

Introduction

When I was a child, I spoke like a child, I thought like a child, I reasoned like a child; when I became a man, I gave up childish ways. (1 Cor 13:11, RSV)

[M]an has almost constant occasion for the help of his brethren, and it is in vain for him to expect it from their benevolence only. He will be more likely to prevail if he can interest their self-love in his favour, and shew them that it is for their own advantage to do for him what he requires of them It is not from the benevolence of the butcher, the brewer, or the baker that we expect our dinner, but from their regard to their own interest. We address ourselves, not to their humanity but to their self-love, and never talk to them of our necessities but of their advantages. (Adams Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, Book I, chapter ii, paragraph 2)

[A]lthough people acting in the political [as in the economic] marketplace have some concern for others, their main motive, whether they are voters, politicians, lobbyists, or bureaucrats, is self-interest. In [James] Buchanan's words the theory [of public choice] "replaces... romantic and illusory... notions about the workings of governments [with]... notions that embody more skepticism." . . . [I]nterest groups are organized by people with very strong gains to be made from governmental action. They provide politicians with campaign funds and campaign workers. In return they receive at least the "ear" of the politician and often gain support for their goals. [Jane S. Shaw, "Public Choice Theory," *The Concise Encyclopedia of Economics*]

The great virtue of a free market is that it enables people who hate each other, or who are from vastly different religious or ethnic backgrounds, to cooperate economically. Government intervention can't do that. Politics exacerbates and magnifies differences. (Milton Friedman, "Free Markets and the End of History," *New Perspectives Quarterly*, Spring, 2006).

Economics 101, the first of two semesters of economic principles, is a rigorous introduction to *microeconomic* theory and its applications. The second semester, Economics 102, introduces the student to *macroeconomic* theory and policy.

Microeconomics is the study of the behavior of individuals in their roles as consumers, workers, producers, employers, and so on—in what Alfred Marshall called “the ordinary business of life.” For households, ordinary business includes making decisions about what goods and services to buy and in what amounts, how much of our income to give to others, and how many hours of work to offer. For firms, ordinary business includes decisions about what goods and services to produce for sale and in what amounts, and how much labor and capital to employ in order to do so. This focus on individuals (consumers, workers and the firm’s decision makers) does not mean, however, that there is *no* aggregation; a certain amount of aggregation occurs when we examine markets in which a number—possibly a very large number—of buyers and sellers interact. Aggregation over the economy *as a whole*, however, is the realm of *macroeconomics*.

A necessary condition for success in this course is demonstration of mastery of the economic theory presented. Such demonstration includes not only the ability to explain the theory clearly but also the ability to use the theory to analyze the changes in behavior of economic actors in response to changes in circumstances and to explain the short-run and long-run consequences for the material welfare of society (i.e., of the individuals who make up the society).

Beyond this, however, the successful student will learn how economists *think about* the problems we encounter in the pursuit of a variety of personal and social goals. This “economic way of thinking” is useful in analyzing an amazingly large number of situations, not all of which are *obviously economic*, and certainly not *exclusively economic*, in nature (e.g., the commission

of certain types of crime and ways to discourage such behavior). Judge Richard A. Posner (U. S. Court of Appeals for the Seventh Circuit), one of the founders of the field of “law and economics,” makes the point as follows:

Although the traditional subject of economics is . . . the behavior of individuals and organizations in markets, a moment’s reflection on the economist’s basic analytical tool . . . will suggest the possibility of using economics more broadly. That tool is the assumption that people are rational maximizers of their satisfactions. The principles of economics are deductions from this assumption [However, if] rationality is not confined to explicit market transactions but is a general and dominant characteristic of social behavior, then the conceptual apparatus constructed by generations of economists to explain market behavior can be used to explain nonmarket behavior as well. [*The Economics of Justice* (Cambridge: Harvard University Press, 1983), 1-2]

