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1978 Volume III: 20th Century American History and Literature

The American Economy

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Section I - Content Objectives

The goal of this unit is to have students gain a basic understanding of how our economic system works. This will be accomplished by posing three vital questions and attempting to answer them. More specific objectives may develop from student inquiry and should be encouraged. The three questions are:

1. Why is our system sometimes called a “free enterprise” system, and sometimes a “mixed economy”?
2. How are goods produced and marketed?
3. What are the functions of money and banking?

Our economic system is based in part on free enterprise. Citizens’ needs will be met by companies that enjoy four basic freedoms in business: 1) a free market in which a buyer may choose any product; 2) free competition and quality; 3) an individual’s freedom to own private property and build up capital; 4) freedom to earn a profit. All these freedoms come with risks and all businessmen also have the freedom to fail.

The American economy is also called a “mixed” economy because of the active role our government plays. Students will be exposed to some of the ways our government interacts in the economy.

The various forms of business organization will be introduced for the students’ consideration. The differences between a single proprietorship, a partnership, and a corporation will be discussed. The organization, financing, and management of corporations will be discussed in some detail. There will also be a discussion of preferred stocks, common stocks, and bonds. This section should provide the students with an understanding of American business. Projects on local businesses and the stock market fit nicely into this section.

Here may be an opportune time to compare the Soviet Union’s “command economy” and our free enterprise system. The two systems can be judged on the basis of the freedom of the worker, the citizens’ standard of living, and the country’s productive capacity. A film or description of the life of a Soviet worker should be of particular interest.

Producing and marketing goods leads us into the four factors of production: land, labor, capital, and management. Each one will be explained and its importance stressed. Terms such as “gross income,” “net income” and “profit” will be analyzed. The students will also divide workers into various classifications.

Producing goods is only part of our economic picture. Students will learn that we are a nation of mass production. We will discuss the various modes of power being used and becoming available for such production. The auto industry may serve as a good example of modern mass production.

The effectiveness of mass production industries depends upon an efficient method of getting their goods to market. Students will be able to identify various methods of transportation used in mass marketing. Mass marketing is made possible by the organization of a system involving manufacturers, wholesalers, transportation experts, and retailers. With this in mind we can explore some factors that have helped to make for more efficient retailing, such as supermarkets, self-service, standard packaging, and the one-price system. The students will, through personal observation, note that within this system of mass marketing, the small retailer can still prosper by offering convenient, special, or personalized service.

Mass marketing presents consumers with an overwhelming variety of products and services. At this stage the students will explore their roles as consumers. 1) Through class projects students will learn where and when to buy, and how to study labels and judge price and quality of products. They will become aware of organizations that aid consumers, and discuss the pros and cons of charge accounts and installment plans. The emphasis will be placed on becoming a wiser shopper.

This unit will conclude with a section on money and banking. 2) We will outline the common features of money, and discuss mediums of exchange and measures of value. The importance of checkbook money will be illustrated as well as the flow, or circulation, of currency.

After a brief introduction to the background of banking, a distinction will be made between state and national banks and between savings and commercial banks. Possible projects may include applying for and renewing a loan. The lesson will end with a consideration of the Federal Reserve System and its effects on banking and credit.

Section II - Our Free Economy

Freedom in American society is not limited to our nation’s form of government. Our nation’s economy, or business system, is based on freedom, too. We are free to choose the products and services we buy, the jobs we seek, and the businesses we start, and to decide where and when we sell our products and the price we sell them for. There is nobody, in our free economy, who decides how many cars, houses, shirts, shoes, or comic books will be produced. Every business firm is free to make its own decisions about what to produce and what price to charge for its products.

In our free economy goods of all kinds are produced to satisfy the needs of the people. It is also possible for a business to produce a product, and then “sell” people the idea that they need their product. Our system works because each person is free to make nearly all of his own economic decisions. Citizens’ needs will be met by companies that enjoy four basic freedoms.

