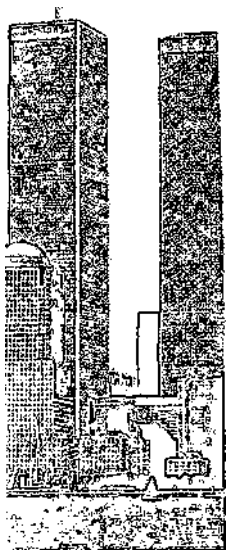


# DETAILED CONTENTS



Preface xx

To the Student xxvi

Acknowledgments xxix

## Part 1 Introduction

### ~~Economics and the World Around Us~~ Defining Moments 3

Chapter Insight 3

Learning Objectives 5

Chapter Puzzle 5

What Is Economics? 5

Defining Moments of Economics 5

1. The Industrial Revolution: The Benefits of Voluntary Exchange 6
2. The Rise (and Fall) of Socialism 7
3. The Great Depression: The Cost of Progress 8
4. Globalization 9
5. The Information Revolution 10

Economic Theory and the Scientific

Method 11

Economic Theories and Models 12

The Scientific Method 12

Logical Fallacies 13

Positive and Normative Economics 13

Unanswered Questions 14

Summary 14

Key Terms 15

Questions and Problems 15

Internet Connection 16

Puzzle Answered 16

Appendix Insight 17

The Use of Graphs in Economics 18

Positive and Negative Relationships 18

Dependent and Independent Variables  
18

Advantages of Graphs 19

Understanding Slope 20

Maximum and Minimum Values 22

Scatter Diagrams 22

Areas of Rectangles and of Triangles 23

The Pitfalls of Graphs 23

The Ambiguity of Slope 24

Inflation and Growth Distortion 24

Unrepresentative Data 25

Summary 25

Key Terms 28

Questions and Problems 28

Internet Connection 29

Chapter Insight 31

Learning Objectives 32

Chapter Puzzle 32

The Economic Problem 32

The Definition of Economics 32

Scarcity 32

Choice 33

Resources 34

Allocation 35

Competing Ends 35

Economic Systems 36

Property Rights	36
Allocation Arrangements	36
Incentives	37
Opportunity Costs	37
Production Possibilities	38
The Law of Increasing Costs	39
The Law of Diminishing Returns	39
Efficiency	39
Economic Growth	40
Economic Growth and the PPF	41
Micro and Macro	42
Microeconomics	42
Macroeconomics	43
The Coming Together of Micro and Macro	43
<b>Summary</b>	<b>43</b>
<b>Key Terms</b>	<b>44</b>
<b>Questions and Problems</b>	<b>44</b>
<b>Internet Connection</b>	<b>45</b>
<b>Puzzle Answered</b>	<b>45</b>
<b>EXAMPLE 1:</b> The Pacific Yew and Cancer: Scarcity, Allocation, and Opportunity Costs	33
<b>EXAMPLE Z:</b> Should We Organize the Internet by Market or by Plan?	35
<b>EXAMPLE 3:</b> Diminishing Returns and American Wines	40

## b i y J the Economic Problem 41

Chapter Insight	47
Learning Objectives	48
Chapter Puzzle	48
The Price System as a Coordinating Mechanism	48
The Invisible Hand	48
Relative Prices and Money Prices	49
The Principle of Substitution	50
Equilibrium	51
The Circular Flow of Economic Activity	52

Specialization, Productivity, and Exchange	53
Productivity and Exchange	54
Money and Exchange	56
Provision for the Future	57
Limits of the Invisible Hand	57
Income Distribution	58
Public Goods	58
Externalities	58
Monopoly	58
Macroeconomic Instability	58
<b>Summary</b>	<b>58</b>
<b>Key Terms</b>	<b>59</b>
<b>Questions and Problems</b>	<b>59</b>
<b>Internet Connection</b>	<b>60</b>
<b>Puzzle Answered</b>	<b>60</b>
<b>EXAMPLE 1:</b> Where Did All the Goods Come From? Russia's Move to a Market Economy	49
<b>EXAMPLE 1:</b> Even Harvard, Princeton, and Yale Must Protect Their Markets	51
<b>EXAMPLE 3:</b> Specialization and the Pin Factory	55
<b>EXAMPLE 4:</b> Comparative Advantage and Hawaiian Pineapples	56

