

About Economics in U.S. History

BASIC ECONOMIC CONCEPTS

- A **need** is something that a person requires to sustain their life, including food, shelter, and clothing. Needs have evolved over time and continue to reflect where and how people live today. For example, education and health care are considered needs in many societies.
- A **want** is anything that a person is interested in having but does not need for their survival. Like needs, wants have evolved over time and vary among individuals, cultures, and locations.
- **Resources** are necessary for producing products or services that meet human needs and wants. They fall into one of three categories: natural, capital, and human. Natural resources occur in nature and may take the form of raw materials like lumber or minerals. Capital resources include the money, tools, machinery, workplaces, and equipment necessary to make a good or service. Human resources are the individuals, and their expertise and time, required to produce a good or service.
- **Goods** are tangible items that are sold to consumers, like bicycles, computers, or shoes.
- **Services** are processes or tasks that are sold to consumers, like haircuts, roof repair, or food delivery.
- **Consumers** are the individuals in an economy who buy goods and services from producers to meet their wants and needs. To be a consumer, an individual generally has to be a producer in some way to earn income to buy goods and services.
- **Producers** are individuals in an economy who provide a good or service to consumers. Producers provide goods and services to earn income so that they may become consumers to meet their own wants and needs.
- **Scarcity** occurs when there are insufficient goods or services to meet the wants and needs of all consumers. Scarcity generally drives up the demand for and the price of a good or service.
- **Opportunity cost** is the value of the option that was not chosen whenever a choice is made. For example, if a business decides to invest its profit in new equipment, the opportunity cost may be that less money is available to hire or train new employees.

The Three Economic Questions

In any economic system, producers must answer three fundamental questions:

1. What to produce?
2. How to produce it?
3. For whom to produce it?

In a free market economy, producers determine what goods to make or services to offer. This decision is shaped by consumer demand. Producers should consider how much of an item to produce; too much supply may exceed consumer demand and result in a loss of profits. This decision may also be influenced by what resources are readily available to the producer. For example, if there is a scarcity of lumber, a producer is unlikely to decide to produce wooden toys.

Once they have identified what to produce, producers are then tasked with deciding how to make their good or service. This includes determining necessary or available natural, capital, and human resources; where to produce; and the most efficient processes to keep costs low.

Finally, producers must consider who their consumer is and how they'll get the good or service to the consumer.

Economic Choices

Numerous factors influence economic choices—often multiple factors at the same time.

Scarcity drives economic choice by increasing the willingness of consumers to pay a premium for the item. When the cost of the item becomes too prohibitive, consumers seek out alternative goods or services. Producers may intervene to reduce scarcity by importing resources from other countries.

Economic decisions involving scarcity involve trade-offs, meaning that by choosing one option, the consumer is sacrificing another. Trade-offs are weighed through opportunity costs, or the value of what the consumer loses in making their decision. For example, a student is faced with the decision to go to the movies with friends or study for an exam. If the student goes to the movies, they'll have a fun time, but their opportunity cost is being prepared for their test. If the student stays home and studies, they'll be prepared for the exam, but their opportunity cost is missing out on time with friends. In either scenario, the student gives up the benefits of the other choice.

Like scarcity, incentives encourage individuals to make trade-offs. Unlike scarcity, however, incentives provide motivation to make a choice. Incentives often take the form of financial motivation. For example, a discount on cereal may incentivize a consumer to purchase one brand over another. The offer of a higher salary at another company may incentivize a worker to change jobs. Incentives also include other forms of motivation. A worker may leave their job for a position in a company that pays less money but offers the option to work from home. Consumers may be incentivized to purchase items based on exceptional marketing or social influences from peers or celebrities. Incentives are not always positive and can serve to deter behaviors, like receiving a parking ticket for failing to move a vehicle after the meter expires.

Economic choices may be influenced by personal values, or the beliefs that guide an individual's actions. One example is prioritizing environmentally or ethically conscious goods and services over others. When presented with two similar products or services, a consumer may choose to spend more money on a product that was produced in a factory that pays its employees a living wage rather than a less expensive alternative. Another consumer might prefer to spend their money on goods that are made from recycled or environmentally friendly materials.