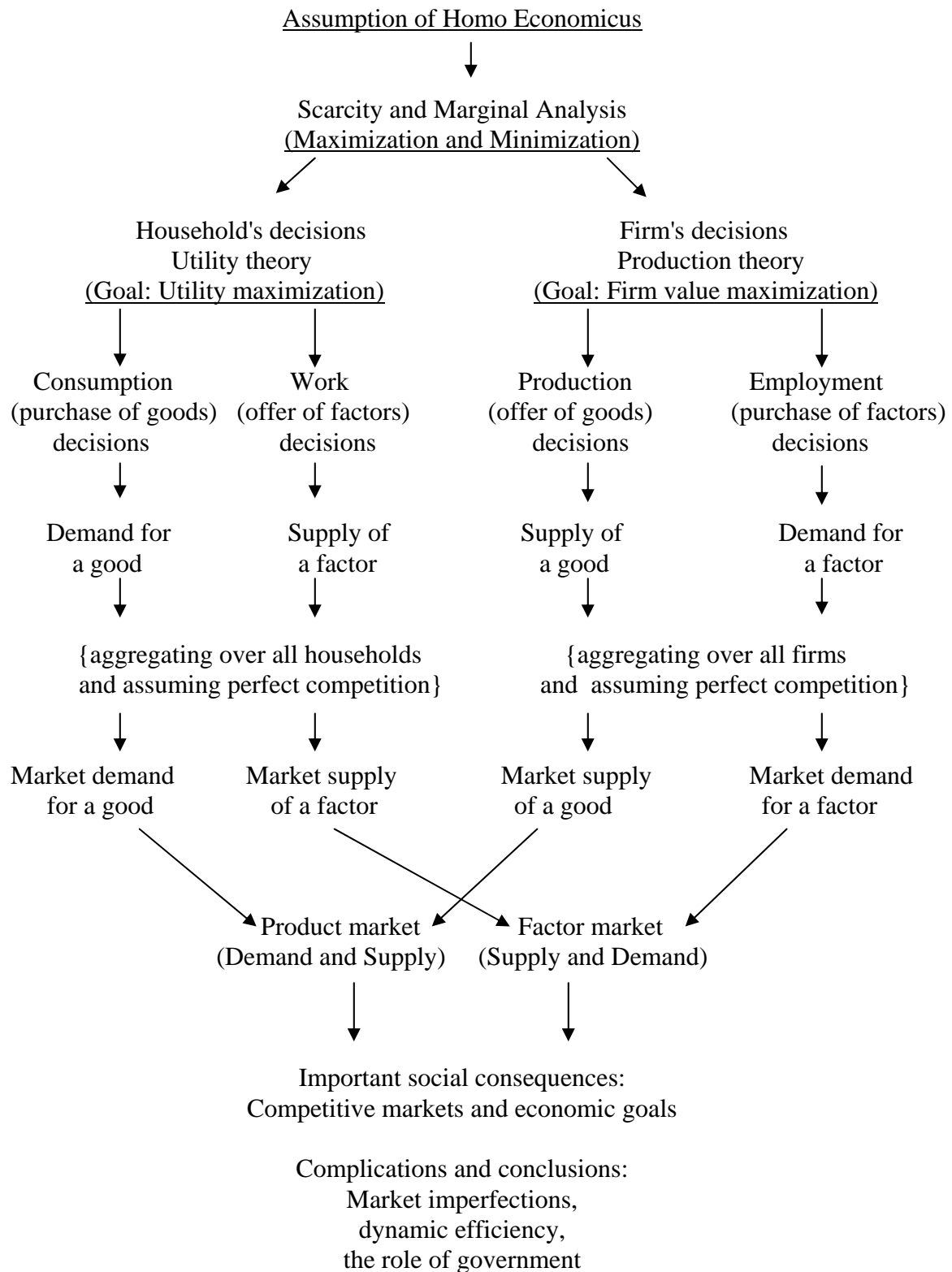
A close friend and colleague of Posner’s, Gary S. Becker, won the 1992 Nobel Prize in economics for “having extended the domain of economic theory to aspects of human behavior which had previously been dealt with—if at all—by other social science disciplines such as sociology, demography and criminology.” (The interested student can check out their joint web log at <http://www.becker-posner-blog.com/>.) More recently, economist Steven D. Levitt and journalist Stephen J. Dubner have applied economic reasoning and empirical analysis to better understand such interesting topics as the relationship between *Roe v. Wade* and the decline in crime in the United States in the 1990’s in their best-selling book, *Freakonomics*.

The point of all this is to emphasize that economic reasoning is important to a broad area of individual and social concerns. The successful student will be able to explain the economic way of thinking and how it leads analysts to certain conclusions and policy prescriptions, even if the student does not ultimately agree with these prescriptions. The ability to use economic thinking is crucial not only to one’s attempts to achieve certain personal objectives but also to a better understanding of the way the world works, and the primary goal of this course is to help students gain the ability to *think like an economist* about a wide variety of issues.

Nevertheless, while you must learn to analyze events and policies as an economist would, it is not the case that you must subscribe to any particular set of values. Decision making involves combining positive analysis of what is possible in any given situation with normative judgments about which goals are most important since reality dictates that not all goals can be achieved in most cases. The positive analysis must be that of the economist; the values are your own.

Rumor has it that this is a difficult course, and it is. However, if you follow the suggestions for how to read the text and how to take notes given in this syllabus, and if you put in at least 12 hours per week on this course (in class, on your assignments, studying, thinking, and practicing), you should do quite well. You will soon discover the way to succeed is to read, think, study, think, practice, and think. If you are not willing to work hard, you should reconsider your decision to take this course.

A “Map” of Economics 101



Primary goal: Demonstrate a mastery of elementary economic analysis
Specific objectives: By the end of the semester, the successful student will be able to

1. explain the meaning of “scarcity” in economics and how this scarcity: (a) is relevant even for relatively wealthy individuals and societies, (b) relates to the necessity of making individual and social choices, and (c) leads to consideration of the important concepts of “opportunity costs” and “constrained” maximization.
2. explain the model of consumer behavior used in economics and how the use of this model under the assumptions of perfect competition leads to the theoretical derivation of (a) the demand curve for a particular good or service and (b) the supply curve of the factor of production we call labor.
3. explain the model of production used in economics and how the use of this model under the assumptions of perfect competition leads to the theoretical derivation of (a) the supply curve for a particular good or service and (b) the demand curve for the factor of production we call labor.
4. explain in detail how prices get set in markets (a) for goods and services and (b) for factors of production under the assumptions of perfect competition.
5. explain in detail, using the above “pieces of the puzzle,” (a) the mechanism of supply and demand by which market societies make the choices necessitated by the existence of scarcity and (b) the consequences for the material well being of the members of that society.
6. explain in detail the costs and benefits to a market society when the assumptions of perfect competition are not met or when markets “fail,” and evaluate the use of government intervention in markets as a means for improving the material well being of the members of society when such problems arise.

