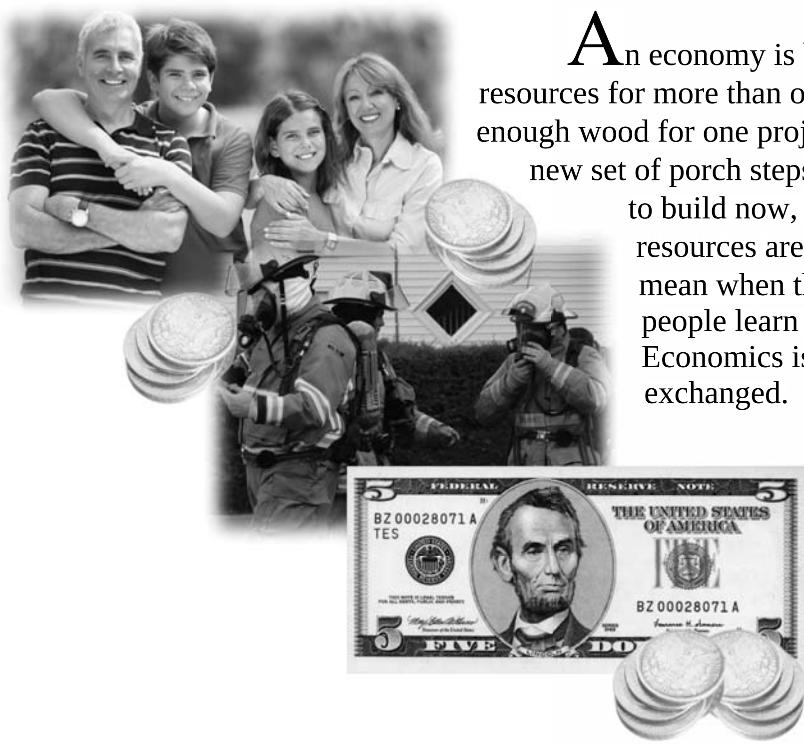
Principles and Precepts of Economics

Topic 1
Defining Economics

Chapter 1

Section One
Introduction to Economics



An economy is basically how people use limited resources for more than one purpose. For example, if you have enough wood for one project, but need a new picnic table and a new set of porch steps, you will have to decide which project to build now, and which one to put off until additional resources are available. That is essentially what people mean when they talk about ***scarcity*** in economics. Wise people learn to use limited resources responsibly. Economics is the science of how money and goods are exchanged.

Perhaps you have experienced financial conflict in your own family. Understanding a ***family economy*** helps you to understand how a national economy works. Your parents work to exchange their time, skill, and effort for financial ***compensation***. Then, the money is exchanged at stores or online shopping sites for goods or services needed by your family. Those resources must then be shared; otherwise, conflicts will arise.

You can probably think of some things your family needs weekly, such as groceries or fuel. Perhaps you can recall other items that were bought with far less frequency, such as a new vehicle. Most likely, you can think of a time when your family had a need, but finances were not available to meet that need right away. As such, you have first-hand knowledge of the concept of scarcity.

Scarcity is also a community issue. The community could be your neighborhood, your scouting group, or even your local church. Each community has needs and a limited amount of resources to meet those needs. People learn to find new ways to get additional resources through cost-cutting, extra jobs, shopping at thrift stores, or garage sales. For these endeavors to

VOCABULARY

Scarcity: limited resources
Family Economy: family policies to acquire goods and services
Compensation: payment for goods or services

be successful, people invest their time and personal resources for the greater good. The more successfully you and your family handle your own resources, the more good you can do to help others.

Another type of economy is a local city economy. People in towns and cities must find ways to raise funds to take care of sidewalks, provide for police, fire, and ambulance services, and a lot of other things that require time and money. Cities raise funds in many ways, including local property or sales taxes, license fees, ***punitive fees***, and through utility fees for water, electric, and waste management.

A state economy works much like a local city economy, but on a much larger scale. Each state needs to provide services such as maintaining state highways and providing for the common defense through a state national guard, and maintaining the state government. These things can be expensive, so in addition to ***revenue*** sources used by local cities, a state can also require its citizens to pay an ***income tax*** or sales tax.

VOCABULARY

Punitive Fees: fees collected by government as punishment
Revenue: money collected through taxes
Income Tax: a tax imposed on annual earnings
Founding Fathers: individuals who designed America’s founding documents
Commodity Money: money based on the value of silver or gold
Tangible: an item detected by human senses

Municipal Firemen

The largest of all economies is the federal economy. Our Federal Government oversees all aspects of governing the nation, including raising revenues and providing protection and essential services. As we will see later, our Federal Government provides far more services and resources to its citizens than our ***Founding Fathers*** ever imagined or intended. We will learn whether that is a good or bad thing. Just as state governments use state income taxes to raise funds, the Federal Government collects federal income taxes, as well as many other types of taxes, to raise revenue.

Money drives most modern economies, so let’s examine different types of money. In order for paper money to have value, it must be backed by something of value. We will learn more about the history of money later, but for now let’s just consider some basic concepts.

Commodity money refers to using a ***tangible*** item of some kind as a source of money. The most common type of commodity money in history has been precious metals, like silver and gold. These commodities are rare (so they have value), are easy to mint into coins, and their value is universally recognized and accepted.

Commodity money is the safest kind of money. Until recent times, the United States dollar bill was backed by gold and silver, therefore a one dollar bill had value because it could be traded for the same amount of gold or silver. People had faith in the paper dollar because it was backed by precious metals. Remember, commodity money is the best kind of money.

Another type of money is called ***representative money.*** This really isn't money at all, but *represents* real money. A classic example is a check. If your employer pays your wages with a check, you are paid in representative money. You can take it to a bank and exchange it for cash, which you can then spend on goods or services. Of course, you can deposit the funds into your own checking account and write checks for the things you need, thus using representative money.

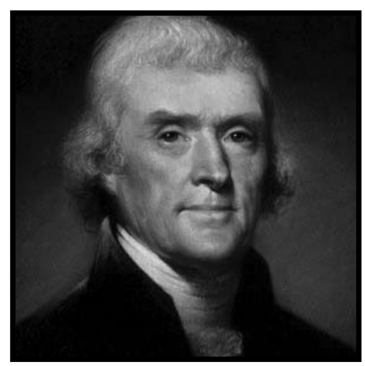
Fiat money represents the worst kind of money, because it has no ***intrinsic*** value. People accept fiat money as payment for goods or services because most governments operate on fiat money. It has no real value of its own, and is not backed by anything of real value. In and of itself, it is worthless. So, we will study where fiat money originates, and why it is accepted as payment for goods or services. For now, remember this: every American bill currency, regardless of the ***denomination*** (one's, five's, ten's, twenties, etc.) is fiat money. Americans accept it because the federal government operates on fiat money.

In the next topic, we will learn about how government policies affect household economics.

VOCABULARY

Representative Money: check, money order, or bank draft
Fiat Money: money made legal through government decree
Intrinsic: in and of itself
Denomination: the printed value of currency

LIFE PRINCIPLE:



"Never spend your money before you have earned it."

-Thomas Jefferson
(Founder, 3rd U.S. President)