## Chapter 4 Demand and Supply 61

Chapter, Insight	61
Learning Objectives	62
Chapter Puzzle	62
"What Is a Market?"	62
Types of Markets	62
Markets and Competition	62
Demand	63
The Law of Demand	63
The Demand Curve	64
Shifts in the Demand Curve	65
Supply	67
The Supply Curve	68
Shifts in the Supply Curve	68

Equilibrium of Demand and Supply	71
What the Market Accomplishes	72
Changes in the Equilibrium Price	72
Change in Demand (or Supply) versus Change in Quantity Demanded (or Supplied)	72
The Effects of a Change in Supply	74
The Effects of a Change in Demand	75
Simultaneous Changes in Demand and Supply	75
Novel Applications of Demand and Supply	76
<b>Summary</b>	<b>79</b>
<b>Key Terms</b>	<b>79</b>
<b>Questions and Problems</b>	<b>79</b>
<b>Internet Connection</b>	<b>80</b>
<b>Puzzle Answered</b>	<b>81</b>
<b>EXAMPLE I:</b> The NASDAQ Stock Exchange	63
<b>EXAMPLE 2:</b> M&M's and the Law of Demand	64
<b>EXAMPLE 3:</b> The Taiwan Earthquake and Computer Stocks	75
<b>EXAMPLE 4:</b> The Political Elections Market	78
 <b>Chapter Insight</b>	<b>83</b>
Learning Objectives	84
Chapter Puzzle	84
Marginal Analysis	84
Marginal Costs and Benefits	84
Marginal Analysis and Optimal Choice	85
Marginal Analysis and Incentives	86
Games and the Prisoner's Dilemma	86
The Principle of Unintended Consequences	88
Third-Party Payments and Copayments	88
Price Controls and Unintended Consequences	89

Price Controls: The Gas Panic of 1973	91
Rent Controls	91
Marginal Analysis and Unintended Consequences	93
Economic Policy and Unintended Consequences	93
<b>Summary</b>	<b>94</b>
<b>Key Terms</b>	<b>94</b>
<b>Questions and Problems</b>	<b>94</b>
<b>Internet Connection</b>	<b>95</b>
<b>Puzzle Answered</b>	<b>95</b>
<b>EXAMPLE 1:</b> The Rent Gradient and Marginal Analysis	85
<b>EXAMPLE Z:</b> Third-Party Payments and Medical Costs	90
<b>EXAMPLE 3:</b> The Unintended Consequences of Rent Controls: Apartmentless in Santa Monica	92

## Part II Product Markets 97

Chapter Insight	99
Learning Objectives	100
Chapter Puzzle	100
The Price Elasticity of Demand	100
The Coefficient of the Price Elasticity of Demand	101
Calculating the Price Elasticity of Demand	101
Elasticity and Total Revenue	102
Elasticity Along a Demand Curve	103
Perfectly Elastic or Perfectly Inelastic Demand Curves	103
Elasticity Versus Slope Along a Demand Curve	105
Determinants of Price Elasticity of Demand	105
Other Elasticities of Demand	108
Cross-Price Elasticity	108

Income Elasticity	108
The Price Elasticity of Supply	109
Perfectly Elastic and Perfectly Inelastic Supply Curves	110
Elasticity of Supply in Three Time Periods	111
Elasticity and the Tax Burden	112
How the Tax Burden Is Shared	112
Elasticities Determine Who Bears the Burden	113

#### **Summary 114**

#### **Key Terms 114**

#### **Questions and Problems 115**

#### **Internet Connection 116**

#### **Puzzle Answered 116**

**EXAMPLE 1:** The Demand for International Telephone Calls 106

**EXAMPLE Z:** The Importance of Substitutes: Call Forwarding 107

**EXAMPLE 3:** Engel's Law and Income Elasticities: Where ITave All the Farmers Gone? 110

**EXAMPLE 4:** Cigarettes and Marijuana: Complements or Substitutes? 113

### **Chapter? Demand and Utility 117**

Chapter Insight	117
Learning Objectives	118
Chapter Puzzle	118
The Concept of Utility	118
The Law of Diminishing Marginal Utility	118
The Diamond/Water Paradox	120
Marginal Utility and the Law of Demand	121
A Numerical Example	122
Income and Substitution Effects	124
Is the Theory Realistic?	126
Market Demand	126
Consumer Surplus	127
The Role of Consumer Surplus	128
<b>Summary</b>	<b>130</b>

