Glossary

A

Absolute advantage
When one country can use fewer resources to produce a good compared to another country; when a country is more productive compared to another country

Adaptive expectations
The theory that people look at past experience and gradually adapt their beliefs and behavior as circumstances change

Adjustable-rate mortgage (ARM)
A loan whose interest rate varies with market interest rates and is used by a borrower to purchase a home

Aggregate demand (AD)
The amount of total spending on domestic goods and services in an economy

Aggregate demand (*AD*) curve
Curve that shows the total spending on domestic goods and services at each price level

Aggregate demand/aggregate supply (AD/AS) model
A model that shows what determines total supply and total demand for an economy and how total demand and total supply interact at the macroeconomic level

Aggregate production function
The process by which an economy as a whole turns economic inputs—such as human capital, physical capital, and technology—into output, measured as GDP per capita

Aggregate supply (AS)
The total quantity of output firms will produce and sell

Aggregate supply (*AS*) curve
Curve showing the total quantity of output that firms will produce and sell at each price level

Allocative efficiency
When the mix of goods produced represents the mix that society most desires; the quantity where the marginal benefit to society of one more unit equals the marginal cost

Antidumping laws
Laws that block imports sold below the cost of production and impose tariffs that increase the price of these imports to reflect their cost of production

Appreciating
When a currency is worth more in terms of other currencies; also called strengthening

Arbitrage
The process of buying and selling currencies across different markets to take advantage of different interest or exchange rates

Asset
Item of value that a firm or an individual owns

Asset-liability time mismatch
Customers can withdraw a bank's liabilities in the short term but repay its assets in the long term

Automatic stabilizers
Programs that are already laws that stimulate aggregate demand in a recession and hold down aggregate demand in a potentially inflationary boom

B

Balanced budget
When federal government spending and taxes received are equal

Balance of trade (trade balance)
The gap between exports and imports

Balance sheet
An accounting tool that lists assets and liabilities

Bank capital
A bank's net worth

Bank run
When depositors rush to the bank to withdraw their deposits because they fear the bank may become insolvent

Barter
Trading one good or service for another without using money

Base year
Arbitrary year whose value is 100

Basic quantity equation of money
money supply × velocity = nominal GDP = price level × real GDP

Basket of goods and services
A hypothetical group of different items, with specified quantities of each one, meant to represent a typical set of consumer purchases and used as a basis for calculating how the price level changes over time

Budget constraint (or **budget line**)
Shows the possible combinations of two goods that are affordable given a consumer's limited income

Budget deficit
When the federal government spends more money than it receives in taxes in a given year

Budget surplus
When the federal government receives more money in taxes than it spends in a given year

Business cycle
The economy's movement from peak to trough and trough to peak

C

Capital deepening
An increase in the average level of physical and/or human capital per person by society

Central bank
An institution that conducts a country's monetary policy and regulates its banking system

Certificate of deposit (CD)
Account that the depositor has committed to leaving in the bank for a certain period of time in exchange for a higher interest rate; also called time deposit

Ceteris paribus
Other things being equal

Checkable deposit
Deposit in a bank that is available by making a cash withdrawal or writing a check; also called a demand deposit

Circular flow diagram
A diagram that views the economy as consisting of households and firms interacting in a goods and services market and a labor market

Coins and currency in circulation
The coins and bills that circulate in an economy that are not held by the U.S. Treasury, at the Federal Reserve Bank, or in bank vaults

Command economy
An economy where economic decisions are passed down from government authority and where the government owns the resources

Commodity-backed currencies
Dollar bills or other currencies with values backed up by gold or another commodity

Commodity money
An item that is used as money but also has value from its use as something other than money

Common market
Economic agreement between countries to allow free trade in goods, services, labor, and financial capital between members while having a common external trade policy

Comparative advantage
When a country can produce a good at a lower cost in terms of other goods; or, when a country has a lower opportunity cost of production

Complements
Goods that are often used together so that consumption of one good tends to enhance consumption of the other

Compound growth rate
The rate of growth when multiplied by a base that includes past GDP growth