Budgets factor heavily in the economic decision-making process. Individuals have a finite amount of money to spend weekly and monthly. Budgets help individuals determine how to allocate their money based on fixed and projected costs. Budgets may also determine discretionary income that may be spent weekly or monthly or help individuals put money aside to save for goods and services they may want at a later time, like a vacation. Budgets involve trade-offs; individuals must decide what goods and services they can afford and what they cannot, resulting in choosing one option over another.

METHODS OF EXCHANGE

Barter

Bartering involves the direct exchange of one good or service for another of equivalent value. Prior to the transaction, parties agree on the relative value of what they have to exchange.

Bartering was central to the economies of early civilizations prior to the development of money and remains the primary means of exchange in traditional economies today. Between 9000 and 6000 BCE, early civilizations used livestock and crops such as grains as a standard of barter. Bartering occurred within and between civilizations in the ancient world. The Phoenicians, a seafaring people, built an extensive trade network beginning in the 900s BCE that frequently relied on bartering goods with other civilizations around the Mediterranean.

Bartering has several advantages and disadvantages as a method of exchange. It fulfills people's needs while simultaneously building community. It also eliminates the need for physical money or credit. At the same time, bartering in today's world can be impractical. Individuals would have to find others to trade with who have what they want and are interested in what they have to exchange. Building bartering relationships is also time-consuming, especially if parties disagree on the value of the goods they would like to exchange.

Money

While money today is generally considered to be metal coins or paper notes, it's really any object that is widely accepted as payment for a good or service.

One example is the use of cowrie shells as currency by African, European, and Asian traders. Cowrie shells may have been used in China as early as 1200 BCE. The first metal money and coins appeared around 1000 BCE, at the end of China's Stone Age, with coins made from silver and other precious metals appearing around the Mediterranean world starting around 500 BCE. The first paper money was printed in 806 CE in China, where it was used for several centuries before disappearing around 1455.

Money presents numerous advantages to consumers. It's a widely accepted form of payment with a clearly defined and relatively stable value over the short term. It's a way to easily measure the value of products and to understand the value of other goods and services in relation to each other, making it an excellent tool for making buying decisions. One major disadvantage of money is that its value in terms of purchasing power is subject to inflation. When the costs of goods and services increase rapidly over a short period of time, the relative value of money decreases.

Credit

Credit is the ability to purchase a good or service by borrowing money from a bank. Today, people associate credit with credit cards, either physical pieces of plastic or accounts tied to applications on smartphones, but credit has been around for thousands of years. Historians and archaeologists believe that ancient Sumer was the first civilization to offer agricultural loans, in 3500 BCE. Credit practices, including setting interest rates, were codified under Hammurabi's Code in Babylon in 1800 BCE.

Historically, merchants, shop owners, and eventually retailers offered credit directly to trusted consumers. This system changed during the twentieth century with the growing consumer economy. Industrialist Henry Ford realized that consumers could not afford to buy his Model T up front, so he offered financing and installment plans so the purchase could be paid off over time. Other manufacturers soon followed suit. After World War II, banks and other financial institutions became the primary source of credit for consumers. Increased mobility led to the adoption of credit cards that could be used anywhere in the country.

The advantage of credit is that it allows people to make a purchase and pay back the lender later. Failure to pay back the money borrowed, however, results in the accrual of interest, raising the overall cost of the purchase and increasing the risk of credit card debt.

THE MARKETPLACE

The marketplace has many meanings. At its most basic, it's a physical location where goods and services are sold. The marketplace, or simply the market, has a different meaning in today's economy. The modern market is the entire geographic area where economic transactions between producers and consumers occur. This might be a state, a country, or even the entire world. These spaces account for the numerous transactions between intermediaries that take a good or service from the initial producer to the final consumer. The term *market* can also refer to a specific sector of an economy, like the housing market or the financial market.

Markets are constantly changing, and they play a key role in determining how much consumers pay for goods and services. One way they do this is through supply and demand. Producers generate supply to meet consumer demand. When demand for a good increases, producers may increase production. If the availability of resources needed to produce that good are limited, the producer may simply increase the price of the good. When supply increases, demand for the product generally goes down. Excess supply may cause prices to decline, too.

Competition is another factor that influences how the market functions. Producers compete with one another for the business of consumers. This competition has a significant impact on prices. More competition leads to lower prices for goods and services of a similar quality.