#### **Key Terms 130**

#### **Questions and Problems 130**

#### **Internet Connection 131**

#### **Puzzle Answered 132**

**EXAMPLE 1:** De Gustibus Est Disputandum 119

**EXAMPLE Z:** Marginal Utility, "All You Can Eat for \$10," and the Daily Newspaper 120

**EXAMPLE 3:** Are Consumer Tastes Stable? 125

**EXAMPLE 4:** Consumer Surplus and Your Television 129

### **AppendixTA Indifference Curves**

Appendix Insight	133
Consumer Preferences	134
The Law of Diminishing Marginal Rate of Substitution	134
The Budget Line	135
Consumer Equilibrium	136
Indifference Curves and Utility	137
The Effect of an Income Change	137
The Effect of a Price Change	138
<b>Summary</b>	<b>139</b>
<b>Key Terms</b>	<b>140</b>
<b>Questions and Problems</b>	<b>140</b>

### **Chapter 8 Economic Organization: Property Rights and the firm )))**

Chapter Insight	141
Learning Objectives	142
Chapter Puzzle	142
Property Rights	142
Entrepreneurs	143
Why Business Firms Exist	143
Limiting the Costs of Using Markets	144
Taking Advantage of Economies of Scale	144
Bearing the Risk	145
Monitoring Team Production	145

Profit Maximization	145
Forms of Business Organization	146
Sole Proprietorships	146
Partnerships	147
Corporations	147
The Stock Market and the Goals of the Corporation	149
Business Enterprises in the U.S. Economy	150
The Multinational Corporation	150
Raising Capital for the Corporation	151
Selling Bonds	151
Issuing Stock	151
Stocks or Bonds?	152
Financial Markets	153
Present Value	153
Bond Prices	154
Stock Prices	154
Stock Prices and Resource Allocation	155
<b>Summary</b>	<b>156</b>
<b>Key Terms</b>	<b>157</b>
<b>Questions and Problems</b>	<b>157</b>
<b>Internet Connection</b>	<b>158</b>
<b>Puzzle Answered</b>	<b>158</b>
<b>EXAMPLE 1:</b> The Profit Motive Spurs Flexibility	146
<b>EXAMPLE 2:</b> How Unlimited Liability Almost Ruined Lloyd's of London	149
<b>EXAMPLE 3:</b> The Market for High-Yield Bonds	152
<b>EXAMPLE 4:</b> Tulip Mania	156
Chapter Insight	159
Learning Objectives	160
Chapter Puzzle	160
Productivity	160
The Short Run Versus the Long Run	160
The Law of Diminishing Returns	160

Opportunity Costs	162
Short-Run Costs	163
Fixed and Variable Costs	163
Marginal and Average Costs	163
The Average/Marginal Relationship	164
The Cost Curves	165
Long-Run Costs	167
Shifts in Cost Curves	167
The Long-Run Cost Curve	168
Economies and Diseconomies of Scale	168
Minimum Efficient Scale	170
Productivity Advances and the Cost Curves	171
Defining Moments	172
<b>Summary</b>	<b>172</b>
<b>Key Terms</b>	<b>173</b>
<b>Questions and Problems</b>	<b>173</b>
<b>Internet Connection</b>	<b>174</b>
<b>Puzzle Answered</b>	<b>174</b>
<b>EXAMPLE 1:</b> What Are Marginal Costs in the New Economy?	164
<b>EXAMPLE 2:</b> Flight Management Systems and Cost Minimization.	167
<b>EXAMPLE 3:</b> Shifts in Cost Curves: The Case of Nuclear Power	170
Appendix Insight	175
The Production Function	176
Marginal Physical Product	176
The Law of Diminishing Returns	177
The Principle of Substitution	177
Least-Cost Production	177
The Isoquant	177
Isocost Lines	178
The Least-Cost Rule	179
The Link Between the Short Run and the Long Run	180
Applying the Least-Cost Rule	180
<b>Summary</b>	<b>181</b>

