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

Accounting profit
Total revenues minus explicit costs, cincluding depreciation

Acquisition
When one firm purchases another

Actual rate of return
The total rate of return, including capital gains and interest paid on an investment at the end of a time period

Additional external cost
Additional costs incurred by third parties outside the production process when a unit of output is produced

Adverse selection
When groups with inherently higher risks than the average person seek out insurance, thus straining the insurance system

Affirmative action
Active efforts by government or businesses that give special rights to minorities in hiring, promotion, or access to education to make up for past discrimination

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

Antitrust laws
Laws that give government the power to block certain mergers and, in some cases, break up large firms into smaller ones

Asymmetric information
A situation where the seller or the buyer has more information than the other regarding the quality of the item for sale

Average profit
Profit divided by the quantity of output produced; also known as profit margin

Average total cost
Total cost divided by the quantity of output

Average variable cost
Variable cost divided by the quantity of output

B

Barriers to entry
The legal, technological, or market forces that may discourage or prevent potential competitors from entering a market

Behavioral economics
A branch of economics that seeks to enrich the understanding of decision-making by integrating the insights of psychology and by investigating how given dollar amounts can mean different things to individuals depending on the situation

Bilateral monopoly
A labor market with a monopsony on the demand side and a union on the supply side

Bond
A financial contract through which a borrower like a corporation, city, state, or federal government agrees to repay the amount that it borrowed and also a rate of interest over a period of time in the future

Bondholder
Someone who owns bonds and receives the interest payments

Bond yield
The rate of return a bond is expected to pay at the time of purchase

Break-even point
Level of output where the marginal cost curve intersects the average cost curve at the minimum point of the *AC*; if the price is at this point, the firm is earning zero economic profits

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

Bundling
A situation in which multiple products are sold as one

C

Capital gain
A financial gain from buying an asset, like a share of stock or a house, and later selling it at a higher price

Cartel
A group of firms that collude to produce the monopoly output and sell at the monopoly price

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

Checking account
A bank account that typically pays little or no interest gives easy access to money, either by writing a check or by using a debit card

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

Coinsurance
When an insurance policyholder pays a percentage of a loss, and the insurance company pays the remaining cost

Collateral
Something valuable—often property or equipment—that a lender would have a right to seize and sell if the borrower does not repay the loan

Collective bargaining
Negotiations between unions and a firm or firms

Collusion
When firms act together to reduce output and keep prices high

Command-and-control regulation
Laws that specify allowable quantities of pollution and that also may detail which pollution-control technologies one must use

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

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

Common resources
Goods that are nonexcludable and rivalrous in consumption

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 interest
An interest rate calculation on the principal plus the accumulated interest

Concentration ratio
An early tool to measure the degree of monopoly power in an industry; measures what share of the total sales in the industry are accounted for by the largest firms, typically the top four to eight firms

Constant-cost industry
As demand increases, the cost of production for firms stays the same

Constant returns to scale
Expanding all inputs proportionately does not change the average cost of production

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

Consumer equilibrium
Point on the budget line where the consumer gets the most satisfaction; this occurs when the ratio of the prices of goods is equal to the ratio of the marginal utilities

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

Copayment
When an insurance policyholder must pay a small amount for each service before insurance covers the rest

Copyright
A form of legal protection to prevent copying, for commercial purposes, original works of authorship, including books and music

Corporate bond
A bond issued by firms that wish to borrow money

Corporate governance
The name economists give to the institutions that are supposed to watch over top executives in companies that shareholders own

Corporation
A business owned by shareholders who have limited liability for the company's debt yet a share of the company's profits; may be private or public and may or may not have publicly traded stock

Cosigner
Another person or firm who legally pledges to repay some or all of the money on a loan if the original borrower does not

Cost-plus regulation
When regulators permit a regulated firm to cover its costs and to make a normal level of profit

Coupon rate
The interest rate paid on a bond; can be annual or semiannual

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

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

Decreasing-cost industry
As demand increases, the cost of production for firms decreases

Deductible
An amount that the insurance policyholders must pay out of their own pocket before the insurance coverage pays anything

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

Deregulation
Removing government controls over setting prices and quantities in certain industries

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

Differentiated product
A product that consumers perceive as distinctive in some way

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

Discrimination
Actions based on the belief that members of a certain group or groups are in some way inferior solely because of a factor such as race, gender, or religion