1. Our economy is based on a *free market* . In a free market people may buy any product from any seller. In our economy there is usually more than one producer or service. This permits the consumer, one who buys or uses products and services, to look for the best price or even purchase a substitute article. Because we have this freedom our choices determine what will be produced and in what quantity. Indirectly, we also help decide a product's price. How do we do this?
2. We do this by the force of *competition* . In the United States, businesses are free to compete with one another for customers. Each business tries to convince us that its product or service will best satisfy our wants or needs. The force of competition leads businesses to find ways of operating more efficiently and effectively. Free competition enables the consumer to show which product s/he favors every time s/he makes a purchase. It can also be a means of keeping the price of products from rising too high. As you can see, the buyer is free to decide what price s/he will pay for any product.

Free competition also exists for jobs and for workers. A worker may work anywhere s/he can get a job. Once employed s/he is free to stay or look for another one. Business firms also compete to hire the best workers. For this reason skilled workers who meet a business' needs are paid often good wages. So important is competition to the American economic system the government often acts to promote it.

3. In our economic system we are free to own *private property* . Every American is free to buy land, machines, tools, and other equipment to produce goods or services. All Americans are also free to sell their private property as they wish. Land, property, machines, or money used to provide services or produce goods is called "capital." The American system is sometimes called "capitalism," or a "capitalistic system," because capital is private property and owned by individuals. A plumber's tools are capital; they cost money and are used to produce things people want. The machines used by the auto makers to produce cars are also capital. Both the auto manufacturer and the plumber are capitalists. A capitalist is for our purposes any person who has money invested in a business firm which produces goods or services. Anyone can be a capitalist.
4. One key to our free enterprise system is the freedom to earn a *profit.* The hope of a profit motivates people to invest and businesses to take risks. Profits are realized when income from sales are greater than the total cost of producing the goods or services.

Any realistic view of our free enterprise system must take into account the role of government. It is a role that has grown greatly in recent times. Today few businesses are completely free in their operations. To some degree their activities are regulated by the government. Many of the goods and services we enjoy are provided directly by the government.

America has a mixed economy. In it owners of private business and government workers try to satisfy our economic desires. Both private people and government play important roles.

One important role is that of a regulator of business. The government fills this role to protect all Americans. In 1906, for example, Congress passed the Federal Food and Drug Act. This law prohibited the use of harmful chemicals or drugs in medicine or food. To prevent monopolies Congress has passed the Sherman Antitrust Act (1890), and the Clayton Act (1914), and created the Federal Trade Commission (1914), thereby preventing such activities as price fixing and regulating deceptive practices. A complete monopoly exists if there is only one seller, who therefore may set his own price. The combined action of several companies who control the supply of a product also results in a monopoly when no competitor can enter the field. The exceptions are called "legal" monopolies. These legal monopolies, such as the telephone company, bus system, and gas and electric companies, are regulated by our government to make certain they provide good service at reasonable rates. In the years since 1914, Congress has set up agencies to regulate the sale of stocks and bonds (SEC), airline traffic (CAB), and a number of other economic activities.

State and local governments also engage in business regulation. Banks are inspected by state banking commissions. Restaurants are inspected by local health officers. There are local building codes that set standards for home and building construction. Labor laws regulate age, kinds of work, hours, safety regulations, and so on.

The government does not just regulate business; it is a business. The government employs thousands of workers. It also produces goods and services.

The national government produces electricity. It does this at government-built projects such as the Tennessee Valley Authority and the Hoover Dam on the Colorado River. The national government is also in the banking business. The Small Business Administration loans money to small businesses, while the Export-Import Bank lends money to foreign countries. The government is in the insurance business. It offers an insurance service through the Federal Deposit Insurance Corporation (FDIC). The FDIC insures bank accounts against bank failure. The national government also runs a park system, schools (West Point, the Coast Guard Academy, etc.), and veterans' hospitals.

On the state and local levels, governments run public schools, colleges, and universities. These governments also run parks, bus lines, and hospitals.

