Brief Contents

Part 1	WHAT IS ECONOMICS? 1 First Principles / 1 2 Economic Models: Trade-offs and Trade / 23 Appendix: Graphs in Economics / 47
Part 2	SUPPLY AND DEMAND 3 Supply and Demand / 66 4 Price Controls and Quotas: Meddling with Markets / 101 5 Elasticity and Taxation / 137
Part 3	THE PRODUCTION DECISION 6 Behind the Supply Curve: Inputs and Costs / 175 7 Perfect Competition and the Supply Curve / 202
Part 4	BEYOND PERFECT COMPETITION 8 Monopoly / 231 9 Oligopoly and Monopolistic Competition / 262
Part 5	MICROECONOMICS AND PUBLIC POLICY 10 Externalities and Public Goods / 286 11 Poverty, Inequality, and the Welfare State / 315
Part 6	INTRODUCTION TO MACROECONOMICS 12 Macroeconomics: The Big Picture / 343 13 GDP and the CPI: Tracking the Macroeconomy / 360 14 Unemployment and Inflation / 377
Part 7	ECONOMIC GROWTH AND FLUCTUATIONS 15 Long-Run Economic Growth / 407 16 Aggregate Demand and Aggregate Supply / 439
Part 8	STABILIZATION POLICY 17 Fiscal Policy / 475 18 Money, Banking, and the Federal Reserve System / 506 19 Monetary Policy / 541
Part 9	THE INTERNATIONAL ECONOMY 20 International Trade, Capital Flows, and Exchange Rates /

Solutions to Check Your Understanding Questions / S-1 Glossary / G-1 Index / I-1 569

Contents

Preface vi

Part 1 WHAT IS ECONOMICS?

Chapter 1 First Principles / 1

Common Ground 1

The Ordinary Business of Life 2

My Benefit, Your Cost 3 Good Times, Bad Times 3 Onward and Upward 4

Principles That Underlie Individual Choice: The Core of Economics 4

Principle #1: Choices Are Necessary Because Resources
Are Scarce 4

Principle #2: The True Cost of Something Is Its Opportunity Cost 5

Principle #3: "How Much" Is a Decision at the Margin 6

Principle #4: People Usually Respond to Incentives, Exploiting Opportunities to Make Themselves Better Off 7

ECONOMICS IN ACTION Boy or Girl? It Depends on the Cost 9

Interaction: How Economies Work 10

Principle #5: There Are Gains from Trade 11

Principle #6: Markets Move Toward Equilibrium 12

Principle #7: Resources Should Be Used Efficiently to Achieve Society's Goals 13

Principle #8: Markets Usually Lead to Efficiency 14

Principle #9: When Markets Don't Achieve Efficiency, Government Intervention Can Improve Society's Welfare 15

ECONOMICS IN ACTION Restoring Equilibrium on the Freeways 15

Economy-Wide Interactions 16

Principle #10: One Person's Spending Is Another Person's Income 17

Principle #11: Overall Spending Sometimes Gets Out of Line with the Economy's Productive Capacity 17

Principle #12: Government Policies Can Change Spending 18

ECONOMICS IN ACTION Adventures in

Babysitting 18

Chapter 2

Economic Models: Trade-offs and Trade / 23

From Kitty Hawk to Dreamliner 23

Models in Economics: Some Important Examples 24

Trade-offs: The Production Possibility Frontier 25
Comparative Advantage and Gains from Trade 30
Comparative Advantage and International Trade, in
Reality 33

Global Comparison Pajama Republics 34

Transactions: The Circular-Flow Diagram 34

ECONOMICS IN ACTION Rich Nation, Poor Nation 36

Using Models 37

Positive versus Normative Economics 37 When and Why Economists Disagree 38

ECONOMICS IN ACTION Economists, Beyond the

Ivory Tower 39

Solved Problem Heavy Metal and High Protein 41

Chapter 2

Appendix: Graphs in Economics / 47

Getting the Picture 47

Graphs, Variables, and Economic Models 47 How Graphs Work 47

Two-Variable Graphs 47 Curves on a Graph 49

A Key Concept: The Slope of a Curve 50

The Slope of a Linear Curve 50 Horizontal and Vertical Curves and Their Slopes 51 The Slope of a Nonlinear Curve 52