Key Terms	181
Questions and Problems	181

## **Chapter 10      Perfect Competition    183**

Chapter Insight	183
Learning Objectives	184
Chapter Puzzle	184
Scarcity and Competition	184
Competition as a Market Model	184
Economic Profits	186
Perfect Competition in the Short Run	187
The Two Rules of Profit Maximization	187
The Firm's Short-Run Supply Curve	189
The Firm's Supply Curve	192
The Industry's Short-Run Supply Curve	192
Short-Run Equilibrium	193
Perfect Competition in the Long Run	194
Long-Run Equilibrium	194
The Mechanism of Entry and Exit	195
Capitalism the Creator	197
The Gains from Voluntary Exchange or Trade	198
Buffet Pricing: Application to the Internet Market	199
Perfect Competition in the Real World	201
An Overview of Perfect Competition	201
Summary	202
Key Terms	202
Questions and Problems	202
Internet Connection	204
Puzzle Answered	204
<b>EXAMPLE 1:</b> Growth of World Trade and Competition	186
<b>EXAMPLE Z:</b> Entry Is Easy on the Internet	196
<b>EXAMPLE 3:</b> The Invisible Hand: The Paradox of Progress	198

## **Chapter 11      Monopoly and Monopolistic Competition    205**

Chapter Insight	205
Learning Objectives	206
Chapter Puzzle	206
Conditions for Monopoly	206
The Sources of Monopoly	206
The Natural Monopoly	206
Government Protection	206
Exclusive Ownership of Raw Materials	207
Price-Making Behavior	207
Price in Relation to Marginal Revenue	208
The Theory of Monopoly	210
How Monopolies Determine Output	210
Monopoly Profits in the Long Run	211
An Overview of Monopoly	212
Measuring Monopoly Power	213
The Theory of Monopolistic Competition	214
Profit Maximization by the Monopolistically Competitive Firm	214
Product Differentiation and Advertising	216
Applications	217
Price Discrimination	217
Product Durability	218
Summary	219
Key Terms	220
Questions and Problems	221
Internet Connection	222
Puzzle Answered	222
<b>EXAMPLE 1:</b> The Original Bell Telephone Monopoly	207
<b>EXAMPLE Z:</b> Intel's Monopoly	213
<b>EXAMPLE 3:</b> America Online: A Dominant Firm	215
<b>EXAMPLE 4:</b> Price Discrimination: Manufacturers' Coupons	220

Chapter Insight	223
Learning Objectives	224
Chapter Puzzle	224
The Efficiency of Competition	224
Prices and Economic Efficiency	224
Measuring Economic Inefficiency	225
Sources of Economic Inefficiency	226
Sources of Inefficiency in Monopoly	226
Contrived Scarcity	226
Monopoly Rent-Seeking Behavior	228
Externalities	228
Technological Progress, Patents, and Competition	229
Patents	229
New Products and Monopolistic Competition	230
Dynamic Competition	231
<b>Summary</b>	<b>234</b>
<b>Key Terms</b>	<b>234</b>
<b>Questions and Problems</b>	<b>234</b>
<b>Internet Connection</b>	<b>235</b>
<b>Puzzle Answered</b>	<b>235</b>
<b>EXAMPLE 1:</b> Mexican Television Ad Rates	227
<b>EXAMPLE 2:</b> Monopoly Rent-Seeking Behavior: Lobbying and Lawyers	230
<b>EXAMPLE 3:</b> Leapfrog Competition: WordPerfect Versus Microsoft Word	233
Chapter Insight	237
Learning Objectives	238
Chapter Puzzle	238
Oligopoly	238
Measurement	238
The Dominant-Firm Oligopoly	240
Cartels	241
Thinking Strategic-ally: Game Theory	242

The Cournot Oligopoly Game	243
The Prisoner's Dilemma Game	, 245
The Advertising Game	246
The Credible Threat'	247
Oligopoly: The Industrial Organization Approach	248
Obstacles to Collusion	249
Unintended Consequences of Government Regulation	.250
A Defense of Oligopoly	250
A Comparison of the Four Market Forms	251
<b>Summary</b>	<b>252</b>
<b>Key Terms</b>	<b>252</b>
<b>Questions and Problems</b>	<b>252</b>
<b>Internet Connection</b>	<b>253</b>
<b>Puzzle Answered</b>	<b>253</b>
<b>EXAMPLE 1:</b> The Learning Curve	239
<b>EXAMPLE 2:</b> Real-World Burger Wars	247
<b>EXAMPLE 3:</b> Predatory Pricing and the Credible Threat-	248
Chapter Insight	255
Learning Objectives	256
Chapter Puzzle	256
Economics of Regulation	256
The Natural Monopoly	256
Government Ownership	257
Regulation	257
Who Is Regulated?	258
Principles of Rate Regulation	259
The Effectiveness of Regulation	260
Privatization	260
Deregulation	261
Deregulation Legislation	.262
The Effects of Deregulation	262
Antitrust Law	263
The Sherman, Act of 1890	263
The Clayton Act and the Federal Trade Commission Act of 1914	263
Interpretation of the Sherman Act	264