Still another governmental role is found in aid given to business. This is done in two ways, through taxes and government spending, and through regulation of our money supply.

The government receives money in the form of taxes. It spends money on a seemingly endless variety of things. It pays us for work being done now (salaries), for past work (pensions), and for work to be done in the future (grants).

Most American businesses fall into one of three general forms of organization: single proprietorship, partnership, and corporation.

A large number of small businesses and farms are controlled by a single owner or family. Here the owner is his or her own boss. S/he makes all the decisions, raises the finances, and gets all the profits. A single proprietorship is easy to set up and run. Its growth, however, is limited to the assets and credits of the owner. The owner is responsible for all losses and business debts. This is known as "unlimited liability." Any property or income of the owner, not just the business, may be legally seized by the firm's creditors if the owner fails to pay them.

Individual proprietorships may turn into partnerships. A person may wish to expand but lack the capital or the "know-how" to make the business a success. In this case the single proprietor may have to form a partnership. A partnership is an agreement between two or more persons to share the profits and responsibilities of a business. Each partner owns a share of the business, but not always in equal parts. The profits are divided according to the agreement made when the partnership was formed. Each partner is responsible for all financial obligations of the business. That is, each partner has unlimited liability. Partnership is a form of business often used by such professions as law, medicine, and architecture.

The corporation is by far the most important form of business organization in America today. A corporation is a business concern which may be large or small and may have many owners, but is operated as an individual firm. It is considered to be legally distinct from its owner; in the eyes of the law a corporation is a “person.” Business is transacted in the name of the corporation, which can sue and be sued in court. As a legal institution, the corporation receives its right to operate from the state government. The state issues the certificate or charter to do business, which describes the nature of the business that may be carried on.

Corporations raise money by selling “stock,” or shares of ownership. Each share represents a part ownership in the corporation. The corporation’s profits are divided to pay stockholders and are called “dividends.” It is important to know that many corporations issue two kinds of stock, preferred and common. Both kinds of stock usually can be bought and sold by anyone who wants to invest in the corporation.

Owners of preferred stock take less risk. As long as the company makes a profit they will receive a fixed dividend. They are paid their dividends before common stockholders receive their dividends. Preferred stockholders do not usually have a vote in the corporation.

Common stockholders take a greater risk. They get no guarantee of a dividend. They are paid dividends only after both preferred stockholders and bond owners are paid. There are, however, three main advantages in owning common stock. If the company’s profits are high, the owner may receive dividends greater than those given to owners of preferred stock. If profits are high, the price of the stock usually will increase. The owner may then sell for a profit. Finally, common stockholders have a vote in electing the board of directors who run the company, and also vote on some company policies. Each stockholder gets as many votes as s/he has shares of stock.

Even after selling preferred and common stock some corporations need to raise more money. The most common method of borrowing money is to issue bonds. A bond is a promise by the firm to repay at the end of a stated number of years the full amount of money loaned to the firm. Interest, at a fixed rate, will be paid to the owner whether or not the corporation is making a profit. The company must pay this interest before it pays dividends to shareholders. If the corporation is not able to pay back the full amount of the bond on the due date, or if the interest is not paid when due, the bondholders may take over the business. The corporation’s assets may be sold to meet these payments. Bond holders do not share in profits or have any voting rights in the corporation. They do have the safest investment.

The corporation has several advantages over individual proprietorships or partnerships. The corporation provides the means of raising adequate funds. Each stockholder has limited liability; s/he can lose no more than s/he has invested. Stockholders do not have to become involved in managing the firm. This is done by professional directors and managers. Shares of stocks are transferable, and may be sold or given away without changing the status of the firm. The actual selling is done by professional brokers. Corporations also have a perpetual life. They do not have to close or reorganize when one of the owners dies or withdraws. The major disadvantage of the corporation is that it must pay high federal income taxes on profits. When the remaining profits are paid to stockholders as dividends, those receiving the dividends then must pay tax on them. This is a case of double taxation.