Reading assignments

Regular reading assignments will be made in five books. The basic text is *Microeconomics*, Sixth Edition, by Robert S. Pindyck and Daniel L. Rubinfeld. This text will not be assigned in full, but you may want to dip into the unassigned portions for topics of particular interest. A second book in which readings will be assigned is accessible on the internet but also available in the bookstore, *Economics in One Lesson*, Fiftieth Anniversary edition, by Henry Hazlitt. The other three books, which will be the basis of one of your two papers, are by Thomas Sowell: *A Conflict of Visions*, *The Quest for Cosmic Justice*, and *The Vision of the Anointed*. A substantial portion of what one reads in the popular press promotes the agenda of those whom Sowell calls “the anointed” and their “unconstrained vision for society” that is, at best, not practical, and at worst, destructive of liberty as well as the overall welfare of society. Sowell’s thoughts on these matters are worthy of serious consideration.

There will also be readings assigned that are on the academic fileserver (see instructions for accessing the fileserver below), on the internet, or sent to you by email. These readings will be the basis for a brief in-class discussion on the date for which they are assigned and the source of

some short-answer questions on the exams. You will also use some of these readings when writing the “Living Wage” paper described below.

A preliminary schedule of the assignments, with an indication of their relationship to both the map of microeconomics and the objectives for the course, is provided below. It is inevitable that there will be some revisions in these assignments during the semester (hence, “preliminary”). It is your responsibility to keep up with the revisions made in class or through email.

Before coming to class on any given day, you must have read, studied, and thought about the assigned material and made a legitimate attempt to understand and work any assigned problems. Furthermore, you must have reviewed and thought about the assignments for, and your notes from, the previous three classes. For you to obtain the most from class time, it is essential that you come to each class with this preparation.

The best way to read material in the text for the first time is to examine the tables and figures and to read the associated captions. A good part of the material in this course can best be understood with the assistance of numerical and graphical examples, and an initial examination of these examples should make the reading of the text somewhat easier. Then, come to class and take good notes. After class, go over your notes, correct them where necessary, make a note of any questions you still have, read the related material in your text in full, add notes from the text to your notes from class (see below), and practice drawing the graphs.

This may sound like a lot of work. I assure you it is. If you are not willing to do the work required, you should reconsider your decision to take this course.

Class attendance, class participation, and taking notes

You are expected to attend every class session, take good notes, and participate constructively. Bring a ruler and colored pens or pencils to each class since we will be drawing a lot of graphs, and having the appropriate tools is essential. There will be a significant amount of material covered in class that is not in your text, and there will be times when the text and lecture material will differ somewhat. When you have questions about these differences, you should raise them in class. In general, when I give you material that differs from the text there is a good reason for doing so, and I expect you to use the material that I give you.

You are responsible for all material covered, announcements, assignments, and changes in assignments made in class whether you are present or not. If you miss a class, it is your obligation to obtain this information from another student, not the instructor, even if you have a decent reason for missing class (official school business, illness, or family crisis).

One of the keys to success in a class like this is taking good notes. You should take notes only on the front side of each page in your notebook, and you must sit down and go over your notes before the end of the day. Doing so will (1) give you an opportunity to make additions and corrections in your notes, including adding notes from the text, using the backs of the previous pages while the material is still fresh in your mind, (2) reinforce what you learned in class, and (3) help you identify any questions you need to raise in the next class.

Papers

You will write two papers for this course. When grading papers, it is impossible to separate form and content, and your papers will be graded on both. In particular, you need to pay close attention to details such as spelling, grammar, sentence structure, coherence, and so forth.

The body of each paper is to be created as a Microsoft Word document using 12 point Times New Roman type with double spacing and one inch margins. Your name, section number, and the page number must be in the top right-hand corner of every page. The papers must be submitted on time, without staples or paper clips, in a folder that I will give to you for this purpose.

The first paper due will be a review of all three of Thomas Sowell's "Vision" books. In which you are to summarize and evaluate Sowell's thoughts about visions and their impact on a person's attitudes toward markets and preferences with respect to economic policy. A more complete description of this assignment is contained in the assignment section of this syllabus (below), and you will find some help on the basics of writing a book review at the following web site:

<http://www.usd.edu/~khackeme/guides/reviewgd.html>. You should read the content of this web site and the more complete description now and then reread these items, perhaps several times, before writing your review.

The second paper you write will serve as your final exam and concerns an important and timely topic that requires the use of economic analysis, empirical research by experts in the field, and ethical considerations to come to a conclusion about raising the federal minimum wage to what is usually called a "Living Wage." The background readings and the writing of this paper are two stages of a single evaluative process. In the first stage, you read about and come to class prepared to discuss the information and alternative empirical and ethical claims in these readings. In the second stage, you analyze the proposal using the information gleaned from the background readings, the readings assigned in the books by Hazlitt and Sowell, and the analysis developed in the course. Then, adding your own thoughts about the ethical ramifications of the proposal, you derive your own conclusion about the desirability of the policy in question.

Each of the papers should include no more than eight pages of text (i.e., not including graphs which are optional for the Sowell paper but required for the living wage paper). Graphs are to be drawn on separate pages, placed at the end of the text, and included in the pagination.

When working on the papers, you may consult assigned readings, your text, your class notes, and me (if necessary). However, you are not to consult with anyone other than me or to consult papers written by present or former students in this class. When you turn in your paper, by your submission you are pledging that you have followed these rules. Should that not be the case, you are violating the honor code by submitting the paper.

If you do not turn in a paper on the date and at the time it is due, you will be assigned a grade of zero. If you turn the paper in within the next 24 hours, your maximum grade on the paper will be a 75 (out of 100). If the paper is not submitted within the first 24 hours after it is due, your maximum grade will be a 50. After 48 hours, the zero initially assigned becomes your grade. If

you wish to plead for a reduction in penalty for a late paper, you must submit a written, pledged explanation of your failure to meet the deadline when you turn the paper in. I may require that you provide supporting evidence with your explanation. I will be the sole judge of the acceptability of your explanation, and very few will be deemed acceptable.