Calculating the Slope Along a Nonlinear Curve 52

Calculating the Area Below or Above a Curve 55 Graphs That Depict Numerical Information 56

Types of Numerical Graphs 56

Problems in Interpreting Numerical Graphs 58

Solved Problem Working with Graphs 60

Part 1 BUSINESS CASES 64

- How Priceline.com Revolutionized the Travel Industry 64
- Efficiency, Opportunity Cost, and the Logic of Lean Production 65

Part 2 SUPPLY AND DEMAND

Chapter 3

Supply and Demand / 66

A Natural Gas Boom 66

Supply and Demand: A Model of a Competitive Market 67

The Demand Curve 68

The Demand Schedule and the Demand Curve 68 Shifts of the Demand Curve 69

Global Comparison Pay More, Pump Less 70
Understanding Shifts of the Demand Curve 72

ECONOMICS IN ACTION Beating the Traffic 77

The Supply Curve 78

The Supply Schedule and the Supply Curve 78
Shifts of the Supply Curve 79
Understanding Shifts of the Supply Curve 80

Pampered 84 CONOMICS IN ACTION Only Creatures Small and

Supply, Demand, and Equilibrium 85

Finding the Equilibrium Price and Quantity 85

Why Do All Sales and Purchases in a Market Take Place at the Same Price? 86

Why Does the Market Price Fall If It Is Above the Equilibrium Price? 87

Why Does the Market Price Rise If It Is Below the Equilibrium Price? 87

Using Equilibrium to Describe Markets 88

ECONOMICS IN ACTION The Price of Admission 88

Changes in Supply and Demand 89

What Happens When the Demand Curve Shifts 90
What Happens When the Supply Curve Shifts 91
Simultaneous Shifts of Supply and Demand Curves 92

ECONOMICS IN ACTION The Cotton Panic and Crash of 2011 93

Competitive Markets—and Others 94

Solved Problem Sugar, Sugar 95

Chapter 4

Price Controls and Quotas: Meddling with Markets / 101

Big City, Not-So-Bright Ideas 101

Consumer Surplus and the Demand Curve 102

Willingness to Pay and the Demand Curve 102 Willingness to Pay and Consumer Surplus 102

Producer Surplus and the Supply Curve 104

Cost and Producer Surplus 104

The Gains from Trade 106

ECONOMICS IN ACTION Take the Keys,

Please 107

Why Governments Control Prices 108 Price Ceilings 109

Modeling a Price Ceiling 109

How a Price Ceiling Causes Inefficiency 111

So Why Are There Price Ceilings? 115

ECONOMICS IN ACTION Price Controls in Venezuela:

"You Buy What They Have" 116

Price Floors 117

How a Price Floor Causes Inefficiency 119 So Why Are There Price Floors? 121

Global Comparison Check Out Our Low, Low Wages! 122

ECONOMICS IN ACTION The Rise and Fall of the

Unpaid Intern 122

Controlling Quantities 124

The Anatomy of Quantity Controls 124
The Costs of Quantity Controls 127

ECONOMICS IN ACTION Crabbing, Quotas, and Saving Lives in Alaska 128

Solved Problem The World's Second Most Expensive City 130

Chapter 5

Elasticity and Taxation / 137

Taken for a Ride 137

Defining and Measuring Elasticity 138

Calculating the Price Elasticity of Demand 138

An Alternative Way to Calculate Elasticities: The Midpoint Method 140

ECONOMICS IN ACTION Estimating Elasticities 141

Interpreting the Price Elasticity of Demand 142

How Elastic Is Elastic? 142

Price Elasticity Along the Demand Curve 147

What Factors Determine the Price Elasticity of Demand? 148

ECONOMICS IN ACTION Responding to Your

Tuition Bill 149

Other Demand Elasticities 150

The Cross-Price Elasticity of Demand 150

The Income Elasticity of Demand 151

Global Comparison Food's Bite in World Budgets 152

ECONOMICS IN ACTION Spending It 152

The Price Elasticity of Supply 153

Measuring the Price Elasticity of Supply 153
What Factors Determine the Price Elasticity of Supply? 154

ECONOMICS IN ACTION European Farm

Surpluses 155

An Elasticity Menagerie 156

The Benefits and Costs of Taxation 157

The Revenue from an Excise Tax 157

Tax Rates and Revenue 158

The Costs of Taxation 160

Elasticities and the Deadweight Loss of a Tax 162

ECONOMICS IN ACTION Taxing the Marlboro Man 164

Solved Problem Drive We Must 165

Part 2 BUSINESS CASES 172

An Uber Way to Get a Ride 172

Medallion Financial: Cruising Right Along 173

The Airline Industry: Fly Less, Charge More 174

Part 3 THE PRODUCTION DECISION

Chapter 6

Behind the Supply Curve: Inputs and Costs / 175

The Farmer's Margin 175

The Production Function 176

Inputs and Output 176

Global Comparison Wheat Yields Around the World 178

From the Production Function to Cost Curves 180

ECONOMICS IN ACTION The Mythical Man-Month 182

Two Key Concepts: Marginal Cost and Average Cost 183

Marginal Cost 183

Average Total Cost 185

Minimum Average Total Cost 188

Does the Marginal Cost Curve Always Slope Upward? 189

ECONOMICS IN ACTION Smart Grid Economics 190

Short-Run versus Long-Run Costs 191

Returns to Scale 194

Summing Up Costs: The Short and Long of It 195

ECONOMICS IN ACTION There's No Business Like

Snow Business 196

Solved Problem Production Challenges for Tesla:

The Model X 197

Chapter 7

Perfect Competition and the Supply Curve / 202

Deck the Halls 202

Perfect Competition 203

Defining Perfect Competition 203

Two Necessary Conditions for Perfect Competition 203

Free Entry and Exit 204

ECONOMICS IN ACTION Paid to Delay 205

Production and Profits 206

Using Marginal Analysis to Choose the Profit-Maximizing Quantity of Output 206

When Is Production Profitable? 209

The Short-Run Production Decision 212

Changing Fixed Cost 215

Summing Up: The Perfectly Competitive Firm's Profitability and Production Conditions 215

ECONOMICS IN ACTION Farmers Move Up Their

Supply Curves 216

The Industry Supply Curve 217

The Short-Run Industry Supply Curve 217

The Long-Run Industry Supply Curve 218

The Cost of Production and Efficiency in Long-Run Equilibrium 222

ECONOMICS IN ACTION From Global Wine Glut to Shortage 223

Solved Problem Is There a Catch? 224

Part 3 BUSINESS CASES 229

- Kiva Systems' Robots versus Humans: The Challenge of Holiday Order Fulfillment 229
- Shopping Apps, Showrooming, and the Challenges Facing Brick-and-Mortar Retailers 230

Part 4 BEYOND PERFECT COMPETITION

Chapter 8 Monopoly / 231

Everybody Must Get Stones 231

Types of Market Structure 232

The Meaning of Monopoly 233

Monopoly: Our First Departure from Perfect Competition 233

What Monopolists Do 233

Why Do Monopolies Exist? 235

ECONOMICS IN ACTION Newly Emerging Markets:

A Diamond Monopolist's Best Friend 237

How a Monopolist Maximizes Profit 239

The Monopolist's Demand Curve and Marginal Revenue 239

The Monopolist's Profit-Maximizing Output and Price 242

Monopoly versus Perfect Competition 242

Monopoly: The General Picture 244

ECONOMICS IN ACTION Shocked by the High Price

of Electricity 244

Monopoly and Public Policy 246

Welfare Effects of Monopoly 246

Preventing Monopoly 247

Dealing with Natural Monopoly 248

ECONOMICS IN ACTION Why Is Your Broadband So

Slow? And Why Does It Cost So Much? 249

Price Discrimination 251

The Logic of Price Discrimination 251

Perfect Price Discrimination 253

ECONOMICS IN ACTION Sales, Factory Outlets, and

Ghost Cities 255

Solved Problem Painkiller Pricing 256

Chapter 9

Oligopoly and Monopolistic Competition / 262

Caught in the Act 262

The Meaning of Oligopoly 263

Understanding Oligopoly 263

Oligopoly in Practice 266

ECONOMICS IN ACTION Bitter Chocolate? 268

Games Oligopolists Play 270

The Prisoners' Dilemma 270

Repeated Interaction and Tacit Collusion 272

ECONOMICS IN ACTION The Rise and Fall and Rise

of OPEC 273

The Meaning of Monopolistic Competition 275

Large Numbers 276

Free Entry and Exit in the Long Run 276

Differentiated Products 276

ECONOMICS IN ACTION Any Color, So Long as It's

Black 278

Solved Problem The Ups (and Downs) of Oil Prices 278

Part 4 BUSINESS CASES 284

- Amazon and Hachette Go to War 284
- Virgin Atlantic Blows the Whistle . . . or Blows It? 285