Government Influence

Governments play a role in economies to varying degrees and to varied effect. Most countries around the world have some version of a mixed economy, meaning that some aspects of the economy are left to free enterprise while others are regulated or owned by the government. In the United States, private individuals and businesses own their resources and the means of production. The U.S. government, like other governments around the world, intervenes in the economy through various programs and policies.

One reason the government intervenes in the economy is to improve the standard of living. An example is regulations that protect workplace safety. Another way is by providing unemployment insurance that provides benefits to individuals who have lost their jobs due to layoffs.

Governments also influence the economy through monetary and fiscal policy. Monetary policy is conducted through a country's central bank to achieve specific macroeconomic goals.

In the United States, the Federal Reserve, or the Fed, is charged by Congress with maximizing employment and stabilizing prices. The primary way the Fed meets its mandate is by manipulating the federal funds rate, an interest rate for exchanges between banks. To curb inflation and stabilize prices, the Fed may raise the federal funds rate. This makes borrowing more expensive and reduces spending, forcing producers to cut costs, such as by laying off workers. To stimulate the economy, the Fed may lower interest rates to encourage new development and investments.

Fiscal policy is based on the ideas of British economist John Maynard Keynes and refers to how the federal government influences the economy through taxation and spending. Taxation and spending are generally done in tandem to achieve a goal. For example, Congress may increase spending to supplant private sector spending and lower taxes to free up capital to stimulate the economy during a recession. Congress may take inverse action to cool an overheated economy where spending is rampant, raising the threat of inflation, by raising taxes to discourage spending and investment.

The Influence of Climate Change

Climate change poses a growing threat to the global economy. Rising global temperatures are contributing to rising sea levels and increasingly extreme and erratic weather patterns. Certain populations, especially those in equatorial and coastal areas and those living in countries with developing economies, stand to bear the greatest burdens caused by these changes.

Climate change, if left unchecked, will continue to disrupt food production, interrupt supply chains, and damage infrastructure. For example, increased rainfall and subsequent flooding threaten crop production in areas such as the American Midwest. Rising temperatures and persistent drought have contributed to rampant wildfires in California and Australia, resulting in catastrophic damage to homes, businesses, farms, and plant and animal life.

The banking institution Morgan Stanley estimated that climate change inflicted more than \$400 billion in damages between 2016 and 2019. Beyond the cost of repairing destruction, climate change is likely to cause a scarcity of certain raw materials, which will further raise prices for consumers. Governments, businesses, local communities, and individuals are working hard to tackle existing issues and prevent the climate crisis from worsening. This includes the development of new technologies to manage carbon emissions and updates and improvements to infrastructure systems.

EXAMPLES OF ECONOMICS IN AMERICAN HISTORY

Economics have always played a part in American history, from its earliest Indigenous settlements to today. The first peoples living in North America had traditional economies based on bartering. As Europeans settled on the continent, they introduced and adopted a regulated money economy and concepts such as credit and the free enterprise system.

Native American Economies

Native Americans developed the first economies in American history. The economies were largely traditional and relied on bartering for goods. Some Native nations formed formal trade agreements that involved the use of money. In lieu of coins and paper notes, Native Americans used a variety of items and goods to standardize exchanges. One of the best-known examples is wampum, or stringed

beads or shells, used by Eastern Woodlands peoples. Native traders also used furs, maize, tobacco, and wheat. Wampum, like minted money, was subject to inflation. Not all wampum was created equal, as some Native nations were highly skilled at producing beads. The arrival of European settlers disrupted traditional mediums of exchange. In some instances, white settlers produced their own wampum, causing its value to decline. Native Americans later began trading using European and eventually American currency.

European Exploration and Colonization

European exploration and settlement of the Americas was largely motivated by economic gain. Initially, explorers sought a maritime route to Asia to trade for spices—one that was quicker than traveling overland or around Africa. After Christopher Columbus's arrival in the Caribbean, countries such as England and the Netherlands sent explorers in search of the Northwest Passage. While maritime routes to Asia were never actually discovered, European empires used the resources of the Americas to their advantage. Their colonies provided an abundance of raw materials and opened new markets for European trade.