Exams

There will be two exams in this course, and both will be cumulative. You will find that preparing for the exams will be easy, and that you will do well on the exams, **if** you (1) carefully prepare the assignment for each class, (2) attend class regularly and on time, (3) take good notes and review/revise them daily, and (4) review and study your previous notes and reading assignments before each class. It is not possible to “cram” for these exams, so if you do not take this advice, you will find yourself in deep trouble.

If you miss an exam, you must submit a written, pledged explanation of your failure to take the exam at the appointed time. I will be the sole judge of the acceptability of your explanation, and I may require you to provide supporting evidence with your explanation. If I do not find your reason to be acceptable, or if you submit no explanation, you will receive a zero on the exam you missed.

IMPORTANT: If you have been granted an accommodation by Rhodes that includes extra time on, or a special environment for, tests, you must present me with the relevant form no later than the beginning of class on January 25 so that we can work out the best way to meet your need early in the semester.

Additional important information

1. Students in this class are expected to abide by the Honor Code which covers all exams and papers submitted for a grade and all reasons given for missing exams or paper due dates. Violations will not be tolerated.

2. I want to be available to meet with you on an individual basis as often as you need me to do so. I expect to be in my office (Buckman 331, ext. 3738) at the following times:

Tuesday and Thursday, 1:00 PM to 3:00 PM

If we cannot get together during my regular office hours, I will be glad to make an appointment to meet with you at another, mutually acceptable, time. Please feel free to call me at home before 9:00 PM if need be. My home phone number is 327-5219.

3. There will be many times when I will contact you through email. Therefore, you need to read your email at least once every day. I will use email when necessary to make or change assignments and to provide other information that you need. There may also be times when I will send you Microsoft Word, Microsoft Excel, pdf or other documents attached to email messages; you are responsible for knowing how to save and (when necessary) print these documents. You will be held responsible for all information and assignments or changes in assignments that are sent to you by email. My email address is mcMahon@rhodes.edu.

4. There will also be many times when I want you to retrieve documents from my folder on the Academic Department and Program Fileserver, and it is your responsibility to learn to use this server. When you are using the campus network, to get to my Econ 101 folder, open the Rhodes home page (<http://www.rhodes.edu/>), highlight the address, and replace it with this fileserver address:

\\fileserver1\Acad_Dept_Pgm\Econ_Bus\McMahon_Marshall\Public\ec101

[Note: In the fileserver address, you need an underline, _, between words to indicate spaces.]

Once you have done this, you can create a shortcut on your desktop so that it will be easier to get to this folder in the future. For instructions for accessing the fileserver from off campus, go to:

<http://www.rhodes.edu/InformationServices/TechnologyandFacilities/Off-campus-Network-Access.cfm>

5. If you have problems with email, the fileserver, or any other matters related to use of computers, consult the staff of Information Technology Services. The ITS Helpdesk extension is 4357. You may also send questions to helpdesk@rhodes.edu. It is your responsibility to handle any information technology problems that arise. Do not ask me for help with technology.

6. I make some changes in the way this course is conducted from one semester to the next. You must not assume that something you have heard through the grapevine about this course in the past will necessarily apply to this semester. This syllabus and any modifications I make in class are the only reliable sources for information about the course.

7. I try to enjoy class and to make it enjoyable for you. I have been told that my casual, not infrequently irreverent, attitude can lead students to assume I have relaxed standards for student performance. It would be a terrible mistake for you to act on this assumption.

8. In determining your grade for the semester, I will compute a weighted arithmetic mean of four grades—the Sowell book review (25%), the two exam grades (25% each), and the final paper grade (25%). The resulting number will be rounded to the nearest tenth and converted to a letter grade as follows: 93.0 or above will be an A (there is no A+ for a course grade), 90.0 – 92.9 will be an A-, 87.0 – 89.9 will be a B+, 83.0 – 86.9 will be a B, 80.0 – 82.9 will be a B-, and so on. After computing your grade as indicated, I may adjust it up or down for class attendance and contribution, progress during the term, and such intangible factors as apparent effort or lack thereof. In some cases, such adjustments might change a grade by as much as one-third of a letter (e.g., from a B to a B+, or vice-versa).

9. There are a number of web sites that you might find interesting. One of these is supported by the Foundation for Economic Education (FEE), an organization that takes a libertarian approach to economics and politics. If you are interested in such an approach, you might want to subscribe to their free (in monetary terms) daily email newsletter at <http://www.fee.org/>.

10. If you are interested in reading about current domestic and international political and economic events in depth, you can probably do no better than the *Economist*, which is published weekly, and the *Wall Street Journal*, which is published daily.

Preliminary assignments for Econ 101, McMahon, Spring 2006

Please note: In the reading assignments, *Micro* is short for *Microeconomics*, Sixth Edition, by Robert S. Pindyck and Daniel L. Rubinfeld; *One Lesson* is short for *Economics in One Lesson* by Henry Hazlitt; *Conflict* is short for *A Conflict of Visions*, *Quest* is short for *The Quest for Cosmic Justice*, and *Anointed* is short for *The Vision of the Anointed*, all by Thomas Sowell. (For instructions on accessing the files server, see item 4 under *additional important information*.)

IMPORTANT: (1) These assignments are preliminary; you must keep up with any changes made in class or by email. (2) If you do not “reread and study” or “review and study” whenever that is the assignment, you will cause yourself unnecessary grief. (3) When the definitions I give you differ from those in the text, there is a reason. You are to know and use the ones I give you.

Scarcity and marginal analysis: Maximization and minimization (objective 1)

[1] January 11

Print and read this syllabus. Bring it to class and ask any questions you have about the course and/or the requirements. Refer to your syllabus often; you are responsible for knowing what it says and following the instructions contained herein.