Chapter 10

Externalities and Public Goods / 286

The Great Stink 286

Externalities 287

Pollution: An External Cost 287

The Socially Optimal Quantity of Pollution 288

Why a Market Economy Produces Too Much Pollution 289

Private Solutions to Externalities 290

ECONOMICS IN ACTION How Much Does Your

Electricity Really Cost? 291

Policies Toward Pollution 293

Environmental Standards 293

Emissions Taxes 293

Global Comparison Economic Growth and Greenhouse Gases in

Six Countries 294

Tradable Emissions Permits 295

Comparing Environmental Policies with an Example 296

ECONOMICS IN ACTION Cap and Trade 297

Positive Externalities 298

Preserved Farmland: An External Benefit 299

Positive Externalities in Today's Economy 300

ECONOMICS IN ACTION The Impeccable Economic

Logic of Early-Childhood Intervention Programs 301

Public Goods 301

Characteristics of Goods 302

Why Markets Can Supply Only Private Goods Efficiently 303

Providing Public Goods 304

How Much of a Public Good Should Be Provided? 305

Cost-Benefit Analysis 307

ECONOMICS IN ACTION Old Man River 308

Solved Problem The Not So Sweet Smell of

Success 309

Chapter 11

Poverty, Inequality, and the Welfare State / 315

The Coming of Obamacare 315

Poverty, Inequality, and Public Policy 316

The Logic of the Welfare State 316

The Problem of Poverty 317

Economic Inequality 320

Global Comparison Income, Redistribution, and Inequality in Rich

Countries 321

Economic Insecurity 322

ECONOMICS IN ACTION Long-term Trends in Income

Inequality in the United States 323

The U.S. Welfare State 325

Means-Tested Programs 325

Social Security and Unemployment Insurance 326

The Effects of the Welfare State on Poverty and Inequality 326

ECONOMICS IN ACTION Welfare State Programs and

Poverty Rates in the Great Recession, 2007–2010 327

The Economics of Health Care 328

The Need for Health Insurance 328

Government Health Insurance 330

Health Care in Other Countries 331

The Affordable Care Act 332

ECONOMICS IN ACTION What Medicaid Does 334

The Debate over the Welfare State 335

Problems with the Welfare State 335

The Politics of the Welfare State 336

ECONOMICS IN ACTION French Family Values 337

Part 5 BUSINESS CASES 341

- Hunting Endangered Animals to Save Them 341
- Welfare State Entrepreneurs 342

Part 6 INTRODUCTION TO MACROECONOMICS

Chapter 12

Macroeconomics: The Big Picture / 343

The Pain in Spain 343

The Nature of Macroeconomics 344

Macroeconomic Questions 344

Macroeconomics: The Whole Is Greater Than the Sum of Its Parts 345

Macroeconomics: Theory and Policy 345

ECONOMICS IN ACTION Fending Off Depression 346

The Business Cycle 347

Charting the Business Cycle 348

The Pain of Recession 349

Taming the Business Cycle 349

ECONOMICS IN ACTION Comparing Recessions 350

Long-Run Economic Growth 351

ECONOMICS IN ACTION A Tale of Two Countries 353

Inflation and Deflation 353

The Causes of Inflation and Deflation 354

The Pain of Inflation and Deflation 354

ECONOMICS IN ACTION A Fast (Food) Measure of

Inflation 355

International Imbalances 355

ECONOMICS IN ACTION Spain's Costly Surplus 356

Chapter 13

GDP and the CPI: Tracking the

Macroeconomy / 360

The New #2 360

Measuring the Macroeconomy 361

Gross Domestic Product 361

Calculating GDP 361

What GDP Tells Us 364

ECONOMICS IN ACTION Creating the National

Accounts 364

Real GDP: A Measure of Aggregate Output 365

Calculating Real GDP 365

What Real GDP Doesn't Measure 367

ECONOMICS IN ACTION Miracle in Venezuela? 367

Price Indexes and the Aggregate Price Level 368

Market Baskets and Price Indexes 368

The Consumer Price Index 369

Other Price Measures 371

ECONOMICS IN ACTION Indexing to the CPI 372

Solved Problem A Change in Fortune? 373

Chapter 14

Unemployment and Inflation / 377

Hitting the Braking Point 377

The Unemployment Rate 378

Defining and Measuring Unemployment 378

The Significance of the Unemployment Rate 379

Growth and Unemployment 381

ECONOMICS IN ACTION Failure to Launch 383