Constant unitary elasticity
When a given percent change in price leads to an equal percentage change in quantity demanded or supplied

Consumer price index (CPI)
A measure of inflation that U.S. government statisticians calculate based on the price level from a fixed basket of goods and services that represents the average consumer's purchases

Consumer surplus
The extra benefit consumers receive from buying a good or service, measured by what the individuals would have been willing to pay minus the amount that they actually paid

Contractionary fiscal policy
Tax increases and/or cuts in government spending designed to decrease aggregate demand and reduce inflationary pressures

Contractionary monetary policy
Monetary policy that reduces the supply of money and the quantity of loans

Contractual rights
Based on property rights, contractual rights allow individuals to enter into agreements with others regarding the use of their property and seek recourse through the legal system in case of noncompliance

Convergence
A pattern in which countries with low per capita incomes grow faster than countries with high per capita incomes, with the possibility of the low-income countries eventually catching up with the high-income countries

Converging economy
Economy of a country that has demonstrated the ability to catch up to the technology leaders by investing in both physical and human capital

Coordination argument
Downward wage and price flexibility requires perfect information about the level of lower wages acceptable to workers

Core inflation index
A measure of inflation typically calculated by excluding volatile economic variables, such as food and energy, from the CPI to better measure the underlying and persistent trend in long-term prices

Corporate income tax
A tax businesses pay based on their profits

Cost-of-living adjustments (COLAs)
A contractual provision that wage increases will keep up with inflation

Countercyclical
Moving in the opposite direction of the business cycle of economic downturns and upswings

Credit card
A card to make purchases with that gives an instruction to immediately transfer money from the credit card company's checking account to the seller; at the end of the month, the user owes the money to the credit card company; a short-term loan

Cross-price elasticity of demand
The percentage change in the quantity of Good A that is demanded as a result of a percentage change in the price of Good B

Crowding out
When federal spending and borrowing cause interest rates to rise and business investment to fall

Current account balance
A broad measure of the balance of trade that includes trade of goods and services, international flows of income, and foreign aid

Cyclically adjusted budget (or **standardized employment budget**)
The budget deficit or surplus in any given year, adjusted for what it would have been if the economy was producing at potential GDP

Cyclical unemployment
The variation in unemployment that results from the economy moving from expansion to recession or from recession to expansion

D

Deadweight loss
The loss in social surplus that occurs when a market produces an inefficient quantity

Debit card
A card that lets the person make purchases, and the financial institution immediately deducts the cost from that person's checking account

Deflation
Negative inflation, which occurs when most of the prices in the economy are falling

Demand
The relationship between price and the quantity demanded of a certain good or service

Demand curve
A graphic representation of the relationship between price and quantity demanded of a certain good or service, with quantity on the horizontal axis and price on the vertical axis

Demand schedule
A table that shows a range of prices for a certain good or service and the quantity demanded at each price

Deposit insurance
Insurance system that makes sure depositors in a bank do not lose their money, at least up to a certain amount, if the bank goes bankrupt

Depreciating
When a currency is worth less in terms of other currencies; also called weakening

Depreciation
The process by which capital ages and loses value

Depression
An especially lengthy and deep recession

Derived demand
Demand for labor is based on demand for the good or service that is produced

Discount rate
The interest rate charged by the central bank on the loans that it gives to other commercial banks

Discouraged workers
Those who have stopped looking for employment due to the lack of suitable positions available

Discretionary fiscal policy
When the government passes a new law that explicitly changes tax or spending levels

Disposable income
Income after taxes

Disruptive market change
Innovative new product or production technology which disrupts the status quo in a market, leading the innovators to earn more income and profits and the other firms to lose income and profits, unless they can come up with their own innovations

Diversification
Making loans or investments with a variety of firms to reduce the risk of being adversely affected by events at one or a few firms

Division of labor
The way in which different workers divide required tasks to produce a good or service

Dollarize
When a foreign country uses the U.S. dollar as its currency

Double coincidence of wants
A situation in which two people each want some good or service that the other person can provide

Double counting
Counting output more than once as it travels through the production stages

