of the means of production, private enterprise, and private credit. The market system, an important institution for making the crucial economic decisions, is not a key element. Theoretically, at least, we can imagine a socialist market system.

According to historical development, there are these kinds of capitalism:

A) Mercantile Capitalism, a partnership of business and monarchs with specific national regulation; very isolationist and protective.

B) Intact Capitalism, pure capitalism in that government intervention is minimized, innovators are comparatively free, as is the financial sector to finance them. Property rights favor allowing the innovators to use their neighbors' property freely even though the changes they introduce may harm neighbors.

C) Mature Capitalism, in large firms, personal entrepreneurship such as Henry Ford's or Philip Armour's is replaced by managementism. The owners—thousands of stockholders—don't make the crucial decisions. The financial system is controlled and regulated by society. A good proportion of output is produced by the large managerial firms that have their own financing acquired by retained profits. The corporations become more and more public and so are like socialist organizations. There is a dual economy: one half is the output produced by a few thousand large corporations; the other half is the output produced by millions of small and medium-sized firms.

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GLOSSARY (continued)

DECISIONS The operation of the economy is all decision-making. The creative economic decision-making called entrepreneurship is the most crucial because it changes the structure of the economy by introducing new things. Think of the entrepreneur as a chef introducing a new cake. He must coordinate the factors of production; workers, kitchen ovens and other equipment, ingredients; he must get the funding to pay for all of those factors. The consumers make decisions, too. Do they like the new products? There are, of course, many other decisions: those of the workers, sellers of the ingredients, owner of the kitchen, the approval of the banker or capitalist. Each innovation represents the result of the workings of a complex network of human decision-making.

SPECIALIZATION Technological improvement, and thus more efficient production, occurs by dividing labor into more specialized activities. For example, a more effective baseball team will use a left-handed pinch hitter to bat against a right-handed pitcher. An advantage of specialization in production is dexterity. Nations also specialize—Portugal in port winemaking and the Netherlands in tulips. This specialization means a higher quantity and better quality of output.

STRUCTURE OF THE ECONOMY An economy's labor is divided into primary, secondary, and tertiary. Primary is agricultural, mining, and fishing; secondary is manufacturing and processing products; tertiary is employment to produce services. A region can be considered rich according to how high the tertiary employment is in relation to the total. Now 70% is the U.S. rate of tertiary employment, with about 5% in primary and 25% in secondary. In contrast, in 1820 about 65% of the U.S. work force was in primary employment.

OUTPUT The difference between a rich and poor country is the amount of good quality goods and services it can produce. This is called output or gross national product. Related is the country's income, the claims to output. If a country (or region) produced an annual output of $100 billion, then its income, or claims to that output, is $100 billion. A nation's output consists of production for current consumption and for the future (investment). So output equals consumption and investment. The proportion of output devoted to the future (investment) determines the growth of the economy.

CONSUMPTION Goods at the end of the productive process. The demand of the household sector of society. Businesses work to create demand for their products. This is a part of the developmental process. They try to persuade consumers that they should have computers, trips to Australia, and many other things.

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GLOSSARY (continued)

INVESTMENT The key to development is investment or capital formation, which is the production of new construction, equipment, or inventories. If businesses "invest" to form new kinds of capital goods, then development will take place. If they are reluctant, a business recession can occur. If they desert a region, it will stop developing. Such a phenomenon recently has been called the "British Disease" because of the Britain's poor record of economic development in the past 100 years.

SCARCITY The condition where the desire for products is greater than those available. It is not wholly a matter of poverty or deprivation; it is a matter of unsatisfied wants. For example, we have a scarcity of water in some parts of the United States; we have a scarcity of medical services meaning we could use more than presently being made available.

CITY and **CITY ECONOMY** Economies have essential parts: 1) a populous urban area with a core where the most important decisions for the region are made concerning commerce, industry, transport, and finance—in short, the decisions that cause the region to develop; 2) a hinterland of primary production; 3) satellites producing manufacturing and tertiary products. In our day, Atlanta, San Francisco, Los Angeles, and Dallas are examples of developing city economies. Within the city economies are lesser economic capitals called submetropolises. Seattle and Honolulu are examples of submetropolises in the San Francisco city economy, mainly because San Francisco is the important financial capital of the West.

INNOVATION The introduction of a change into the economy. An example is the steam locomotive railway as a new form of transportation. Innovations will be resisted because they damage established techniques. For example, stage coach companies resisted railroads.

FINANCIAL INTERMEDIARIES This name is given to banks and other organizations in the financial sector because they act as an intermediary between a household and business to collect funds for investment. Financial intermediaries include insurance companies, banks, brokerage houses, pension funds, savings and loan associations, and credit unions.

BALANCE OF PAYMENTS A comparison of a region's or nation's revenue and expenditures, including the sale and purchase of products and the flow of funds to buy and sell properties or assets. A successfully developing country may have a deficit in its balance at first, but after some time the balance should reflect a surplus. Citizens in the "creditor" nation or region will begin to own more and more of the other region's property.

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GLOSSARY (continued)

PRODUCTION POSSIBILITIES Nations and regions continually made tradeoffs of high level consumption now or more wellbeing in the future. If the people in society make the choice of consumption now, they are putting off investment. If instead they put off consumption and use resources to increase capital stock (plants, roads, schools), they have decided to invest now to increase the wellbeing of the people in the future.

DEVELOPMENT The change in the structure of the economy as compared to growth, which is just a change in sizes. By illustration, the structure of the U.S. economy changed when railroads were introduced. To produce a large quantity of railroads and other things that already exist is to grow. Development is a change of output, for good or for bad. Growth is more of the same kind of output we have. Development increases the options people have. After railroads came, the people could choose yet another mode of transportation in addition to stagecoach, steamboat, sailboat, and horse.

COMPETITION In economic activity, both competition and cooperation are needed for effective performance. Cooperation to establish community and solidarity necessary for a humane economy and society. Competition to heighten motivation and eliminate waste, thereby bringing about development to improve the material wellbeing of the people. There are other kinds of competition in addition to firms competing with each other. Cities also compete. It was not clear which city would become the economic capital of the Midwest, St. Louis or Chicago. Nations also compete. Some evidence of their success is a surplus in their balance of payments of exports and imports. Most important to development is dynamic competition, that is, competition to innovate. DuPont was of one of the most dynamically competitive firms in the 1950s. The firms of the Silicon Valley, near San Francisco, were dynamic competitors of the 1980s. The core idea of dynamic competition is not the product but that the firm is more successfully innovative than the other.

INTERDEPENDENCE Economic regions are integrated in that the farmers and miners in the hinterland and the manufacturers in the suburbs look to the city for financing and for upper-echelon managerial decision making. For example, in the first half of the 19th century, the New York region extended up the Hudson and along the Great Lakes to Chicago. With fur trading, the region extended all the way to Astoria, Oregon, on the Columbia River. The river network with Philadelphia, St. Louis, New Orleans, other river cities, and the Ohio, Mississippi, Illinois, and Missouri Rivers were parts of another region that also had a social integrity and communal spirit of its own. Business owners, river boat crews, farmers around Louisville, cotton growers in Mississippi had their economic region in common, as did canal workers and sailors on the Great Lakes, manufacturers of the reaper in Chicago, and bankers in New York.

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