The Natural Rate of Unemployment 384

Job Creation and Job Destruction 384

Frictional Unemployment 385

Structural Unemployment 386

The Natural Rate of Unemployment 389

Changes in the Natural Rate of Unemployment 389

ECONOMICS IN ACTION Structural Unemployment in

East Germany 391

Inflation and Deflation 392

The Level of Prices Doesn't Matter . . . 392

... But the Rate of Change of Prices Does 393

Winners and Losers from Inflation 396

Inflation Is Easy; Disinflation Is Hard 397

ECONOMICS IN ACTION Israel's Experience with

Inflation 397

Solved Problem The Current Population Survey 399

Part 6 BUSINESS CASES 404

 The Business Cycle and the Decline of Montgomery Ward 404

Getting a Jump on GDP 405

Day Labor in the Information Age 406

Part 7 ECONOMIC GROWTH AND FLUCTUATIONS

Chapter 15

Long-Run Economic Growth / 407

Airpocalypse Now 407

Comparing Economies Across Time and Space 408

Real GDP per Capita 408
Growth Rates 410

ECONOMICS IN ACTION India Takes Off 411

The Sources of Long-Run Growth 412

The Crucial Importance of Productivity 412

Explaining Growth in Productivity 413

Accounting for Growth: The Aggregate Production Function 413

What About Natural Resources? 417

ECONOMICS IN ACTION Is the End of Economic

Growth in Sight? 418

Why Growth Rates Differ 419

Explaining Differences in Growth Rates 419

Global Comparison What's the Matter with Italy? 421

The Role of Government in Promoting Economic Growth 421

ECONOMICS IN ACTION Why Did Britain Fall

Behind? 423

Success, Disappointment, and Failure 424

East Asia's Miracle 424

Latin America's Disappointment 426

Africa's Troubles and Promise 426

ECONOMICS IN ACTION Are Economies

Converging? 427

Is World Growth Sustainable? 429

Natural Resources and Growth, Revisited 429

Economic Growth and the Environment 430

ECONOMICS IN ACTION The Cost of Limiting

Carbon 432

Solved Problem Tracking India's Economic Growth 433

Chapter 16

Aggregate Demand and Aggregate Supply / 439

What Kind of Shock? 439

Aggregate Demand 440

Why Is the Aggregate Demand Curve Downward Sloping? 441

Shifts of the Aggregate Demand Curve 442 Government Policies and Aggregate Demand 445

ECONOMICS IN ACTION Moving Along the Aggregate Demand Curve, 1979–1980 446

Aggregate Supply 447

The Short-Run Aggregate Supply Curve 447
Shifts of the Short-Run Aggregate Supply Curve 449
The Long-Run Aggregate Supply Curve 451
From the Short Run to the Long Run 453

ECONOMICS IN ACTION Sticky Wages in the Great Recession 455

The AD-AS Model 456

Short-Run Macroeconomic Equilibrium 457
Shifts of Aggregate Demand: Short-Run Effects 458
Shifts of the SRAS Curve 458

Global Comparison Supply Shocks of the Twenty-first Century 460

Long-Run Macroeconomic Equilibrium 460

ECONOMICS IN ACTION Supply Shocks versus Demand Shocks in Practice 463

Macroeconomic Policy 464

Policy in the Face of Demand Shocks 465 Responding to Supply Shocks 466

ECONOMICS IN ACTION Is Stabilization Policy Stabilizing? 466

Solved Problem A Shocking Analysis 467

Part 7 BUSINESS CASES 473

- · How Boeing Got Better 473
- Slow Steaming 474

Part 8 STABILIZATION POLICY

Chapter 17

Fiscal Policy / 475

How Big Is Big Enough? 475

Fiscal Policy: The Basics 476

Taxes, Purchases of Goods and Services, Government Transfers, and Borrowing 476

The Government Budget and Total Spending 477 Expansionary and Contractionary Fiscal Policy 478

Can Expansionary Fiscal Policy Actually Work? 480

A Cautionary Note: Lags in Fiscal Policy 481

ECONOMICS IN ACTION What Was in the Recovery Act? 482

Fiscal Policy and the Multiplier 483

Multiplier Effects of an Increase in Government Purchases of Goods and Services 483

Multiplier Effects of Changes in Government Transfers and Taxes 484

How Taxes Affect the Multiplier 485

ECONOMICS IN ACTION Austerity and the

Multiplier 486

The Budget Balance 487

The Budget Balance as a Measure of Fiscal Policy 488
The Business Cycle and the Cyclically Adjusted Budget
Balance 488

