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ABSTRACT

Educators should assess the economics curricula in order to determine whether the latest and most accurate views of economic life in the United States and the world are taught to high school students. Economic literacy involves knowing and applying fundamental economic theories in order to make rational decisions about the use of limited resources. This digest considers the nature of economic literacy through an exploration of the basic economic concepts that students should learn, a definition of economics as a way of thinking, and desired outcomes of education for economic literacy. Fundamental themes of economics education should include scarcity, productive resources, economic systems, exchange, incentives, the market place, and managing the economy. An economic way of thinking refers to decision-making as the central skill of economic literacy and emphasizes the application of this skill to decision-making. While the ability to conduct objective and reasoned analysis of economic issues is the most important benefit of economic literacy education, students also learn to understand the economic dimensions of issues, to evaluate the consequences of economic decisions, and to participate intelligently in the political process. (JHP)

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According to Alfred Marshall, the famous British economist, "Economics is a study of mankind in the ordinary business of life." Indeed, we encounter economics as workers, consumers, savers, and citizens, and we make countless personal and societal decisions of great practical importance every day in response to various kinds of economic issues and problems.

Economics is both a body of knowledge and a way of thinking about certain phenomena. Educators generally agree about the basic ideas in economics every high school graduate should know, and they tend to agree that the discipline of economics is dynamic; the economy and our knowledge of it continue to evolve. Thus, educators must continually assess the economics curriculum in terms of the current status of the academic discipline in order to provide students with the latest and soundest view of economic life in the United States and the world.[1]

Economic literacy involves knowing and applying fundamental economic ideas to make rational decisions about the use of limited resources. This ERIC Digest treats the nature of economic literacy through discussion of (1) basic ideas in economics that every culturally literate person should know, (2) economics as a way of thinking, and (3) likely outcomes of education for economic literacy.

What are the fundamental themes of economics? The general themes of economics are presented below in a very introductory manner. For a more detailed description see TEACHING ECONOMICS: CONTENT AND STRATEGIES (Banazak and Brennen 1982) or MASTER CURRICULUM GUIDE IN ECONOMICS: A FRAMEWORK FOR TEACHING THE BASIC CONCEPTS. (Saunders et al. 1984).

- *Scarcity is the imbalance of wants and resources.* We live on a finite world that has limited resources, but our wants for products (goods) and services are unlimited. Scarcity requires the making of choices between alternate uses of productive resources. When making choices, it is important to consider all alternative uses of the resources. The choice ultimately is made between the most desirable and the next most desirable alternative which can be considered the value of the decision measured in lost opportunity (the opportunity cost).

- *Productive resources, also called factors of production, include everything used to create products and services.* The three types are human (labor), natural (land), and capital. Human resources are all the workers and their abilities. Efficient use requires workers to specialize in what they do best. Entrepreneurs, people who take risk associated with starting a new business or producing a new product or service, are an important type of human resource. Natural resources are all the basic gifts of nature whether above, on, or below the surface of the earth. They are either renewable, such as trees, or non-renewable, like petroleum. Capital resources are the resources that have been created by human effort and savings, to be used to produce products or services. Capital resources include tools, machines, and factories. The creation of capital resources requires deferring to the future the consumption of some desired products or services.

- *Economic systems are the organized ways by which people determine how to allocate scarce productive resources.* Traditional, command, and market are the three basic types of economic systems. Each economic system answers at least three basic questions: (1) What to produce?, (2) How to produce?, and (3) How to distribute output? In the traditional system, economic decisions are formulated by the customs of the society. Economic decisions in the command system, are made by decision-makers, usually government employees. In the market system, economic decisions are made by individuals and institutions, guided by their own self-interest, in a free market process with a minimum of government intervention. The market economy also requires competition among producers, awareness of product availability and alternatives, private ownership, and a limited role for government in the economy. In the real world, all economic systems are mixtures of the three.

- *Exchange involves trading resources, products, or services.* When exchange is voluntary, both sides believe they have gained. Exchange is fundamental, permitting specialization in production and resulting in more efficient use of resources. Exchange may be direct, as in barter, or involve the use of money. Money facilitates trade by providing a standard medium of exchange. Money also provides a uniform means to measure and compare the worth of things, a store of value, and a standard of deferred payment.

- *Economic incentives influence human behavior by offering financial rewards which allow larger claims for products and services.* We all attempt to make the best choices to maximize our output and satisfactions, thus promoting our self-interest. Consumers seek to maximize their satisfaction, workers their wages, producers their profits, and investors their return. Understanding and manipulating incentives is a powerful way to influence the economy.

- *The market is the principle feature of a market economy.* The market is not a place where buyers and producers meet, but a process through which the decisions of individuals and businesses are used to answer the basic economic questions listed above. The forces of supply and demand interact, seeking an equilibrium, and register the decision through the price.

