

Lecture 56: Government and the American Economy (1940-1973)

Multiple Choice Questions-

|| = Correct

1. What were two of the fiscal policies of the American government?
 - a. Using taxation and government spending to influence the economy and tax cuts.
 - b. Minimizing government spending and tax cuts.
 - c. Government spending and encouraging monopolies.
 - d. Increase taxes and government spending.
2. Who developed the policy of The New Economics?
 - a. Malcolm X
 - b. Adam Smith
 - c. Thomas Dewey
 - d. John M. Keynes
3. What was the formula for New Economics?
 - a. $GNP = C + \text{Population}$
 - b. $GNP = C + I + G$
 - c. $GNP = \text{Gross national product}$
 - d. $GNP = \text{GDP}$
4. What did the Employment Act of 1946 do?
 - a. Said that labor unions were no longer legal.
 - b. Said that the return of laissez faire was necessary for the nation to grow again.
 - c. Said the Government shall play a role in protecting the government.
 - d. Said that the federal government shall play less of a role in protecting and aiding the state governments.
5. The purpose of the Defense Production Act of 1950 was what?
 - a. To give the President less power and more power to the people.
 - b. Gave the President more power in controlling wages and prices.
 - c. Gave the President the ability to create an imbalance between prices and wages.
 - d. To give the President less influence in controlling wages and prices for the safety of the country.
6. Which President was the first Republican President nominated in approximately twenty years?
 - a. Reagan
 - b. Nixon
 - c. Truman
 - d. Eisenhower
7. What does FDIC stand for and what is its purpose?
 - a. Federal Deficit Integration Committee, the purpose of the FDIC is to help ease the shock and possibility of depression of the American economy during a severe debt crisis.

- b. Federal Deposit Insurance Corporation, the purpose of the FDIC is that the government is guaranteeing money to the people when they put it in the bank.
- c. Federal Deposit Insurance Corporation, the purpose of the FDIC is to give the banks more leeway in being able to spend and loan more money than available.
- d. Federal Department of International Concerns, the purpose of the FDIC is similar to the Foreign Affairs Commission in that its purpose is to deal with global issues.
8. One of President Kennedy's goals during his term as President of the United States was to decrease the unemployment rate, what was that rate during the beginning of his term?
- a. 7.3%
- b. 5.023%
- c. 6.206%
- d. 6.3%
9. Johnson wanted both "guns and butter", which caused huge budget debts, what did "guns and butter" stand for?
- a. Guns stood for the National Guard armament, and butter stood for the food for the people so that the war on poverty was won.
- b. Guns stood for the arms used in the Vietnam War, and butter stood for the food for the people so that the war on poverty was won.
- c. Guns stood for defense and weapons, and butter stood for social programs.
- d. Guns stood for defense on the home front and butter stood for supplies and necessities of war.
10. What were the four phases of Nixon's New Economic Policy?
- a. 1) puts in freeze on prices, wages and rents, 2) eases off wage and price control, 3) puts back on more wage and price controls and 4) tries to make prices and wages control voluntarily.
- b. 1) gives the military more money, 2) debt increases and panic makes Nixon take away military spending, 3) increase in casualties makes President increase military spending, and 4) realizes war is lost and pulls out.
- c. 1) uses stagflation, 2) tries to cure high unemployment and high inflation, 3) stops production of money, and 4) abandons Republican ideals in panic.
- d. 1) allows the people to vote on minimum wage, 2) discusses price control with Congress and is denied, 3) returns nation to laissez faire, monopolies start up again and stronger, and 4) President decides to control wages and prices strictly.

Key Terms

New Economics- New Economics was founded by John Maynard Keynes. New Economics is the concept the GNP (gross national product) is equal to consumer spending plus investment (usually means capital) plus government spending, this all equals together the total amount of monetary spending. Investment is the most important part of the formula. The government is unable to affect the consumer spending or investments made.

Jawboning- Similar to President Johnson, Nixon used jawboning to gain support for voluntary price and wage controls, he tried to communicate and influence the public by

utilizing the advantages of the media and the fad of television. Nixon was unsuccessful in his attempt.

Monetary- Monetary policies deal with money supply and influences inflation and deflation in an attempt to shape the economy. Monetary policies affect interest rates through Federal Reserve Boards, and regulate banks and the set amount of money that must be in the bank available at anytime.

Fiscal- Fiscal policies include using taxation and government spending to influence the economy, as well as applying tax cuts, and government spending.

Fine Tuning- Fine tuning was a method used by the Eisenhower Administration used to make minor changes to monetary policies to regulate the economy. The three flaws of fine tuning are the that it takes a while for the government to recognize a problem and for the government to figure out what action to take, and once the government takes action it takes time for it to actually affect the economy. Fine tuning works to a certain degree but its success is limited.

Nixonomics- Nixonomics refers to Nixon's plan, involving a solution to high inflation and unemployment or stagflation, Nixon did not know what to do and abandoned the Republican ideals for a New Economic Policy.

"Guns or Butter"- "Guns and Butter" was part of President Johnson's "Great Society", the guns represented defense and weapons and the butter represented the social problems. Johnson wanted to give equal attention and money to both causes. This caused huge budget debts, which then leads to huge inflation.