Go to <http://www.jim.com/econ/contents.html> where you will find the Table of Contents for an online version of *One Lesson*. Read and be prepared to discuss the two Prefaces and Chapters 1, 14, 15, 22, and 25.

Start on your lengthy assignment for Tuesday.

[2] January 16

Read and be prepared to discuss **all** of *Conflict*.

[3] January 18

Read pages 1 – 32, read about the production possibilities frontier on pages 596 – 598, and study fig. 16.9 in *Micro*.

[4] January 23

From the files server, download, print, read and study “notesmax.doc.” Bring this document to class with you on this date. Start learning the definitions of the terms in ***bold italics*** (e.g., ***marginal benefit***) in “notesmax.doc.”

From the files server, download, print, read, and think about “TNBprob1.doc.” (Please do not yet open the three documents entitled “TNBprob[2,3,4].doc.”) Bring “TNBprob1.doc” to class with you on this date.

From the files server, download, print and bring to class the two files, “changeTNB.doc” and “fivetangTB.xls.”

Read and be prepared to discuss the content of “1a krugman.doc”, “1b waters.doc”, “1c bernasek.doc”, “1d leonhardt.mht”, and “2 hcvaluecostca.pdf”, in the “healthcare” folder on the files server.

[5] January 25

Work the problem in “TNBprob1.doc.” Use interpolation to add rows for $q_x = 0.5, 1.5$, etc., down to and including 8.5, and fill in the corresponding columns for these rows. Then, draw two

graphs on a single page using the data points given in the table: On the first graph, plot TB, TC, and TNB on the vertical axis and q_x on the horizontal axis. On the second graph, drawn directly under the first graph, plot MB, MC, and MNB on the vertical axis and q_x on the horizontal axis using the same scale for this horizontal axis that you used for the plot of TB, TC, and TNB. I encourage you to work with other students in the class on this and similar assignments. When you have done the very best you can, from the ec101 folder in my folder on the academic volume, download, print “TNBprob[2,3,4].doc.” Compare your results to those you downloaded and printed, and come to class prepared to ask questions. Bring both your work and a printed copy of “TNBprob[2,3,4].doc” to class on this day.

From the fileserver, download and print “timelog.xls.” Use this aid to keep track of how you spend your time over the next seven days. Bring your completed time log to class on February 1. Read and be prepared to discuss the content of “3a friedman.mht”, “3b barnes.mht”, “3c canada.doc”, “3d hurd.doc”, and “4 ahcshow.ppt”. Think about the relationship between the problems associated with providing health care and the relationship between these problems and our discussion of scarcity, production possibilities, and total net benefit maximization.

[6] January 30

Look over the TNB problem and make sure you understand the point. Read pages 128 – 130 in *Micro* and think about the relationship between “consumer surplus” and what we have identified as TNB.

Review documents 1a – 4 on health care and come to class prepared to pick up on the discussion begun on Tuesday.

Think about the meaning of “scarcity” in economics and how this scarcity: (a) is relevant even for relatively wealthy individuals and societies, (b) relates to the necessity of making individual and social choices, (c) leads to consideration of the important concepts of “opportunity costs” and “constrained” maximization, and (d) how (a) – (c) relate to problems in the provision of health care.

From the fileserver, download and print “consumer.doc” and “cardutil.doc.” Read and study these documents carefully and bring them to class.

The household’s decisions and utility theory (objective 2)

[7] February 1

Reread and study “consumer.doc” and “cardutil.doc.” Learn the definitions of the terms in ***bold italics*** (e.g., ***market demand***) in “consumer.doc”, and do your best to work the problem in “cardutil.doc.” As before and as always, I encourage you to work with other students in the class on problem assignments such as this.

Read and be prepared to discuss Chapters 16 and 17 of *One Lesson* and how they relate to “3c canada.doc.” (Look out for Hazlitt’s use of “demand” and “supply” where he should have used “quantity demanded” and “quantity supplied”)

[8] February 6

When you have done the very best you can on the cardinal utility problem, download and print “cardutilso11.xls”, and compare with your results. Come to class prepared to clarify any questions you have about this problem.

Review and study pages 19 – 32 in *Micro*.

Read and study pages 61 – 72, 75 – 89, and 92 – 94.

[9] February 8

Skim pages 32 – 46 and 55 – 56 in *Micro*

Read, reread and study pages 107 – 131 in *Micro*.

Read and study pages 525 – 527 (but don't take the "backward-bending supply of labor curve" too seriously since it is a rare exception).

If you have an interest in calculus, read pages 145 – 152 in *Micro*.

[10] February 13

Review and study all of the material assigned and covered in class to date. Be prepared to ask questions about anything you don't understand. Note that you have a test over this material on February 15.

[11] February 15

First exam.

[12] February 20

Read and be prepared to discuss pages 1 – 95 of *Quest*.

Read and be prepared to discuss the content of (1) "Public Choice Theory" by Jane S. Shaw at: <http://www.econlib.org/library/Enc/PublicChoiceTheory.html> and (2) the introduction and first two sections (I and II) of "Bureaucracy and the Civil Service in the United States," by Murray N. Rothbard at: <http://www.mises.org/story/2181>

Get a start on your assignment for Thursday.

[13] February 22

It's time to evaluate a proposal to reform the provision of health care.