Is big business a blessing or a curse? The answer is of course both. In manufacturing, large businesses can use specialized machinery economically. Large firms are able to use by-products to a greater extent than small firms. They may have workers who have specialized skill or training. Research is carried on by large firms.

Large firms buy materials at lower rates and can pass the savings on to the consumers. They also have an advantage in advertising their products. All these factors help to increase sales. However, big business does have some disadvantages. Big business is impersonal. Workers may feel that their work is not appreciated or that they are not needed. They may lose their sense of accomplishment or pride of workmanship. Mass production and automation have greatly improved our lives but they also create uncertainties. Automation is seen by many workers as a threat to their job security. In some industries, size is not necessarily an advantage. If a few firms get too large they may get a disproportionate control of output. Critics of big business and monopoly say that when a few firms gain control of the supply of a product, artificially high prices will result.

At this point it might be fruitful briefly to compare our economic system with that of the Soviet Union.

The Soviet Union has established a command economy. In this type of system, the government completely controls, or commands, the entire economy. The Communist government owns all businesses, and almost all of the capital, tools and equipment, and land used for production. The government dictates what jobs people must take, where they work, their wages, and the prices of goods. The government, not the market, decides what goods and services are to be provided. The Soviet Union is rich in natural resources. The way these resources are used is also determined by the government. Almost all farmland is owned and managed by the government, and organized into farms called “collectives.” Farm workers are not permitted the same job mobility as Americans. On the collectives bonuses are awarded to squads who exceed their quota. Small plots of land may be given to individuals, but they must work the plots themselves.

Americans enjoy a much higher standard of living. The average Soviet worker earns about 1/7 of what his American counterpart earns. Americans can own a great variety of goods including land, capital, businesses, and tools of production.

There are “rich” men in this classless society. They are always high-ranking members of the Communist party. Artists, performers, scientists, and business managers also fare better than the average worker.

The basic difference between the two systems lies in the orientation of their goals. The American system is designed to serve and meet the needs of the consumers. By contrast, the Soviet economy is established to serve the needs of the government, not the people.

Section III - How Goods Are Marketed and Produced

In economic terms the word “production” takes on new meaning. Production is the creation of economic value—making goods or services to satisfy human wants. There are four factors or necessary elements in every product or service: land, capital, management, and labor.

Land includes all of the natural resources used in our economy. Nature has given us a limited or fixed amount of natural resources and raw materials so wise use is essential. The United States uses more of the world’s land resources than any other nation.

Production requires capital. Capital is money used to buy tools and equipment to make goods or provide services. Capital goods are machines, tools, buildings and the like, used in production. These are a form of wealth. Capital goods are used to make more of the things that people want. Each business must utilize its capital wisely. Decisions about how to use capital are made by each company's management.

The men who run a business are called managers, or "management." They are the people who make the decisions which determine whether the business will succeed. But when management makes decisions it must take risks. Risks are taken with the hope of increasing profits.

The total amount of money received from sales of goods or services is called gross income. Out of this gross income the business pays for all of its production costs. The amount left over is called net income. Most businesses will probably set aside part of this net income for future needs. The rest of this net income is called "profits." Profit is what is left after all obligations have been met.

All businesses need workers. "Labor" includes all the people engaged in the production process except the enterpriser himself. The various types of work that people bring to the process lead us to classify workers in seven general categories. *Professional* workers include most educated workers, such as teachers, nurses, lawyers, and doctors. *Self-employed workers* work for themselves, in small businesses or on farms, for example. *Service workers* provide us with services (barbers, waiters, tailors). *Clerical workers* work in offices as secretaries, typists, or clerks. *Skilled workers* are those whose jobs require long training and special skills, such as plumbers, electricians, or carpenters. *Semiskilled workers* need only a short training period: they include bus drivers, telephone operators, and some factory workers. *Unskilled workers* perform jobs requiring little or no training, such as delivery or freight handling.