Dumping
Selling internationally traded goods below their cost of production

Durable goods
Long-lasting goods, like cars and computers

E

Economics
The study of how humans make choices under conditions of scarcity

Economic surplus
See *social surplus*

Economic union
Economic agreement between countries to allow free trade between members, a common external trade policy, and coordinated monetary and fiscal policies

Economies of scale
The long-run average cost of producing output decreases as total output increases

Efficiency
When the economy is getting as much benefit as possible from its scarce resources and all the possible gains from trade have been achieved

Elastic demand
When the elasticity of demand is greater than one, indicating a high responsiveness of quantity demanded or supplied to changes in price

Elasticity
An economic concept that measures responsiveness of one variable to changes in another variable

Elasticity of savings
The percentage change in the quantity of savings divided by the percentage change in interest rates

Elastic supply
When the elasticity of supply is greater than one, indicating a high responsiveness of quantity demanded or supplied to changes in price

Employed
Those who are currently working for pay

Employment cost index
A measure of inflation based on wages paid in the labor market

Equilibrium
The situation where quantity demanded is equal to quantity supplied; the combination of price and quantity where there is no economic pressure from surpluses or shortages that would cause price or quantity to change

Equilibrium in the labor market
Price and quantity where quantity demanded of labor equals the quantity supplied of labor

Equilibrium price
The price where quantity demanded is equal to quantity supplied

Equilibrium quantity
The quantity at which quantity demanded and quantity supplied are equal for a certain price level

Excess demand
At the existing price, the quantity demanded exceeds the quantity supplied; also called a shortage

Excess reserves
Reserves banks hold that exceed the legally mandated limit

Excess supply
At the existing price, quantity supplied exceeds the quantity demanded; also called a surplus

Exchange rate
The value of one currency in terms of another currency

Excise tax
A tax on a particular good, such as gasoline, tobacco, or alcohol

Expansionary fiscal policy
Tax cuts and/or increases in government spending designed to stimulate aggregate demand and move the economy out of a recession

Expansionary monetary policy
Monetary policy that increases the supply of money and the quantity of loans

Expenditure multiplier
Keynesian concept that asserts that a change in autonomous spending causes a more-than-proportionate change in real GDP

Exports
Domestically produced goods and services that a country sells abroad

F

Factors of production
The resources such as labor, materials, and machinery that are used to produce goods and services; also called inputs

Federal funds rate
The interest rate at which one bank lends funds to another bank overnight

Fiat money
Money that has no intrinsic value but is declared by a government to be the country's legal tender

Final goods and services
Goods at the end of the chain of production that are sold for consumption, investment, government, and trade purposes

Financial capital
Money supplied by savers and demanded by borrowers in financial markets

Financial intermediary
An institution, like a bank, that receives money from savers and provides funds to borrowers

Fiscal policy
Economic policies that involve government spending and taxes

Floating exchange rate
An exchange rate determined by the foreign exchange market

Foreign direct investment (FDI)
Purchasing more than 10% of a firm or starting a new enterprise in another country

Foreign exchange market
The market in which people use one currency to buy another currency

Free trade
International trade that is not subject to tariffs, quotas, or any regulations

Free trade agreement
Economic agreement between countries to allow free trade between members

Frictional unemployment
Unemployment that occurs when workers are between jobs

Full-employment GDP
When the economy is producing at its potential and unemployment is at the natural rate of unemployment

G

Gains from trade
The additional output a country can consume as a result of specialization and trade

GDP deflator
A price index measuring the average prices of all final goods and services included in the economy

GDP per capita
GDP divided by population

Globalization
The trend in which buying and selling in markets have increasingly crossed national borders

Goods and services market
A market in which firms are sellers of what they produce and households are buyers

Gross domestic product (GDP)
The value of all final goods and services produced within a country in a given year

Gross national product (GNP)
The value of all final goods and services produced by a country's residents, wherever located, in a given year

H

Hard peg
An exchange rate policy in which the central bank sets a fixed and unchanging value for the exchange rate

Hedge
Using a financial transaction as protection against an investment risk

Human capital
The accumulated skills and education of workers

Human capital per person
The amount of knowledge, experience, or skills available to help a person produce a good or service