In spite of many failed efforts, there continue to be politicians who want to pass legislation requiring the federal government to fund medical care for all residents of the United States. This care would be provided without regard to consumers' ability to pay and whether or not they have ever paid taxes. Such proposals usually involve increasing taxes paid by people whose incomes are considered "high" by the politicians backing the proposals. Typically, advocates see health care as a human right and believe it is the responsibility of society's wealthiest citizens to provide health care to all—although it is not put quite this starkly. The template for such proposals involves replacing all existing insurance programs with a national health care plan. Under this system, frequently called a single payer system, anyone residing in the U.S. would, theoretically, be able to obtain all health care prescribed by any physician without a direct monetary payment; that is, the patient would not be charged for a visit to the doctor, or for drugs, tests run, surgery, hospital stays, and so forth, when prescribed by a doctor. In effect, the marginal cost of additional health care to the individual consumer of health care would be zero under this arrangement. (Note that this does not say that total cost or average cost would be zero; neither can be zero. Hence, although this is usually thought of as "free" health care, it is not.)

In Bill Clinton's first term as president, Hillary Clinton's task force on health care, guided by Ira Magaziner, proposed reforms in the delivery of health care that were rejected as too complicated, too expensive, and economically inefficient. While the proposal didn't exactly fit the template described above, if adopted, it would likely have evolved into that design. (Recall that Senator Clinton's more recent musings on the provision of health care—along with a critique of Clinton's original proposal by Fred Barnes and several other articles—may be found in the

healthcare folder within the ec101 folder on the fileserver. Interestingly, in November of 2002, Oregon voters turned down, by a four to one vote, a universal health care plan that fit the template quite well except that it substituted the state government for the federal government. Regardless of their lack of success thus far, proponents of universal, single-payer health care are not likely to give up their quest (and, I believe, sooner or later they will prevail).

For class on this day, you are to examine a simplified version of a realistic case in which consumers are faced with a consumption decision involving health care that is provided at a marginal cost to consumers that is much lower than the true marginal cost to society and the average cost to both consumers and society. Under the proposed scheme, provision of health care will be financed by an increase in the income tax on people with “high” incomes (as defined by our elected representatives). The result is that health care will be “overused” in a very specific and important sense. You are to explain in detail, with the assistance of analytical graphs the problems with such a system.

However, in order to simplify the analysis, you are to abstract from reality and begin by examining two typical consumers who pay no income tax and purchase health care (good X) on the market just as they buy any other good (i.e., neither consumer has health insurance, and health care is just like any other good available in a market). In this case, the consumers get to spend all their income as they wish since they pay no income tax; however, the MC of health care to these consumers is the same as the market price of health care (p_x) which is not zero. The other good that the consumers buy is the composite good Y, also purchased on the market in the usual way so that the MC of Y to the consumer is the same as the price of good Y (p_y) which, in this special case, is unity (i.e., $p_y = 1$). To summarize: Initially,

each consumer is allowed to spend all of her income ($Z = p_x q_x + p_y q_y$),

$MC_{x \text{ to the consumer}} = P_x$, where $P_x > \$1/\text{unit of } x$, and

$MC_{y \text{ to the consumer}} = P_y$, where $P_y = 1$.

1. Starting with the no-tax, market-provided-health-care case, and using two different graphs—one for Sally, a “high-income, healthy” person, and one for Sue, a “low-income, unhealthy” person—illustrate clearly each consumer’s initial equilibrium point. That is, for each consumer, show the total utility maximizing combination of q_x and q_y , given the consumer’s preferences (as embodied in her indifference map), money income, p_x , p_y , *etc.* Briefly explain what is illustrated in these two graphs.

2. Explain, and illustrate on Sally’s graph what happens to her budget constraint after an income tax of 25% is imposed and she has access to health care at zero marginal cost. Then, examining your graph carefully, summarize and explain fully what has happened to Sally’s equilibrium q_x and q_y , and to her total utility, by comparing the post-change equilibrium with the pre-change equilibrium. Explain how you know whether Sally is made better off or worse off by this new policy.

3. Explain, and illustrate on Sue’s graph what happens to her budget constraint, given that she still faces no income tax, but now has access to health care at zero marginal cost. Then, examining your graph carefully, summarize and explain fully what has happened to Sue’s equilibrium q_x and q_y , and to her total utility, by comparing the post-change equilibrium with the pre-change equilibrium. Explain how you know whether Sue is made better off or worse off by this new policy.

4. Explain the interpretation of the results in 2 and 3 in the case in which utility is cardinally measurable. In particular, explain what the effect of this program is on the MU_x (the marginal utility of health care) to all consumers if MC_x to the consumer = 0.

5. Why is it not likely that such a program could make all consumers better off? What groups, including but not limited to the most obvious ones, are likely to gain? What groups, including but not limited to the most obvious ones, are likely to lose? What is likely to happen to the welfare of society as a whole? Explain all your answers. (Note: The last in this series of questions is by far the most difficult, so examine the issue and explain your conclusion carefully.)

6. It is possible—even likely—that the imposition of the income tax in this example (in the real world, the increase in the income tax) on high income individuals will reduce the amount of time they devote to work and the amount of their income they save. Why is this so? If it does these two things, what impact will this have on society? Explain all your answers.

7. Do you favor such a proposal? Explain why or why not.

I encourage you to work with others in the class on this assignment.

The firm's decisions and production theory (objective 3)

[14] February 27

Read and study pages 187 – 241 in *Micro*.

If you have an interest in calculus, read pages 256 – 260.

From the fileserver, download and print “prodcost.doc.” Read the first two pages of this document carefully several times, learn the definitions of the terms in ***bold italics*** (e.g., “***production function***”), read through Part A of the production and cost problem, and study the graph on page 5.