One reason that the American economy is prosperous is the use of methods of mass production. Mass production means producing huge amounts of goods rapidly. There are three basic elements necessary for producing goods by mass production: machine tools, standardized parts, and division of labor.

Machine tools or machinery is carefully built to turn out parts that are exactly alike. The identical parts are called standard parts. Because they are identical they are interchangeable, making for easier assembly and repair. Each part becomes a replacement part for others. The principle of division of labor provides each worker with the opportunity to become a specialist at his job. The use of machinery, standardized parts, and division of labor led to increased production early in America's history. But production was slow at first, because machinery was operated by muscle power. A new search for a more efficient source of power began.

Americans first turned to water power. The force of falling water was used to operate machines. Many factories were located near streams. Dams were constructed and water wheels used to supply power. The next significant change took place when a Scottish engineer, James Watt, developed a practical steam engine. Soon steam power replaced water power, as the principle source of power during the 1800's. By the 1900's several new sources of power had been developed. The internal combustion engine, operated by exploding gasoline fumes, was used for automobiles and small machines. But none of these sources of power was suitable for mass production.

Early in the 1900's electricity began to be used widely. At first it was used to light homes and streets. Today it is used in an ever-increasing variety of ways. Electricity is the source of power used in almost all American businesses and factories.

American businesses, industries, and scientists are still seeking new sources of power. Many experts believe that atomic energy is the answer to our energy needs. Atomic energy now powers ships and submarines. Atomic energy plants are being constructed and used to produce electricity. Nuclear energy is not problem-free, since it raises the questions of public safety in case of accidents and what to do with radioactive waste.

As these issues are dealt with and as the cost of atomic energy decreases, its use will probably increase.

Scientists are exploring still other sources of power. One of the greatest sources is the power of the sun. Solar energy is already being used to produce electricity and supplement hot water heating systems. At the present time, solar energy is too expensive for the average consumer. But as technology progresses, solar energy may become more practical.

The production of goods is only part of our economic picture. Mass production depends upon efficiently transporting goods to markets. Moving goods to market is called marketing. Early in our history, Americans realized the importance of a good transportation system. They utilized lakes and rives, and built canals, roads, and railroads.

Railroads served as our main form of transporting people and freight for over fifty years. American railroads operate on standard gauge tracks. This means that they are all the same distance apart, enabling any car from any company to use them. Today, the railroads must compete with other forms of transportation. In passenger transportation buses, automobiles, and airlines have grown rapidly and have overtaken railroads. By the late 1960's planes traveled over 90 billion passenger miles annually, intercity buses over 844 million miles, and trains only 170 million miles.

Railroads have also lost the lead in transporting freight, both raw materials and finished products. In 1926 railroads carried 3/4 of all freight business. Now they carry less than half. More and more products are being moved by large trailer trucks. Goods that require rapid transportation use air freight. Many large bulky goods are using river, lake, and ocean shipping in increasing numbers. Today railroads, with government aid, are trying to make a comeback.

America's primary means of transportation is the automobile. The car is the leading form of passenger travel and usually transports goods on the last part of their trip, from the store to our homes. Roads have changed our the years from dirt to asphalt and concrete superhighways. We now have over 3.5 million miles of roads. Some of our new roads are toll roads, roads on which drivers must pay a fee. Other new roads are limited access superhighways. "Limited access" means that drivers can enter the highway only at certain points. This eliminates cross traffic and allows traffic to flow with more regularity. Our Interstate Highway System makes use of such highways. These roads are very expensive, costing on an average more than $1 million per mile. The federal government pays 90% and the states pay the remaining 10%.

Mass production depends upon mass marketing. Mass marketing means moving huge amounts of goods efficiently so as to reach millions of people.

Products usually pass through several hands before reaching the consumer. Businesses sell the products to a wholesaler or a middleman. The retail stores sell the products directly to the public. Often the cost of marketing a product is equal to or greater than the cost of producing the product.