Hyperinflation
An outburst of high inflation that often occurs when economies shift from a controlled economy to a market-oriented economy

I

Implementation lag
The time it takes for fiscal policy funds to be dispersed to the appropriate agencies to implement the programs

Import quotas
Numerical limits on the quantity of products that a country can import

Imports
Goods and services that are produced abroad and purchased domestically

Indexed
A wage, price, or interest rate that is automatically adjusted for inflation

Index number
A unit-free number derived from the price level over a number of years, which makes computing inflation rates easier; has a value around 100

Individual income tax
A tax based on all forms of income received by individuals

Inelastic demand
When the elasticity of demand is less than one, indicating that a one percent increase in price paid by the consumer leads to less than a one percent change in purchases (and vice versa); this indicates a low responsiveness by consumers to price changes

Inelastic supply
When the elasticity of supply is less than one, indicating that a one percent increase in price paid to the firm will result in a less than one percent increase in production by the firm; this indicates a low responsiveness of the firm to price increases (and vice versa if prices drop)

Infant industry argument
Argument to protect new industries by blocking imports for a limited time to give the infant industry time to mature before it starts competing on equal terms in the global economy

Inferior good
A good in which the quantity demanded falls as income rises, and in which quantity demanded rises as income falls; a good that has a negative income elasticity of demand

Infinite elasticity
The extremely elastic situation of demand or supply where quantity changes by an infinite amount in response to any change in price; horizontal in appearance

Inflation
A sustained increase in the overall level of prices

Inflationary gap
Equilibrium at an output level above potential GDP

Inflation targeting
A rule that the central bank is required to focus only on keeping inflation low

Infrastructure
A component of physical capital, such as roads and rail systems

Innovation
Putting advances in knowledge to work in a new product or service

Inputs
The resources such as labor, materials, and machinery that are used to produce goods and services; also called factors of production

Interest rate
The "price" of borrowing in the financial market; a rate of return on an investment

Intermediate goods
Goods that are part of production for other goods

Intermediate zone
Portion of the *SRAS* curve where GDP is below potential but not so far below as in the Keynesian zone; the curve is upward-sloping but not vertical

International capital flows
Flow of financial capital across national boundaries, either as portfolio or direct investment

International price index
A measure of inflation based on the price of merchandise that is exported or imported

Intertemporal choices
Choices that are made over time

Intertemporal decision-making
Making decisions over time

Intra-industry trade
International trade of goods within the same industry

Invention
Advances in knowledge

Inventories
Goods that have been produced but not yet sold

Invisible hand
Adam Smith's concept that individuals' self-interested behavior can lead to positive social outcomes

K

Keynesian zone
Portion of the *SRAS* curve where GDP is far below potential and the curve is flat

Keynes' law
Demand creates its own supply

L

Labor force
Those who are employed and those who are unemployed but actively looking for work

Labor force participation rate
The percentage of adults in an economy who are either employed or who are unemployed and looking for a job

Labor market
The market in which households sell their labor as workers to business firms or other employers

Labor productivity
The value of what is produced per worker or per hour worked

Law of demand
The common relationship that a higher price leads to a lower quantity demanded of a certain good or service and a lower price leads to a higher quantity demanded, while all other variables are held constant

Law of diminishing marginal utility
The common pattern that each marginal unit of a good consumed provides less additional utility than the previous unit

Law of diminishing returns
As additional increments of resources are added to producing a good or service, the marginal benefit from those additional increments will decline

Law of supply
The common relationship that a higher price leads to a greater quantity supplied and a lower price leads to a lower quantity supplied, while all other variables are held constant

Legislative lag
The time it takes to get a fiscal policy bill passed

Lender of last resort
An institution that provides short-term emergency loans to banks and other financial institutions during financial crises

Liability
Any debt or amount that a firm or an individual owes

Liquidity
How quickly a financial asset can be converted into a medium of exchange used to buy a good or service

Living wage
A wage that will ensure a reasonable standard of living

Long-run aggregate supply (*LRAS*) curve
Vertical line at potential GDP showing no relationship between the price level for output and real GDP in the long run