[15] March 1

Do your best to work the problem in “prodcost.doc.” As always, I encourage you to work with other students in the class on problems. When you have done the very best you can on your own, download and print “LRcost.xls” and “SRcost.xls” from the fileserver. Compare your results to those you downloaded and printed, and come to class prepared to ask questions. Bring both your work and your printed copies of “LRcost.xls” and “SRcost.xls.”

[Continued on next page]

Read and study pages 675 – 682. We will not cover this material in class, but try to get as much from this appendix as possible. In particular, do your best to get the basic idea of “regression analysis.” You may want to refer back to this appendix from time to time.

[16] March 6

Review and study the assignments for February 27 and March 1, and make sure you understand short-run and long-run production and cost. **You need to do this.**

[17] March 8

Read and be prepared to discuss pages ix – 63 of *Anointed*. Reread the instructions for writing a book review at <http://www.usd.edu/~khackeme/guides/reviewgd.html>.

March 13 and 15
Spring Recess.

[18] March 20

Read and be prepared to discuss pages 64 – 142 and 241 – 246 of *Anointed*. Be thinking about how you will approach a review of Sowell’s three “Vision” books (or, at least those parts you have been assigned).

Markets under perfect competition: Supply, demand and important social consequences
(objectives 4 & 5)

[19] March 22

Review and study pages 19 – 32, and reread and study pages 32 – 46 in *Micro*.
Download, print and study “elasticity.doc”, and look at “elasticityexamples” on the fileserver.
Download, print, think about, and bring to class “catfish.doc.”
Read and study pages 261 – 295 and 299 – 318 in *Micro*.

[20] March 27

Turn in your Sowell paper at the beginning of class.

Your assignment is to write a review of all three of Thomas Sowell’s “Vision” books in which you are summarize and evaluate Sowell’s thoughts about visions and their impact on a person’s attitudes toward markets and preferences with respect to economic policy. Since we are nearing the end of your first semester of study of economics, you should have a clearer picture of how Sowell’s thoughts on visions are related to the study of economics and the formation of public economic policy. You will need to rely on this picture in writing this review.

Recall what Sowell said about a number of topics, but primarily those having to do specifically with economics, and evaluate his position. To do this, you will need to come up with examples from your study of economics to illustrate and, if you feel appropriate, disagree with some of Sowell’s ideas. Coming up with examples will not be hard if you have studied this semester as you were advised to do. Using them to illustrate and critique Sowell’s “Vision” books may be a bit more challenging. Remember that, “critique” means more than finding fault, although you may want to do that. While I am a fan of Sowell’s work, you do not have to be. No matter what position you take, you will be graded on how well you argue your position. You are not required to draw graphs to support your arguments in this paper, but you may do so if you’d like, and you should not overlook the opportunity to improve upon a point by doing so. I can imagine a paper without graphs that would be superb, but I can also imagine a paper that would be strengthened by the judicious use of graphs.

You should write for an audience of people who know very little about economics but don’t necessarily realize that. Think about David Waters or some of the other people who approach economic policy as believers in the proposition that a “correct” social conscience demands we provide for the disadvantaged through the political process. (Recall that Waters appears to

believe that it is a moral imperative that “we” provide health care, including expensive organ transplants, because “our society”—in other words, people with “high” incomes—can afford to pay the taxes required to do so. Recall also the judgment of economist [!] David Cutler that we ought to be satisfied with the amount of “stuff” we have and therefore put more of “our” resources into health care.)

I think by now that you realize that those described in the previous paragraph belong to the group that Sowell describes as either “unconstrained visionaries” or “the anointed” or both. If you agree that either economic analysis or Sowellian (pardon my made-up word) thought is unsatisfactory, say so in your paper and criticize economics and/or Sowell based on something solid that you find lacking therein. Include a succinct summation of how studying economics and Sowell has or has not changed your views of the world. Either way, relying on what you have written before this point in the paper, explain why and how you have or have not changed.

[21] March 29

Reread and think about “catfish.doc” and pages 261 – 295 and 299 – 318 in *Micro*.

[22] April 3

Read pages 515 – 522, and 523 - 543 in *Micro* We will return to the topics in these pages with a slightly different approach; for now, work on the basic ideas and the concepts that are similar to concepts we have seen before.

Read and be prepared to discuss Chapter 19 of *One Lesson*.

Read and be prepared to discuss those articles and essays in the “livingwage” folder on the fileserver that are NOT in the “other” folder within the “livingwage” folder.

April 5

Recess

[23] April 10

Review and study the assignment for April 3. **You need to do this.**

[24] April 12

Second exam

Conclusions and complications: Market imperfection and other real-world complications, social consequences and the role of government (objectives 6 – 8)

[25] April 17

Read and study pages 337 – 345, 359 – 371, 381 – 386, and 435 – 441 in *Micro*.

From the fileserver, download, print, read, study and begin working the exercises in “notperfect.doc”

[26] April 19

Reread, study and continue working the exercises in “notperfect.doc”

[27] April 24

Read and study pages 606 – 609, 641 – 645, and 662 – 669 in *Micro*.

[28] April 26

Work on your final paper and come to class prepared to ask questions.

May 1—3:30 PM class

Final exam: Your living wage paper is due in my office no later than noon.

May 4—11:00 AM class

Final exam: Your living wage paper is due in my office no later than noon.