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

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

Dividend
A direct payment from a firm to its shareholders

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

Dominant strategy
The strategy an individual (or firm) will pursue regardless of the other individual's (or firm's) decision

Dumping
Selling internationally traded goods below their cost of production

Duopoly
An oligopoly with only two firms

E

Economic profit
Total revenues minus total costs (explicit plus implicit costs)

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

Effective income tax
Percentage of total taxes paid divided by total income

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

Entry
The long-run process of firms entering an industry in response to industry profits

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

Equity
The monetary value a homeowner would have after selling the house and repaying any outstanding bank loans used to buy the house

Estate and gift tax
A type of tax that is placed on people who leave large amounts of assets and/or gifts to the next generation

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

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

Exclusive dealing
An agreement that a dealer will sell products from only one manufacturer

Exit
The long-run process of firms reducing production and shutting down in response to industry losses

Expected rate of return
How much a project or investment is expected to return to the investor, either in future interest payments, capital gains, or increased profitability

Explicit costs
Out-of-pocket costs for a firm, for example, payments for wages and salaries, rent, or materials

Exports
Domestically produced goods and services that a country sells abroad

Externality
A market exchange that affects a third party who is outside, or external, to the exchange; sometimes called a spillover

F

Face value
The amount that the bond issuer or borrower agrees to pay the investor

Factor payments
What the firm pays for using the factors of production

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

Fee-for-service
When medical care providers are paid according to the services they provide

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

Firm
An organization that combines inputs of labor, capital, land, and raw or finished component materials to produce outputs

First rule of labor markets
An employer will never pay a worker more than the value of the worker's marginal productivity to the firm

Fiscal policy
Economic policies that involve government spending and taxes

Fixed cost
Cost of the fixed inputs; expenditure that a firm must make before production starts and that does not change regardless of the production level

Fixed inputs
Factors of production that can't be easily increased or decreased in a short period of time

Four-firm concentration ratio
The percentage of the total sales in the industry that are accounted for by the largest four firms

Free rider
A person who wants others to pay for the public good and then plans to use the good themselves; if many people act as free riders, the public good may never be provided

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

Fungible
The idea that units of a good—such as dollars, ounces of gold, or barrels of oil—are capable of mutual substitution with each other and carry equal value to the individual

G

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

Game theory
A branch of mathematics that economists use to analyze situations in which players must make decisions and then receive payoffs based on what decisions the other players make

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

H

Health maintenance organization (HMO)
An organization that provides health care and is paid a fixed amount per person enrolled in the plan, regardless of how many services are provided

Herfindahl-Hirschman Index (HHI)
Approach to measuring market concentration by adding the square of the market share of each firm in the industry

High-yield bonds
Bonds that offer relatively high interest rates to compensate for their relatively high chance of default; also called junk bonds

I

Imperfect information
A situation where either the buyer, seller, or both are uncertain about the qualities of what they are buying and selling

Imperfectly competitive
Firms and organizations that fall between the extremes of monopoly and perfect competition

Implicit costs
Opportunity cost of resources already owned by the firm and used in business, for example, expanding a factory onto land already owned

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

Income
A flow of money received, often measured on a monthly or an annual basis

Income effect
A higher price means that, in effect, the buying power of income has been reduced, even though actual income has not changed; always happens simultaneously with a substitution effect

Income inequality
When one group receives a disproportionate share of total income or wealth than others

Increasing-cost industry
As demand increases, the cost of production for firms increases

Index fund
A mutual fund that seeks only to mimic the market's overall performance

Indifference curve
A graphic representation of the combinations of two goods that provide an equal level of utility for an individual

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

Initial public offering (IPO)
The first sale of shares of stock by a firm to outside investors

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

Insurance
Method of protecting a person from financial loss, whereby policyholders make regular payments to an insurance entity; the insurance firm then remunerates a group member who suffers significant financial damage from an event covered by the policy

Intellectual property
The body of law including patents, trademarks, copyrights, and trade secret law that protects the right of inventors to produce and sell their inventions

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

International externalities
Externalities that cross national borders and that a single nation acting alone cannot resolve

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

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

J

Junk bonds
See *high-yield bonds*

K

Kinked demand curve
A perceived demand curve that arises when competing oligopoly firms commit to match price cuts but not price increases

L

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

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 productivity
General rule that as a firm employs more labor, eventually the amount of additional output produced declines

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

Legal monopoly
Legal prohibitions against competition, such as regulated monopolies and intellectual property protection