The Spanish Mission System

The Spanish were the first to colonize the Americas, beginning with the arrival of Christopher Columbus in 1492 CE. The first Spanish mission was established in 1565 in Saint Augustine, Florida. The mission system was a way to both spread Catholicism to Native peoples and develop self-sustaining local economies.

Spanish missions began as small settlements that featured a church, housing for clergy and various other buildings, a central courtyard, and an exterior wall for protection. Priests and Spanish officials developed farmland around the mission and mined for metals like copper, iron, and tin.

Because the missions were tasked with converting Native people to Catholicism, they were generally built near existing Native populations. Pacification played a large role in attracting converts. The missions provided food, Spanish-made goods, and vocational training to Native people. The life of a convert was difficult and generally one of servitude. In many instances, the missions enslaved local populations to farm the mission land and work in the mines.

British Colonial Policy

British exploration and colonization of the Americas, like that of the Spanish, was motivated by economic gain. At this time, European empires embraced mercantilism, an economic system driven by the accumulation of wealth at the expense of other countries. Countries focused on increasing their exports and reducing their imports as a way to amass wealth in the form of gold and silver. The acquisition of colonies was one way to achieve these ends. The colonies, rich in natural resources, shipped raw materials to England, where English artisans turned them into finished goods that could be sold back to the colonies and to other countries.

Jamestown, the first English colony in North America, was established by the Virginia Company in 1607. The Virginia Company was a joint-stock company, a precursor to the modern corporation. The goal of the company was to make money from raw materials found in the colony. The settlers did not find the precious metals and gemstones they expected, and a lack of preparedness, famine, and disease thwarted early productivity. Trade with the local Powhatan tribe, strict measures under the leadership

of John Smith, and the eventual introduction of tobacco as a cash crop by John Rolfe made the colony profitable.

Industrialization

Industrialization had a massive impact on the American economy. The First Industrial Revolution began in Great Britain in the late 1700s with mechanization of Britain's textile industry. Over time, production in all industries became increasingly mechanized, and factories relied on water power. This reduced the need for skilled laborers while increasing output and lowering costs to producers and consumers.

The United States, as did other countries, underwent a Second Industrial Revolution starting in the mid-1800s. The Second Industrial Revolution expanded on earlier technologies and relied on new sources of power to not only mass-produce consumer goods but also more quickly and efficiently produce iron and steel. The Second Industrial Revolution coincided with the massive expansion of transportation. Railroads connected regional markets and markets across the country, lowering the cost and time required to ship goods and people from one place to another.

Industrialization had numerous effects on the United States. It created a culture of mass consumption. Cheaply produced goods were now widely available to many Americans. At the same time, industrialization reshaped American society. People living in rural areas and immigrants flocked to cities in search of factory jobs, causing an increase in urbanization. Women increasingly worked outside of the home, which changed the nature of family life.

Industrialization also gave rise to unions. Factory conditions were often dangerous. Workers toiled for long hours for little pay, and they lacked benefits like paid sick leave and unemployment insurance. Unions formed to advocate for workers' rights and frequently used collective bargaining and strikes to improve working and living conditions.

Globalization

Globalization describes the interconnectedness of countries around the world through trade and technology. Globalization is not a new concept. Societies and cultures have experienced varying degrees of interconnectedness throughout world history. For example, the Silk Road connected peoples from China to Europe starting in 130 BCE.

Globalization was accelerated by the arrival of European settlers in the Americas, beginning with Columbus's voyage in 1492 CE. The resulting Columbian Exchange of the 1500s and 1600s was characterized by the massive exchange of plants, animals, goods, and people between the Eastern and Western Hemispheres in a way the world had never seen before. Colonization and imperialization further connected peoples and economies around the world as European countries sought raw materials and new markets for their goods.

Globalization has evolved and changed over time and is largely impacted by technology. The digital age has made it possible for people to communicate instantaneously with others around the world. Technology also facilitates the movement of people and goods and the exchange of services.

Today, the United States is part of the global economy, the worldwide system of trade and economic activity. Countries in the global economy are interdependent, meaning that actions and events that affect the world affect the United States, too. Actions or events in the United States also affect the rest of the global community. One example is the Great Recession of the early 2000s: the collapse of the U.S. housing market affected all of the United States' trading partners.