Living wage paper assignment: “An evaluation of the impact of raising the federally mandated minimum wage to a ‘living wage’”

While some people feel that it is a moral imperative to amend the federal minimum wage law to require employers to pay a “living wage” (about twice the current level), others think that any attempt to set a wage rate above the equilibrium wage will create economic inefficiency and significant unemployment in both the short run and the long run. Likewise, while some people believe that adopting a “living wage” will reduce poverty, others think it will hurt the most economically vulnerable workers (for example, the least-skilled workers who are trying to support families) and possibly raise the wages of some groups that do not “need” a higher wage (for example, teenagers who are not trying to contribute to the support of their families). In other words, there are important ethical issues regarding both efficiency and distribution associated with the proposal to mandate an economy-wide “living wage.” Your job is to write a paper analyzing the consequences of doubling the minimum wage using the neoclassical analysis we have developed this semester and the empirical results about which you have read.

You are to assume that the current minimum wage is equal to the equilibrium wage (i.e., that the labor market starts out in short-run equilibrium at the current minimum wage) and that the “living wage” is twice the current minimum wage. The readings from the “livingwage” folder on the fileserver, parts of Pindyck and Rubinfeld, and Hazlett’s chapter 19 present some of the different positions on a mandated wage and some of the relevant empirical findings. In addition, Sowell’s three “vision” books raise issues germane to the wisdom of a legal living wage. You must use the relevant parts of these readings in your paper.

In writing your paper you will make the usual assumptions: the typical firm buys its inputs (labor and capital) and sells its output (good X) in perfectly competitive markets, while the price of capital, the state of technology (as embodied in the isoquant maps), and consumers’ preferences (as embodied in their indifference maps), do not change. If you are to work with different assumptions in any part of the paper, that will be clearly stated.

In this assignment you will use appropriate analytical graphs to highlight problems with the use of a “living wage” as an instrument of social policy by illustrating and explaining the likely short-run and long-run effects of doubling the federally mandated minimum wage. You will do so by answering some specific questions with the aid of appropriate graphs and by blending your graphical and verbal analyses into a cohesive discussion of the problems created should this

proposal be adopted. While you must include in your paper responses to the specific instructions, recall that you are writing an essay, not answering questions on a test. You need to use your graphs by making frequent references to them in the body of your paper. Where appropriate, you are also to use the assigned readings to relate your analysis to the real world. Recall that style, grammar, spelling, etc., are important.

The body of your paper is to be created as a Microsoft Word document using 12 point Times New Roman type with double spacing and one inch margins all around. The graphs are to be drawn on separate sheets of paper from the text and placed before the text. The graphs may be drawn by hand, using a ruler and colored pens and/or pencils. In drawing the graphs, keep in mind the usual instructions: graphs must be carefully drawn and large enough and clear enough to illustrate the point you are trying to make; the relevant curves must be identified, the axes labeled, and units of measurement indicated for each variable. Then, when changes are introduced in a graph, make clear which curves and points represent the situation before the changes and which curves and points represent the situation after the changes.

Your name, section number, and the page number must be in the top right-hand corner of every page of your submission. Do not use a staple or paper clip when submitting a paper. Put your paper back in the folder I gave you and submit it at the beginning of class on November 30.

Specific instructions:

1. After providing a suitable introduction to your paper, turn to the market for labor in short-run equilibrium before the change in the minimum wage and illustrate and explain the effects of the imposition of the doubled minimum wage rate on this market. In your answer, include a brief explanation of the importance of the price elasticity of demand for labor and the price elasticity of supply of labor on the amount of unemployment created by this higher mandated wage. Also briefly explain the impact of this change on the total net benefit created in the labor market.

2. Then, go into greater detail regarding the importance of the price elasticity of demand for labor for the questions of (a) how much disemployment is created and (b) how much total labor income would change as a consequence of the new minimum wage. One of the primary issues in the assigned readings was the sign and size of the coefficient of price elasticity, and you should provide a brief summary of, and your conclusions from, these readings. You also need to consider here, based on the readings and your own logic, which individuals are most likely to gain and which ones are most likely to lose from such a rise in the legal minimum wage.

3. Illustrate and explain the derivation of the demand for labor by a single firm and briefly explain how the market demand curve is derived from the individual firms' demand curves for labor. Then illustrate and explain the derivation of the supply of labor for a single utility maximizing individual. As you explain the derivation of the individual's supply curve of labor, illustrate and explain the price effect, the substitution effect, and the income effect, and explain the importance of the income and substitution effects for the sign (positive or negative) of the slope of the individual's supply of labor curve. Finally, briefly explain how the market supply curve of labor is derived from the individuals' supply curves of labor.

4. Illustrate and explain the effects of the rise in the price of labor on the individual firm's short-run marginal and average variable cost curves for good X and therefore the individual firm's

short-run supply of X curve. Then illustrate and explain the effects of these changes on the short-run supply in the market for good X and the impact of this change on the equilibrium price and quantity in this market.

5. Illustrate and briefly explain how the typical utility maximizing consumer of good X would respond to the changes in the market for good X you described in question 4.

6. Turning to the long run, illustrate and explain the impact of the rise in the price of labor on the firm's cost-minimizing combinations of labor and capital in the production of good X and therefore on (a) the firm's long-run expansion path and (b) the firm's long-run total cost curve. Explain what this would mean for the long-run effects of the mandated higher wage on employment. Then explain the likely effects of dropping the assumption of a given technology in the "ultra long run."

7. Conclude your essay by stating whether or not you favor the proposal and explaining why. In your answer, integrate your theoretical analysis with the empirical findings about which you read to support your conclusion. At this point, also bring in the likely impact of the higher mandated wage rate on society's total net benefit or, in other words, the welfare of all the people affected by the changes you analyzed.

Include the following on the last page of text in your paper:

Pledge: I have neither given nor received any unauthorized aid on this paper. I have followed the instructions regarding discussion of this paper given in the assignment. This paper represents my own work in the sense both that I have followed the instructions and that I understand the graphs and explanations.

Signature _____