The Rule of Reason, 1911-1945	264
Questioning the Rule of Reason	264
Rule of Reason Returns	266
Definition of Market	267
Network Effects	267
Superior Innovation	268
Mergers	268
Repealing Antitrust Laws	270
Evolving Views of Antitrust	270
<b>Summary</b>	<b>271</b>
<b>Key Terms</b>	<b>271</b>
<b>Questions and Problems</b>	<b>271</b>
<b>Internet Connection</b>	<b>273</b>
<b>Puzzle Answered</b>	<b>273</b>
<b>EXAMPLE 1:</b> Cable Television: Should It Be Regulated?	258
<b>EXAMPLE Z:</b> Licensing Taxicabs: Who Is Protecting Whom?	26.1
<b>EXAMPLE 3:</b> Standard Oil 1911 Versus Microsoft 1999	265
<b>EXAMPLE 4:</b> The Microsoft Case	269
<b>EXAMPLE 5:</b> When Is a Merger Too Big?	270

## **Chapter 15**

## **The Economics of Information 275**

Chapter Insight	275
Learning Objectives	276
Chapter Puzzle	276
Transaction Costs and Information Costs	276
The Economics of Search	277
Information Gathering and Price Dispersion	278
Information Problems	279
The Moral-Hazard Problem	279
The Adverse-Selection Problem	281
The Role of Intermediaries	282
Speculation and Risk Bearing	284
The Economic Role of the Speculator	285
Profitable Speculation	285

Unprofitable Speculation	286
The Futures Market	288
The Mechanics of Futures Trading	289
Hedging	289
Information and Speculation in the Futures Market	290
<b>Summary</b>	<b>290</b>
<b>Key Terms</b>	<b>291</b>
<b>Questions and Problems</b>	<b>291</b>
<b>Internet Connection</b>	<b>292</b>
<b>Puzzle Answered</b>	<b>292</b>
<b>EXAMPLE I:</b> Should Refiners Own Gasoline Retailers?	277
<b>EXAMPLE Z:</b> Shopping in the Twenty-First Century	280
<b>EXAMPLE 3:</b> The Lemons Principle: Adverse Selection	284
<b>EXAMPLE k:</b> Scalping	287

## **Part III Factor Markets 293**

### **Chapter 16 factor Markets W**

Chapter Insight	295
Learning Objectives	296
Chapter Puzzle	296
Competition in Factor Markets	296
Basic Concepts of Factor Demand	296
Derived Demand	296
Joint Determination of Factor Demand	297
Marginal Revenue Product	298
Profit Maximization	299
The Demand Curve for a Factor	299
The Two Sides of the Firm	300
Cost Minimization	302
The Marginal Productivity Theory of Income Distribution	302
Marginal Productivity and Efficiency	303
Marginal Productivity and Factor Incomes	304



The Aggregate Production Function	304
<b>Summary</b>	<b>305</b>
<b>Key Terms</b>	<b>306</b>
<b>Questions and Problems</b>	<b>306</b>
<b>Internet Connection</b>	<b>307</b>
<b>Puzzle Answered</b>	<b>30.7</b>
<b>EXAMPLE I:</b> Farmers and Food Markets	297
<b>EXAMPLE Z:</b> Is the Marginal Productivity Theory True?	301
 <b>Chapter Insight</b>	 <b>309</b>
<b>Learning Objectives</b>	<b>310</b>
<b>Chapter Puzzle</b>	<b>310</b>
The Difference Between Labor and Other Factors of Production	310
Labor Market Trends	310
The Working of the Labor Market	311
Household Production and Leisure	312
Wages and Household Production	313
The Demand for Labor	313
The Supply of Labor	315
Labor Market Equilibrium	316
Efficiency Wages	317
Shifts in Labor Demand and Supply Curves	318
Rising Service Employment	320
fringe Benefits	320
Labor Unions	320
A Brief History of American Unionism	321
American Unionism Today	321
Union Objectives	321
Union Behavior	322
Limitations of Labor Supply	323
Strikes and Collective Bargaining	323
The Effects of Unions on Wages and Efficiency	324