Loose monetary policy
See *expansionary monetary policy*

M

M1 money supply
A narrow definition of the money supply that includes currency in circulation, demand deposits, and traveler's checks

M2 money supply
A definition of the money supply that includes everything in M1 but also adds savings deposits, money market funds, and certificates of deposit

Macroeconomic externality
Occurs when what happens at the macro level is different from and inferior to what happens at the micro level

Macroeconomics
The branch of economics that focuses on broad issues such as growth, unemployment, inflation, and the trade balance

Marginal analysis
The examination of decisions on the margin, meaning a little more or a little less from the status quo

Marginal tax rates
A tax due on all yearly income

Market
Interaction between potential buyers and sellers; a combination of demand and supply

Market economy
An economy where economic decisions are decentralized, private individuals own resources, and businesses supply goods and services based on demand

Medium of exchange
Whatever is widely accepted as a method of payment between buyer and seller

Menu costs
Costs firms face when changing prices

Merchandise trade balance
A balance of trade that only measures trade of physical goods

Merged currency
When a nation chooses to use another nation's currency as its own

Microeconomics
The branch of economics that focuses on actions of particular agents within the economy, like households, workers, and business firms

Minimum wage
A price floor that makes it illegal for an employer to pay employees less than a certain hourly rate

Model
See *theory*

Monetary policy
Economic policies that involve altering the level of interest rates, the availability of credit in the economy, and the extent of borrowing

Money market fund
The deposits of many investors that are pooled together and invested in safe assets, like short-term government bonds

Money multiplier
Determines how many times a loan will be multiplied as it is spent in the economy and then redeposited in other banks; the reciprocal of the reserve requirement

N

National debt
The total accumulated amount that the government has borrowed over time and not yet paid back

National income
All income to businesses and people that is generated in GDP

National interest argument
The argument that a nation should not depend too heavily on another nation for key imports

National saving
The total of a nation's domestic saving by households and companies (private saving), and the government (public saving)

National saving and investment identity
The quantity of financial capital supplied in an economy must equal the quantity of financial capital demanded

Natural rate of unemployment
The baseline level of unemployment that occurs even if the economy is producing at potential (or full-employment) GDP

Neoclassical economists
Economists who generally emphasize the importance of aggregate supply in determining the size of the economy in the long run

Neoclassical perspective
The philosophy that, in the long run, the business cycle will fluctuate around the potential, or full-employment, level of output

Neoclassical zone
Portion of the *SRAS* curve where GDP is at or near potential output and the curve is steep

Net national product (NNP)
GNP minus the value of physical capital that is worn out or reduced in value because of aging

Net worth
The excess of the value of assets over and above the amount of the liabilities; total assets minus total liabilities

Nominal value
An economic statistic measure with actual prices

Nondurable goods
Short-lived goods, like food and clothing

Nontariff barriers
Ways a nation can draw up rules, regulations, inspections, and paperwork to make it more costly or difficult to import products

Normal good
A good in which the quantity demanded rises as income rises, and in which quantity demanded falls as income falls; a good that has a positive income elasticity of demand

Normative statement
Statement which describes how the world should be

O

Open market operations
In the U.S., refers to the Federal Reserve selling or buying Treasury bonds to influence the quantity of money and the level of interest rates

Opportunity cost
Measures cost by what is given up/forfeited in exchange; measures the value of the forgone alternative

Opportunity set
All possible combinations of consumption an individual can afford given the prices of goods and the individual's income

Out of the labor force
Those who are not working and not looking for work

P

Payment system
Helps an economy exchange goods and services for money or other financial assets

Payroll tax
A tax based on pay received from employers; in the U.S., it provides funds for Social Security and Medicare

Peak
The highest point of the economy before a recession begins

Perfect elasticity
See *infinite elasticity*

Perfect inelasticity
See *zero elasticity*

Phillips curve
Curve that shows the tradeoff between unemployment and inflation

Physical capital
The factories and equipment that firms use in production; this includes infrastructure

Physical capital per person
The amount and kind of machinery and equipment available to help a person produce a good or service