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

Logrolling
The situation in which groups of legislators all agree to vote for a package of otherwise unrelated laws that they individually favor

Long run
Period of time during which all of a firm's inputs are variable

Long-run average cost (*LRAC*) curve
Shows the lowest possible average cost of production, allowing all the inputs to production to vary so that the firm is choosing its production technology

Long-run equilibrium
Where all firms earn zero economic profits producing the output level where $P = MR = MC$ and $P = AC$

Lorenz curve
A graph that compares the cumulative income actually received to a perfectly equal distribution of income; it shows the share of population on the horizontal axis and the cumulative percentage of total income received on the vertical axis

M

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 cost
The additional cost of producing one more unit; mathematically, $MC = \Delta TC/\Delta Q$

Marginal cost of labor
The additional cost to a firm when it hires one more worker

Marginal product of labor
The change in a firm's output when it employees more labor; mathematically, $MP = \Delta TP/\Delta L$

Marginal rate of subsitution
The rate at which an individual is willing to trade a good for another to keep utility constant; the slope of the indifference curve at a given point

Marginal revenue
The additional revenue gained from selling one more unit

Marginal utility
The additional utility provided by one additional unit of consumption

Marginal utility per dollar
The additional satisfaction gained from purchasing a good given the price of the product; *MU*/price

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

Marketable permit program
A permit that allows a firm to emit a certain amount of pollution; firms with more permits than pollution can sell the remaining permits to other firms

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

Market failure
When the market on its own does not allocate resources efficiently in a way that balances social costs and benefits; externalities are one example of a market failure

Market share
The percentage of total sales a firm has in a market

Market structure
The conditions in an industry, such as number of sellers, how easy or difficult it is for a new firm to enter, and the types of products that are sold

Maturity date
The date that a borrower must repay a bond by

Median voter theory
The theory that politicians will try to match policies to what pleases the median voter preferences

Merger
When two formerly separate firms combine to become a single firm

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

Minimum resale price maintenance agreement
An agreement that requires a dealer who buys from a manufacturer to sell for at least a certain minimum price

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-back guarantee
A promise that the seller will refund the buyer's money under certain conditions

Monopolistic competition
Many firms competing to sell similar but differentiated products

Monopoly
A situation in which one firm produces all of the output in a market

Monopsony
A labor market where there is only one employer

Moral hazard
When people have insurance against a certain event, they are less likely to guard against that event occurring

Municipal bond
A bond issued by cities that wish to borrow money

Mutual funds
Funds that buy a range of stocks or bonds from different companies, thus allowing an investor an easy way to diversify

N

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

Natural monopoly
Economic conditions in an industry, such as economies of scale or control of a critical resource, that limit effective competition

Near-poor
Those who have incomes just above the poverty line

Negative externality
Harmful spillovers to a third party or parties who did not purchase the good or service that provided the externalities

Nonexcludable
When it is costly or impossible to exclude someone from using the good and thus hard to charge for it

Nonrival
Even when one person uses the good, others can also use it

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

Occupational license
Licenses issued by government agencies, which indicate that a worker has completed a certain type of education or passed a certain test

Oligopoly
When a few large firms have all or most of the sales in an industry

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

P

Partnership
A company that is unincorporated and owned by two or more people who are jointly liable for anything done by the business

Patent
A government rule that gives the inventor the exclusive legal right to make, use, or sell an invention for a limited time

Perfect competition
Type of market were each firm faces many competitors that sell identical products

Perfect elasticity
See *infinite elasticity*

Perfect inelasticity
See *zero elasticity*

Perfectly competitive labor market
A labor market where neither suppliers of labor nor demanders of labor have any market power; thus, an employer can hire all the workers they would like at the going market wage

Pollution charge
A tax imposed on the quantity of pollution that a firm emits; also called a pollution tax

Pork-barrel spending
Spending that benefits mainly a single political district

Positive externality
Beneficial spillovers to a third party or parties who did not purchase the good or service that provided the externalities; also called external benefits

Positive statement
Statement which describes the world as it is

Poverty
The situation of being below a certain level of income one needs for a basic standard of living

Poverty line
The specific amount of income one requires for a basic standard of living

Poverty rate
Percentage of the population living below the poverty line

Poverty trap
A problem that arises from antipoverty programs set up so that government benefits decline substantially as people earn more income; as a result, working provides little financial gain

Predatory pricing
When an existing firm uses sharp but temporary price cuts to discourage new competition