Mass marketing is well illustrated by the supermarket, a large retail store selling hundreds of different kinds of food. Customers push carts around aisles making their own selections. Usually there is no clerk to wait on them. After the selections are made the customer brings the items to the cashier to pay for them. This kind of marketing is called "self-service." It is an efficient way to sell goods. Customers can choose exactly what they want. It is cheaper because it requires fewer clerks.

Standard packaging of items also increases the efficiency of self-service markets. "Standard packing" means that goods are sent from the factory already wrapped. Items are wrapped, weighed, and put in attractively labeled packages.

The one-price system is also a feature of our mass marketing. Under this system the selling price is put on each item before it is offered for sale. First used over 100 years ago in Philadelphia by Wanamaker's Department store, this practice eliminates bargaining to get the best price.

Chain stores, retail stores owned and operated by a company that has many stores, often eliminate the need for the wholesaler. They, in many cases, buy directly from the producers at low prices and in large quantities.

Smaller retail stores also play an important role in our economic picture. These stores often offer services that bigger stores cannot afford to offer. They often will take orders by telephone and even may deliver to your door. They may handle goods which are unique or not in great demand. They may specialize and offer a specific expertise that a large department store cannot.

Throughout this unit the word "consumer" has been used often. At this point we should investigate what a consumer is and how to be a good consumer.

We are all consumers of customers. A consumer is one who buys or uses products or services. America's businesses spend millions of dollars annually in advertising their products, trying to convince us that their products are the best and that we need their products. Some think up a clever slogan about their products hoping we will remember it when it comes time to go to the store.

Advertisers are not always perfectly honest about their products, which makes intelligent shopping more difficult. Some shoppers do not try to learn to be good shoppers. They are called "impulse" buyers. They buy things without planning to, on the spur of the moment. They make purchases whether they can afford to or not.

There are a number of ways to get more for your shopping dollar. A wise shopper will look for advertisements of sales. A low price does not always mean a bargain. A product is not a bargain if you can't really use it or if it is poorly made or lacking a proper guarantee from an established company. "Caveat emptor" is an old expression that it is well to remember. It means "let the buyer beware."

Good shoppers are able to judge good price and good quality. Some do this by shopping at stores which guarantee everything they sell. Others shop around or do comparison shopping to find the better bargain. Some people buy only brand-name goods. These are goods known to most American consumers. They are usually products from large corporations that spend a lot of money to develop products of good quality and they stand behind them.

A good shopper also studies the product's labels. The U.S. government requires most of these labels to help consumers judge the content and quality of the product. Labels may also be deceiving. Such terms as "pre-shrunk" or "highest quality" mean very little, whereas "sanforized" tells you that a garment won't shrink more than one percent.

Today there are a number of organizations that protect or aid consumers. Some examples are the Better Business Bureau, the Federal Trade Commission, the National Bureau of Standards, the Department of Agriculture and the Postal Service. There are also some private organizations that help consumers, most notably Consumer's Research and Consumers' Union.

Once you have made your decision about what to buy, you must decide when to pay for it. You can pay cash right away, or charge it or buy it on an installment plan.

If you pay cash you are likely to be careful before spending your money, since you must pay in full at the time of purchase. Sometimes paying cash may get you a discount.

A charge account is a form of credit that stores give to their reliable customers, allowing them to make purchases at any time during the month and to pay for them later. The customer is usually expected to pay the bill within thirty days. A charge account is usually given to anyone who has a steady job and pays bills on time.

There are both advantages and disadvantages to charge accounts. Charge accounts are an easy way of buying things. They provide an accurate record of what you bought and how much you paid. You are able to purchase items without any money, enabling you to take advantage of sales. It also is easy to have things exchanged. If you pay your bills regularly, having a charge account enables you to establish a good credit rating. A credit rating tells how well a customer pays his bills. A good credit rating is important when applying for a loan or a mortgage.