John Maynard Keynes- Keynes was the author of Keynesian economics or new economics. Keynes was an important economist of the time and analyzed the relations between consumer spending, investment and government spending. Keynes encouraged an interventionist government policy that could utilize fiscal and monetary policies to prevent recessions.

Questions

1. What justifies deficit spending?
 - a. It keeps money in circulation.
 - b. Spend more to earn more
 - c. It is the only way to keep up with the demands of the Americans.
 - d. The theory of "guns or butter"

2. According to Keynesian economics, what can't the government influence in the equation of $GNP = C + I + G$?
 - a. C
 - b. I
 - c. G

- d. Both a and b
3. All of the following are the economy's built in stabilizers EXCEPT:
 - a. deficit spending
 - b. OXPC, then revival in the business cycle
 - c. Social security
 - d. FDIC
 4. Why was there major inflation after World War II was over?
 - a. The US had to feed the rest of the world.
 - b. The US was the richest country in the world.
 - c. There had been a lot of rationing during the war, so after the war, people were not forced to save their money.
 - d. The stock market was doing very well.
 5. What was the significance of the 1950 Defense Production Act?
 - a. It gave the government control over the economy so that they could make sure it was stable.
 - b. The government forcibly took over defense related matters in order to prolong a war that the American public did not support.
 - c. It was a dangerous shift towards communism.
 - d. The government ordered more nuclear weapons to be made.
 6. How did the Phillips curve represent the relationship between unemployment and inflation?
 - a. more inflation led to more unemployment
 - b. less inflation means less unemployment
 - c. less unemployment means more inflation
 - d. both a and b
 7. Why is the Phillips curve inaccurate?
 - a. Inflation and unemployment are not actually related.
 - b. It breaks down when there are more factors involved.
 - c. There is an inverse relationship between inflation and unemployment.
 - d. The information that was given was inaccurate.
 8. Why was the Johnson's "guns and butter" campaign unsuccessful?
 - a. He wanted to devote everything to war.
 - b. He wanted to devote the budget to the social programs.
 - c. There were no successful "butter" proposals.
 - d. His attention was too divided, so he was able to give enough attention to neither the foreign nor domestic programs.
 9. All of the following is a phase of Nixonomics EXCEPT:
 - a. wage and price controls
 - b. making wage and price controls voluntary

- c. go into debt on purpose
- d. stagflation

10. Why was fine tuning not very successful?

- a. It was hard for the government to recognize a problem in time.
- b. People did not respond at all to the changes.
- c. The government never actually fine tuned like they were supposed to.
- d. They were not significant enough changes to do any good for the country.

Key Terms

New Economics: This is the same thing as Keynesian Economics. It was based on the equation $GNP = \text{consumer spending} + \text{investment} + \text{government spending}$. The government cannot actually control consumer spending or investment directly. It can only control the government spending portion of the equation. The government should play a major role in regulation of growth.

Fine Tuning: This is where the government would not make any major changes in its policy, only minor ones to achieve their goals. It did not work very well because it was too hard for the government to recognize a problem in time, and then it would take too long to see the effects of the changes made.

Jawboning: This was Nixon's attempt to get the public to support his ideas of voluntary wage and price controls. He would talk on TV to try to get the citizens to volunteer for everything he proposed. This still did not work very well because people knew there would be no consequences for not following Nixon's suggestions.

Nixonomics: At first he tried fine tuning, but when that did not work, he made wage and price controls. He later eased off the wage and price controls, but the people raised the prices again. There was stagflation. Then he put the controls back in, the public was not accepting of it and it led to a scarcity of goods. At the end he decided to make wage and price controls voluntary, but no one wanted to follow this because they did not have to.

Monetary Policy: This is regulation money supply. The economy can overproduce too quickly. The Federal Reserve Board set interest rates.

"Guns or butter": Guns is money spent on defense and war, while butter is money spent on social programs. Johnson tried to focus on both and failed in both areas because his attention was too divided to help either one enough.

Fiscal Policy: This is using taxation and government spending to influence the economy. Taxation can slow down or increase government spending. It is the idea of priming the pump.

John Maynard Keynes: He came up with Keynesian Economics, which is the same thing as new economics. He basically said that the government should use their influence on the economy to regulate its growth.

Summary

The United States government was never completely laissez-faire. Their economic monetary policies dealt with money supply and helped shape the economy. Under fiscal policies, the government used taxation and government spending to influence the economy. An influential economist of the time believed that the government could not influence consumer spending or investment, but it could regulate the economy through government spending. The economy has built in stabilizers such as social security, unemployment insurance, etc. During Truman's administration, the Defense Production Act of 1950 was created so that the government could control wages, prices, and consumer credit in order to stabilize the economy during the Korean War. Eisenhower did not believe in making major changes and supported investors with low inflation. He was not as focused on helping unemployment. Kennedy's New Frontier focused on helping unemployment with a huge tax cut. Johnson did not accomplish much with his "guns and butter" goal. His attention was too divided to actually accomplish either of his goals. Nixon had tried fine tuning, but when that did not work, he made wage and price controls. Later, he eased off the controls but was forced to put the controls back in. When the mandatory controls could no longer be maintained, he made them voluntary. This did not work either because there were no consequences that forced the people to do what the government suggested.