Premium
Payment made to an insurance company

Present value
A bond's current price at a given time

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

Price cap regulation
When the regulator sets a price that a firm cannot exceed over the next few years

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

Price taker
A firm in a perfectly competitive market that must take the prevailing market price as given

Prisoner's dilemma
A game in which the gains from cooperation are larger than the rewards from pursuing self-interest

Private benefits
The benefits a person who consumes a good or service receives or the benefits a company is able to capture from a new product or process

Private company
A firm owned by the people who run it on a day-to-day basis

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

Private rates of return
When the estimated rates of return go primarily to an individual; for example, earning interest on a savings account

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

Product differentiation
Any action that firms do to make consumers think their products are different from their competitors'

Production
The process of combining inputs to produce outputs, ideally of a value greater than the value of the inputs

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

Production technologies
Alternative methods of combining inputs to produce output

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

Protectionism
Government policies to reduce or block imports

Public company
A firm that has sold stock to the public, which investors can then buy and sell

Public good
Good that is nonexcludable and nonrival and, thus, is difficult for market producers to sell to individual consumers

Q

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

Quintile
Dividing a group into fifths, a method economists often use to look at distribution of income

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 ignorance
The theory that rational people will not vote if the costs of becoming informed and voting are too high or because they know their vote will not be decisive in the election

Redistribution
Taking income from those with higher incomes and providing income to those with lower incomes

Regulatory capture
When the supposedly regulated firms end up playing a large role in setting the regulations that they will follow; as a result, they "capture" the people, usually through the promise of a job in that "regulated" industry once their term in government has ended

Restrictive practices
Practices that reduce competition but do not involve outright agreements between firms to raise prices or to reduce the quantity produced

Risk
A measure of the uncertainty of a project's profitability

Risk group
A group that shares roughly the same risks of an adverse event occurring

S

Safety net
The group of government programs that provide assistance to the poor and the near-poor

Savings account
A bank account that pays an interest rate; withdrawing money typically requires a trip to the bank or an automatic teller machine

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

Service contract
The buyer pays an extra amount, and the seller agrees to fix anything specified in the contract that goes wrong for a set time period

Shareholders
People who own shares of stock in a firm

Shares
A firm's stock, divided into individual portions

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
Period of time during which at least one or more of the firm's inputs is fixed

Short-run average cost (*SRAC*) curve
The average total cost curve in the short term; shows the total of the average fixed costs and the average variable costs

Shutdown point
Level of output where the marginal cost curve intersects the average variable cost curve at the minimum point of the *AVC*; if the price is below this point, the firm should shut down immediately

Simple interest
An interest rate calculation only on the principal amount

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

Social benefits
The sum of private benefits and positive externalities

Social costs
Costs that include both the private costs incurred by firms and also additional costs incurred by third parties outside the production process, like costs of pollution

Social rate of return
When the estimated rates of return go primarily to society; for example, providing free education

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

Sole proprietorship
A company that is unincorporated, with one owner who is legally liable for anything done by the business

Special interest groups
Groups that are small in number relative to the nation but are well-organized and, thus, exert a disproportionate effect on political outcomes

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

Spillover
See *externality*

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

State bond
A bond issued by a state that wishes to borrow money

Stock
Represents partial ownership of a specific company

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

Substitution effect
When a price changes, consumers have an incentive to consume less of the good with a relatively higher price and more of the good with a relatively lower price; always happens simultaneously with an income effect

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

Tariffs
Taxes that governments place on imported goods and services

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

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

Total cost
The sum of fixed and variable costs of production

Total product
Synonym for a firm's output

Total revenue
Income from selling a firm's product; defined as price times quantity sold

Total surplus
See *social surplus*

Trademark
An identifying symbol or name for a particular good and can only be used by the firm that registered that trademark

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

Treasury bond
A bond issued by the federal government through the U.S. Department of the Treasury

Tying sales
A situation where a customer is allowed to buy a product only if the customer also buys another product

U

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

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

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

Variable cost

The cost of production that increases with the quantity produced; the cost of the variable inputs

Variable inputs

Factors of production that a firm can easily increase or decrease in a short period of time

Venture capital

Financial investments in new companies that are still relatively small in size but that have potential to grow substantially

Voting cycle

The situation in which a majority prefers A over B, A over C, and C over A

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

Warranty

A promise to fix or replace the good for a certain period of time

Wealth

The sum of the value of all assets, including money in bank accounts, financial investments, a pension fund, and the value of a home

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