Labor Unions: A Brief International Perspective	325
<b>Summary</b>	<b>326</b>
<b>Key Terms</b>	<b>327</b>
<b>Questions and Problems</b>	<b>327</b>
<b>Internet Connection</b>	<b>328</b>
<b>Puzzle Answered</b>	<b>328</b>
<b>EXAMPLE I:</b> The Elasticity of Supply of Labor	314
<b>EXAMPLE Z:</b> Matching Workers and Employers	317
<b>EXAMPLE 3:</b> Compensating Differentials for Scientists	318
<b>EXAMPLE 4:</b> Monopsony: How Labor Unions Can Increase Wages and Employment	325
 <b>Chapter Insight</b>	 <b>329</b>
<b>Learning Objectives</b>	<b>330</b>
<b>Chapter Puzzle</b>	<b>330</b>
Interest	330
The Stock of Capital	330
Credit Markets	330
The Rate-of Interest	331
Determining the Rate of Interest	331
Real Versus Nominal Interest Rate: The Impact of Inflation	333
The Structure of Interest Rates: Risk, Liquidity, Maturity	334
Rent	336
Pure Economic Rent	336
Quasi Rents	337
Economic Rent and Other Factors of Production	338
Profits	338
Entry Barriers, Risk, and Innovation	339
Sources of Profits	341
<b>Summary</b>	<b>343</b>
<b>Key Terms</b>	<b>343</b>
<b>Questions and Problems</b>	<b>343</b>

**Internet Connection 344**

**Puzzle Answered 344**

**EXAMHE 1:** The Timeless Real Rate of Interest 335

**EXAMHE Z:** The Price of Risk 335

**EXAMHE 3:** "Happy Birthday" and Economic Rents 339

**EXAMHE 4:** The Entrepreneurship of Fred Smith 341

## **Chapter 19 Inequality, Income Distribution, and Poverty 345**

Chapter Insight 345

Learning Objectives 346

Chapter Puzzle 346

Patterns of Income Distribution 346

Sources of Income Inequality 347

Noncompeting Groups 347

Occupational Differences 348

Human Capital Investment 348

Discrimination 350

Screening and Inequality 350

Measuring Income Inequality 352

The Lorenz Curve 352

The Gini Coefficient 352

Facts and Figures on the U.S.