Should the Budget Be Balanced? 490

ECONOMICS IN ACTION Europe's Search for a

Fiscal Rule 491

Long-Run Implications of Fiscal Policy 492

Deficits, Surpluses, and Debt 493

Global Comparison The American Way of Debt 494

Problems Posed by Rising Government Debt 494

Deficits and Debt in Practice 495

Implicit Liabilities 497

ECONOMICS IN ACTION Are We Greece? 498

Solved Problem Mind the Gap 500

Chapter 18

Money, Banking, and the Federal Reserve System / 506

Funny Money 506

The Meaning of Money 507

What Is Money? 507

Roles of Money 508

Global Comparison The Big Moneys 508

Types of Money 509

Measuring the Money Supply 510

ECONOMICS IN ACTION The History of the

Dollar 511

The Monetary Role of Banks 512

What Banks Do 513

The Problem of Bank Runs 514

Bank Regulation 515

ECONOMICS IN ACTION It's a Wonderful Banking

System 516

Determining the Money Supply 517

How Banks Create Money 517

Reserves, Bank Deposits, and the Money Multiplier 518

The Money Multiplier in Reality 519

ECONOMICS IN ACTION Multiplying Money

Down 521

The Federal Reserve System 521

The Structure of the Fed 522

What the Fed Does: Reserve Requirements and the Discount Rate 523

Open-Market Operations 523

The European Central Bank 525

ECONOMICS IN ACTION The Fed's Balance Sheet,

Normal and Abnormal 526

The Evolution of the American Banking System 528

The Crisis in American Banking in the Early Twentieth Century 528

Responding to Banking Crises: The Creation of the Federal Reserve 529

The Savings and Loan Crisis of the 1980s 530

Back to the Future: The Financial Crisis of 2008 531

ECONOMICS IN ACTION Regulation After the 2008

Crisis 534

Solved Problem Multiplying Money 535

Chapter 19

Monetary Policy / 541

The Most Powerful Person in Government 541

The Demand for Money 542

The Opportunity Cost of Holding Money 542

The Money Demand Curve 544

Shifts of the Money Demand Curve 545

ECONOMICS IN ACTION A Yen for Cash 546

Money and Interest Rates 547

The Equilibrium Interest Rate 547

Monetary Policy and the Interest Rate 549

Long-Term Interest Rates 550

ECONOMICS IN ACTION The Fed Reverses

Course 551

Monetary Policy and Aggregate Demand 552

Expansionary and Contractionary Monetary Policy 552

Monetary Policy in Practice 553

The Taylor Rule Method of Setting Monetary Policy 554

Inflation Targeting 554

Global Comparison Inflation Targets 555

The Zero Lower Bound Problem 556

ECONOMICS IN ACTION What the Fed Wants, the

Fed Gets 556

Money, Output, and Prices in the Long Run 557

Short-Run and Long-Run Effects of an Increase in the Money Supply 558

Monetary Neutrality 559

Changes in the Money Supply and the Interest Rate in the Long Run 559

ECONOMICS IN ACTION International Evidence of Monetary Neutrality 560

Solved Problem The Great Mistake of 1937 561

Part 8 BUSINESS CASES 566

- Here Comes the Sun 566
- The Perfect Gift: Cash or a Gift Card? 567
- PIMCO Bets on Cheap Money 568

Part 9 THE INTERNATIONAL ECONOMY

Chapter 20 International Trade, Capital Flows, and Exchange Rates / 569

The Everywhere Phone 569

Comparative Advantage and International Trade 570

Production Possibilities and Comparative Advantage, Revisited 571

The Gains from International Trade 572

Comparative Advantage versus Absolute Advantage 574

Global Comparison Productivity and Wages Around the World 575

Sources of Comparative Advantage 576

ECONOMICS IN ACTION How Hong Kong Lost Its Shirts 578

Supply, Demand, and International Trade 579

The Effects of Imports 579

The Effects of Exports 581

International Trade and Wages 583

ECONOMICS IN ACTION Trade, Wages, and Land Prices in the Nineteenth Century 584

The Effects of Trade Protection 585

The Effects of a Tariff 585
The Effects of an Import Quota 587

ECONOMICS IN ACTION Trade Protection in the United States 588

Officed States 300

Capital Flows and the Balance of Payments 588

Balance of Payments Accounts 589

Underlying Determinants of International Capital Flows 592

Global Comparison Big Surpluses 593

Two-Way Capital Flows 593

ECONOMICS IN ACTION The Golden Age of Capital Flows 594

The Role of the Exchange Rate 595

Understanding Exchange Rates 595

The Equilibrium Exchange Rate 596

Inflation and Real Exchange Rates 599

Purchasing Power Parity 601

ECONOMICS IN ACTION Low-Cost America 602

Solved Problem Trade Is Sweet 604

Part 9 BUSINESS CASE 609

Li & Fung: From Guangzhou to You 609

Solutions to Check Your Understanding Questions S-1

Glossary G-1

Index I-1