Portfolio investment
An investment in another country that is purely financial and does not involve any management responsibility

Positive statement
Statement which describes the world as it is

Potential GDP
The maximum quantity that an economy can produce given full employment of its existing levels of labor, physical capital, technology, and institutions

Price
What a buyer pays for a unit of the specific good or service

Price ceiling
A legal maximum price

Price control
Government laws to regulate prices instead of letting market forces determine prices

Price elasticity
The relationship between the percent change in price resulting in a corresponding percentage change in the quantity demanded or supplied

Price elasticity of demand
Percentage change in the quantity demanded of a good or service divided by the percentage change in price; calculated as an absolute value

Price elasticity of supply
Percentage change in the quantity supplied divided by the percentage change in price; calculated as an absolute value

Price floor
A legal minimum price

Private enterprise
System where private individuals or groups of private individuals own and operate the means of production (resources and businesses)

Producer price index (PPI)
A measure of inflation based on the prices paid for supplies and inputs by producers of goods and services

Producer surplus
The extra benefit producers receive from selling a good or service, measured by the price the producer actually received minus the price the producer would have been willing to accept

Production function
A mathematical equation that tells how much output a firm can produce with given amounts of the inputs

Production possibilities frontier (PPF)
A diagram that shows the productively efficient combinations of two products that an economy can produce given the resources it has available

Productive efficiency
When it is impossible to produce more of one good (or service) without decreasing the quantity produced of another good (or service)

Progressive tax
A tax system in which the rich pay a higher percentage of their income in taxes, rather than a higher absolute amount

Property rights
The legal rights of ownership on which others are not allowed to infringe upon without paying compensation

Proportional tax
A tax that is a flat percentage of income earned, regardless of level of income

Protectionism
Government policies to reduce or block imports

Purchasing power parity (PPP)
The exchange rate that equalizes the prices of internationally traded goods across countries

Q

Quality/new goods bias
How inflation calculated over time using a fixed basket of goods tends to overstate the true rise in the cost of living because it does not take into account improvements in the quality of existing goods or the invention of new goods

Quantitative easing (QE)
The purchase of long-term government and private mortgage-backed securities by central banks to make credit available in hopes of stimulating aggregate demand

Quantity demanded
The total number of units of a good or service consumers are willing to purchase at a given price

Quantity supplied
The total number of units of a good or service producers are willing to sell at a given price

R

Race to the bottom
When production locates in countries with the lowest environmental (or other) standards, putting pressure on all countries to reduce their environmental standards

Rational expectations
The theory that people form the most accurate possible expectations about the future that they can, using all information available to them

Real interest rate
The nominal interest rate minus the inflation rate

Real value
An economic statistic measure adjusted for inflation

Recession
A significant decline in real GDP

Recessionary gap
Equilibrium at an output level below potential GDP

Recognition lag
The time it takes to determine that a recession has occurred

Regressive tax
A tax in which people with higher incomes pay a smaller share of their income in taxes

Reserve requirement
The percentage amount of its total deposits that a bank is legally obligated to either hold as cash in its vault or on deposit with the central bank

Reserves
Funds that a bank keeps on hand and does not loan out or invest in bonds

Ricardian equivalence
The theory that rational private households might shift their saving to offset government saving or borrowing

Rule of law
The process of enacting laws that protect individual and entity rights to use their property as they see fit; laws must be clear, public, fair, enforced, and applicable to all members of society

S

Savings deposit
Bank account you cannot withdraw money from by writing a check but can withdraw the money at a bank or transfer it easily to a checking account

Say's law
Supply creates its own demand

Scarcity
When human wants for goods and services exceed the available supply

Services
The most common jobs in a modern economy, where no tangible good is produced; jobs in education, health care, and legal and financial services

Shift in demand
When a change in some economic factor (other than price) causes a different quantity to be demanded at every price

Shift in supply
When a change in some economic factor (other than price) causes a different quantity to be supplied at every price

Shortage
At the existing price, the quantity demanded exceeds the quantity supplied; also called excess demand

Short-run aggregate supply (*SRAS*) curve
Positive short-run relationship between the price level for output and real GDP, holding prices of inputs fixed