Distribution of Income 353

Government and Income Redistribution 353

A Brief International Perspective 354

What Is a Just Distribution of Income? 355

Natural Law, Marginal Productivity, and the Leaky Bucket 355

The Utilitarian Case for Equality 356

Poverty 357

Definitions of Poverty 357

Trends in Poverty 357

Who Are the Poor? 358

Government Solutions: The Welfare State 359

Unintended Consequences 360

Welfare Reform 361

**Summary 361**

**Key Terms 362**

**Questions and Problems 362**

**Internet Connection 363**

**Puzzle Answered 363**

**EXAMHE 1:** Comparable Worth and Unintended Consequences 351

**EXAMHE Z:** How Important Is Human Capital? 352

**EXAMHE 3:** Why Has the Distribution of Income Become More Unequal? 356

**EXAMHE 4:** Our Modest Negative Income Tax 360

## **Part IV Microeconomic Issues 365**

### **Chapter 20 Market failure, the Environment, and Natural Resources 367**

Chapter Insight 367

Learning Objectives 368

Chapter Puzzle 368

Why Does the Market Fail? 368

Externalities: Private Versus Social Costs 368

Social Efficiency 368

What to Do about Externalities 369

Redefinition of Property Rights 369

Voluntary Agreements 371

Government Taxes and Subsidies 371

Pollution, Externalities, and Government Action 371

Optimal Pollution 373

Pollution and Government Considerations 373

U.S. Environmental Policy 374

Exhaustible Resources 375

Rational Allocation of Exhaustible Resources 375

The Market for Exhaustible Resources 376

The Technology of Resource Extraction 377

The Price System and Exhaustible Resources	378
Recycling of Exhaustible Resources <sup>1</sup>	379
Doomsday Predictions	379
<b>Summary</b>	<b>380</b>
<b>Key Terms</b>	<b>381</b>
<b>Questions and Problems</b>	<b>381</b>
<b>Internet Connection</b>	<b>382</b>
<b>Puzzle Answered</b>	<b>382</b>
EXAMPLE 1: How to Deal with Trash	370
EXAMPLE Z: Unintended Consequences: The Electric Car	372
EXAMPLE 3: Trading Pollution Rights	375
EXAMPLE 4: Doomster Versus Boomster: Are We-Running Out of Natural Resources?	379
EXAMPLE 5: Global Warming—The Great Debate	380

## **Chapter 21**      **Government Spending, Taxation,**

Chapter Insight	383
Learning Objectives	384
Chapter Puzzle	384
Public Goods	384
Nonrival Consumption	384
Nonexclusion	384
Free Riders Versus Cooperation	385
Government Spending	387
Trends in Government Spending	387
Spending by Federal, State, and Local Governments	389
Principles of Taxation	390
Taxes and Fairness	390
Taxes and Efficiency	391
Taxes and Social Goals	392
The U.S. Tax System	392
The Federal Individual Income Tax	392
The Federal Corporate Income Tax	393
Social Security and Payroll Taxes	393

State and Local Government Revenue Sources	395
Is the U.S. Tax System Progressive?	395
Proposals for Federal Tax Reform	395
Tax Consumption	395
Eliminate Corporate Income Taxes	396
Impose a Flat Tax	396
Tax "Real" Capital Gains	396
Index for Inflation	396
Government Surpluses and Deficits	397
How Big Should Government Be?	397
<b>Summary</b>	<b>399</b>
<b>Key Terms</b>	<b>401</b>
<b>Questions and Problems</b>	<b>401</b>
<b>Internet Connection</b>	<b>401</b>
<b>Puzzle Answered</b>	<b>402</b>
EXAMPLE I: Technological Change and Public Goods	386
EXAMPLE Z: The U.S. Income Tax: A Brief History	394
EXAMPLE 3: The U.S. Tax System in International Perspective	400

## **Chapter 22**      **Public Choice 403**

Chapter Insight	403
Learning Objectives	404
Chapter Puzzle	404
Cost/Benefit Analysis of Government Activity	404
Unanimity: The Ideal World	405
Majority Rule	407
Voting Problems	408
Logrolling	408
The Paradox of Voting	410
The Political Market	410
Voters	410
Special Interest Groups	411
Politicians and Political Parties	411
Bureaucrats	412
Proposals for Government Reform	413

Democracies and Economic Efficiency 414

**Summary 414**

**Key Terms 415**

**Questions and Problems 415**

**Internet Connection 416**

**Puzzle Answered 416**

**EXAMPLE 1:** Why Zero-Tolerance Drug Programs Don't Work 405

**EXAMPLE Z:** The Median-Voter Rule and School District Budgets 408

**EXAMPLE 3:** Special Interest Legislation: Ethanol 412

**EXAMPLE 4:** The 2000 Elections 414

**Questions and Problems 696**

**Internet Connection 696**

**Puzzle Answered 696**

**EXAMPLE I:** Does Free Trade Pay? 691

**EXAMPLE Z:** North American Free trade Agreement (NAFTA) 693

**EXAMPLE 3:** The Importance of Intraindustry Trade 694

**Glossary 769**

**Name Index 111**

**Subject Index 779**

In this volume, Chapter 22 is followed by Chapter 35.

## **Part VIII The World Economy 681**

### **Chapter 8 international Trade 683**

Chapter Insight 683

Learning Objectives 684

Chapter Puzzle 684

The Global Economy 684

Mercantilism 684

Reasons for International Trade 685

The Law of Comparative Advantage

The Case of Self-Sufficiency 686

The Case of International Trade 688

The Gains from Trade 688

Low-Wage and High-Wage Countries 690

Intraindustry Trade 692

Trading Blocs and Free Trade 692

The European Union 692

North American Free-Trade Bloc 694

The U.S. Comparative Advantage 695

**Summary 695**

**Key Terms 696**