An installment plan is similar to a charge account. A customer may buy an item without paying in full immediately, paying a “down payment” in cash. The remainder or balance is paid in a number of payments or installments over a period of weeks, months, or possibly years. Larger purchases, such as refrigerators, furniture, or cars, are often bought on an installment plan. Buying on the installment plan increases the total cost.

In addition to the normal cost the business adds a carrying charge. This charge helps the business pay for bookkeeping and mailing bills. Sometimes interest is also added to the payments.

Before using an installment plan one would be wise to try and save for the item or check with local banks for a loan. It may be cheaper to borrow from a bank than pay the installment payments. A large down payment also reduces the size of the installments. Before buying any product be sure that you want and need it.

Charge accounts and installment plans can be used improperly. Often, they lead to impulse buying. The convenience of the credit may discourage comparison shopping. Both plans of buying, unless used wisely, can lead customers to overextend themselves financially. Failure to pay for items will result in the store’s suing for the balance or repossessing the goods, and may ruin the buyer’s credit ratings.

Section IV - Money and Banking

In early times, people managed to get along without money. They would trade one thing for another. This type of trade is called “barter.” People never knew for sure the worth of their items; they were worthless if the other party didn’t need them. Items were also bulky and measurement inaccurate.

Money has a number of uses in our economy. Money is a medium of exchange. It is something that can be exchanged or traded for goods and services. Money is a measure of value. Americans use money as a measure of what things are worth. The value of things in terms of money is their price. Money is also used as a means of storing up wealth and measuring the amount one person owes another.

Money in different forms and values is used all over the world today. But all money has four common features. Money must be easy to carry and take up little space; it must be based upon units that are easily multiplied and divided; it must be durable; and it must be made in a standard form and guaranteed by a nation's government. With these conditions met, people will accept money in exchange for goods and services.

American money, or "currency," comes in the form of both paper and metal coin. We consider these forms "legal tender," meaning that we accept them as payment for goods, services, and debts. Another form of money is checkbook money. Checks are among the most commonly used forms of money. They are different in that the government does not back up a check's worth. Checks are guaranteed by the "drawer," the person who writes the check. Checks are written orders to the bank to pay a sum of money to the person named on the check, the "payee." Checks are not considered legal tender and therefore do not have to be accepted an payment for goods and services.

Money has another important role in our economy. Credit is based upon money. Credit is a promise to pay later for goods or services received now. Credit is based upon the creditor's, or lender's, faith that the debtor will be willing and able to repay the loan with interest. Credit extends the amount of money in use, and uses "future" money. Money is of little value unless it is used in an economy. The flow or circulation of money through our economy stimulates it and increases growth. Money is received by workers who then spend it on goods and services, or who may also save some in a bank account. The bank uses this money to make loans to businesses and individuals. This way, both money spent and money saved continues to circulate.

Banking began when people realized the need to keep their money in a safe place. In most communities there was at least one man who kept his wealth well guarded. That man was the goldsmith. Before long his neighbors asked if he would keep their money in his safe. Eventually more and more people wanted this protection and soon he began to charge a small fee for this service. It soon followed that people who needed money began to ask the goldsmith for a loan. They had to sign a paper saying when the money would be repaid. They also promised to pay interest, an additional sum for the use of the money. Signing a paper promising to repay the loan was not enough of a guarantee; the borrower had to promise to give the lender his property if the borrower didn't pay on time. Property used to guarantee that a loan will be repaid is called "collateral." These and other practices started by early moneylenders later developed into modern banking.

Banks may be characterized in two different ways, by the source of their charters, and by the kind of business they carry on. There are "national banks" which are chartered and supervised by the federal government. And there are state banks which are chartered and supervised by the state government. Most banks fall into one of two categories according to the business they handle: commercial banks, and savings and loan associations.