Slope
The ratio of rise to run; shows the opportunity cost of choosing one good over another

Smart card
A card that stores a certain amount of money, which can be used to make purchases

Social surplus
The sum of consumer surplus and producer surplus; also called economic surplus or total surplus

Soft peg
An exchange rate policy in which the government usually allows the foreign exchange market to determine the exchange rate, but the central bank may intervene if the currency is moving rapidly in one direction

Special economic zone (SEZ)
An area of a country, usually with access to a port, where the government does not tax trade

Specialization
When workers or firms focus on particular tasks for which they are well-suited within the overall production process

Splitting up the value chain
Many of the different stages of producing a good happen in different geographic locations

Stagflation
When an economy experiences high unemployment and inflation at the same time

Standard of deferred payment
If money is usable to make purchases today, it must also be acceptable to make purchases today that will be paid in the future

Standard of living
A measurement that includes all elements that affect people's well-being, whether or not they are bought and sold in the market

Store of value
Something that serves as a way of preserving economic value that one can spend or consume in the future

Structural unemployment
Unemployment that occurs because workers lack skills valued by the labor market

Structures
A supply-side component of GDP that includes homes, office buildings, shopping malls, and factories

Substitute
A good that can replace another to some extent, so that greater consumption of one good can mean less of the other

Substitution bias
How an inflation rate calculated over time using a fixed basket of goods tends to overstate the true rise in the cost of living because it does not take into account that people can substitute away from goods whose prices rise considerably

Sunk costs
Costs made in the past that cannot be recovered

Supply
The relationship between price and the quantity supplied of a certain good or service

Supply curve
A graphic representation of the relationship between price and quantity supplied, with quantity on the horizontal axis and price on the vertical axis

Supply schedule
A table that shows a range of prices for a good or service and the quantity supplied at each price

Surplus
At the existing price, quantity supplied exceeds the quantity demanded; also called excess supply

T

T-account
A balance sheet with a two-column format and a *T* shape formed by the vertical line down the middle and the horizontal line under the column headings, "Assets" and "Liabilities"

Tariffs
Taxes that governments place on imported goods and services

Tax incidence
Manner in which the tax burden is divided between buyers and sellers

Technological change
A combination of invention and innovation

Technology
All the advances that make existing inputs produce more, higher quality, different, or new products

Theory
A representation of an object or situation that is simplified while including enough of the key features to help us understand the object or situation

Tight monetary policy
See *contractionary monetary policy*

Total surplus
See *social surplus*

Trade balance
The difference between exports and imports

Trade deficit
When a country's exports are less than its imports

Trade secrets
Methods of production kept secret by the producing firm

Trade surplus
When a country's exports are greater than its imports

Traditional economy
Typically an agricultural economy where things are done the same as they have always been done

Transaction costs
The costs associated with finding a lender or borrower for money

Trough
The lowest point of a recession before a recovery begins

Twin deficits
Deficits that occur when a country is running both a trade and budget deficit

U

Underemployed
Those who are trained or skilled for one type of work but are working in a lower-paying job or one that does not utilize their skills

Underground economy
A market where the buyers and sellers make transactions in violation of one or more government regulations

Unemployed
Those who are out of work and actively looking for a job

Unilateral transfers
One-way payments that governments, private entities, or individuals make that they send abroad with nothing received in return

Unitary elasticity
When the calculated elasticity is equal to one, indicating that a change in the price of the good or service results in a proportional change in the quantity demanded or supplied

Unit of account
The common way in which we measure market values in an economy

Usury laws
Laws that impose an upper limit on the interest rate that lenders can charge

Utility
The satisfaction, usefulness, or value one obtains from consuming goods and services

V

Value chain
How a good is produced in stages

Velocity
The speed with which money circulates through the economy; calculated as nominal GDP divided by the money supply

W

Wage
The price in the labor market; also called salary

Wage elasticity of labor supply
The percentage change in hours worked divided by the percentage change in wages

Z

Zero elasticity
The highly inelastic case of demand or supply in which a percentage change in price, no matter how large, results in zero change in the quantity; vertical in appearance