- *Managing the economy is an attempt to achieve socially determined goals.* In the United States, the goals are to promote economic freedom, economic efficiency, economic equity, economic security, full employment, economic growth, and price stability. Managing a modern complex economy is a difficult task, not easily achieved. Measurement problems and the changing dynamics of the economy add to the difficulty. Further, the goals are sometimes in conflict, such as full employment and stable prices. Fiscal and monetary policy are used to manage the market economy. Fiscal policy refers to the taxing, borrowing, and spending decisions made by the federal government which can influence the total (aggregate) demand and supply of products and services in the economy. Monetary policy refers to the control of interest rates and money supply to influence the amount of money in circulation and thus affect the demand for products and services.

What is the economic way of thinking? The economic way of thinking refers to a system for making decisions. Since economics deals with choices about the use of limited resources for unlimited wants, decision-making is the central skill of economics. Economic decision-making is a logical, reasoned approach using economic concepts and generalizations.

• *Decision-Making Model.* Economic decisions involve six steps.

1. Clearly identify the details of the decision situation. What choice is involved? What are the details?

2. Determine what personal or social goal(s) are to be attained. What are you trying to achieve by the decision? Which goals are of highest priority?

3. Identify all the alternatives. What possible choices could be made?

4. Consider each alternative and its consequences. What are the likely costs, benefits, and outcomes of each alternative?

5. Decide on the best alternative for reaching the desired goal(s). Which alternative is most likely to reach the goals? Which alternative is most feasible? Which have the least undesirable effects?

6. Review and evaluate the decision. Did it attain the desired goal? Did predicted consequences occur? Did it maximize benefits that could be obtained from the resources used?

• *Factors of Economic Decision Making.* The following economic relationships are useful as we make economic decisions: (1) trade-offs, (2) law of supply and demand, (3) marginal analysis, (4) cost/benefit analysis, and (5) short-term and long-term effects.

1. Decisions about the use of productive resources seldom become mutually exclusive. We do not choose between guns or butter, but between relative amounts of guns and butter or various production possibilities. In making decisions, it is imperative to consider the trade-offs between alternative uses of the resources.

2. The laws of supply and demand state relationships between quantities demanded by consumers and quantities producers are willing to supply at a given time, assuming all other conditions remain constant. The law of demand states that as price increases, quantity demanded decreases, and conversely, if price decreases, quantity demanded increases. The law of supply states that, as price rises, producers are willing to increase the quantity supplied. As price falls, the quantity producers are willing to supply also falls. The tendency in the economy is for the quantity demanded and quantity supplied to move toward an equilibrium price at which the quantity producers are willing to produce is identical with the quantity consumers are willing to buy.

3. Economic decision makers attempt to make choices that maximize output and satisfaction. Marginal analysis is used to determine the value of producing or consuming an additional unit of the same good or service. The law of diminishing marginal utility teaches that additional quantities of goods yield successively smaller increments of satisfaction. Marginal productivity shows additional output received by adding an additional unit of resources as input.

4. Every decision has costs and benefits. By examining the costs associated with each decision in relation to the expected benefits, we attempt to make choices that maximize benefits for the least cost.

5. When examining the consequences of a decision it is important to consider the long-term, as well as, the immediate effect. A choice that has a less desired short-term effect may be the better choice if it has a much more desirable long-term effect.

What are the likely outcomes of education for economic literacy? Since economics is the study of decision-making about the use of productive resources, the central benefit of education for economic literacy should be development of the ability to conduct objective, reasoned analysis of economic issues. These economic issues and decisions are private and public; they pertain to daily personal concerns and to matters of broad economic policy.

Informed decision-making requires acquisition and use of knowledge of economic concepts and generalizations. This knowledge allows citizens to understand the economic dimensions of issues. It permits them to determine and evaluate both the short-term and long-term consequences of potential economic decisions. Economically literate citizens will be more intelligent readers and listeners. This will enable them to participate intelligently in the political process and to be less easily misled by a demagogue. Finally, economically literate citizens will be life-long learners, capable of incorporating new economic knowledge into their existing knowledge.

Economically literate citizens, because they possess an understanding of economic generalizations and concepts, will enjoy a more complete understanding of their world, be better able to make reasoned decisions, and be more fully in control of their economic future.

References and ERIC Resources

Following is a list of resources, including references used to prepare the Digest. Those items followed by an ED number are in the ERIC system and are available in microfiche and /or paper copies from the ERIC Document Reproduction Service (EDRS). For information about prices, write EDRS, 3900 Wheeler Avenue, Alexandria, Virginia 22304. Entries followed by an EJ number are annotated monthly in CIJE (*Current Index to Journals in Education*) which is available in libraries containing ERIC collections. EJ documents are not available through EDRS; however, they can be located in the journal section of most libraries using the bibliographic information provided below.

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