Commercial banks and trust companies specialize in making loans. It is the interest from these loans which supports the bank. These banks handle checking accounts for businesses and individuals. They will usually also have savings departments and trust departments. Trust departments help people and businesses manage their property and invest their money wisely. Savings banks accept a person's savings and pay interest to him for the use of the funds. The bank then uses this money to make loans and to invest in stocks and bonds. Only recently have some savings institutions offered checking accounts to their customers.

The banking activities in America are greatly influenced by the Federal Reserve System, created in 1913 by Congress "to maintain sound banking conditions and an adequate supply of credit at reasonable cost for use in commerce, industry, and agriculture." All national banks are required to be members and some state banks are members, although they are not required to join.

The United States is divided into twelve Federal Reserve Districts. There is one Federal Reserve Bank in each district. The district bank is run as a business corporation. All of its stock is owned by banks in the district. The Federal Reserve Banks have no financial dealings with private individuals or businesses. In other words, the Federal Reserve Bank is a bankers' bank.

The Federal Reserve Banks serve two main purposes. First, they handle the national government's banking needs. The Secretary of the Treasury deposits the funds of the United States in these banks. The Secretary then writes checks on these accounts, just as an individual would. These banks also sell government bonds. The Federal Reserve System is also in charge of putting United States currency into circulation. Secondly, member banks must deposit a part of their reserve funds in the local district bank. When they need more money, the members may withdraw some of their reserves to build up their cash on hand.

Supervision of the twelve Federal Reserve Banks is in the hands of the Federal Reserve Board of Governors. There are seven members, appointed by the President, and approved by the Senate for a fourteen-year term. The Board decides how much credit and loans most banks can give.

The Board, by stating the amount a member has to set aside in reserve, affects that member's ability to lend money. By increasing the amount in reserve, they decrease the amount available to lend. This would be reflected in higher interest rates to discourage borrowing. In this way, the Federal Reserve System influences banking and the use of credit in the United States.

Class Activities for Section II

1. Have the students explain the following terms: economy, free market, free competition, capital, capitalism, profit, monopoly, legal monopoly, dividends.
2. Discuss how free competition influences prices.
3. What does "laissex-faire" mean economically?
4. How does the government "referee" our economy?
5. Draw and fill in the following chart:

(figure available in print form)

6. List the reasons you would rather own common stock, preferred stock, or bonds.
7. Have the students list business activities of government and list the services they provide. (A) Transit lines: transportation (B) Public schools: education (C) TVA: hydroelectric production (D) FDIC: insurance (E) Parks: recreation (F) Small Business Administration: loans (G) Government hospitals (VA): health care
8. Draw a comparison between a command economy and our own.

Class Activities for Section III

1. Have the students explain the following terms: GNP, rent, mass production, mass marketing, machine tools, standard parts, division of labor, transportation, wholesaler, consumer, charge accounts, credit rating.
2. Visit a museum and find early examples of American machinery. What do they tell you about the production methods used and the power source?
3. Have the students list and explain the significance of each of the four factors of production.
4. Have the students list the four types of economic activities and name a business as an example of each.
   A. Basic production: (Examples will vary)
   B. Manufacturing:
   C. Distribution:
   D. Services:
5. Have the students section off the main industrial areas of the U.S.
6. Compile a list of local organizations to aid consumers.
7. Discuss the rules for wise buying.

Class Activities for Section IV

1. Discuss the advantages of money over barter.
2. Have the students explain these terms: barter, medium of exchange, measure of value, bullion, legal tender, credit, checkbook money loans, discounting, demand deposit, time deposit.
3. Draw a chart showing how currency flows through our economy.
4. Discuss: What would life be like without money? How would trade go on?
5. Explain the role our government plays in our money system.
6. How do banks obtain their money?
7. Go to a bank and speak to a loan officer, and apply for and renew a loan.
8. Draw on a map of the U.S. the twelve Federal Reserve Districts, showing where each district bank is located.

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Multimedia Resources

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mp= motion picture	fs= film strip
ch= chart	tr= tape recording

American Transportation (fs), Life.

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Basic Ideas of Democratic Economics (fs), McGraw-Hill.

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