

ECONOMICS...The Foundation of Entrepreneurship

The purpose of the study of economics is to help society decide how to create, distribute, and consume wealth. Every human activity has an economic dimension. Every time you wonder if there will be enough money to pay the rent or the mortgage, question the increase of food prices or decide to buy certain products, you are acting as an economic decision-maker.

Most people want to know more about the economy. Knowing some economics is essential to understanding what is going on in your life. Economics is not always easy to figure out and many adults and young people feel that understanding the economy is difficult.

As an individual it is important to be able to evaluate the impact of the economy on your life. As a business owner, it is important to understand economic terms and how economic changes affect your business. You don't have to be a professional economist, but you should be able to evaluate the impact of economic changes and the effects in your town, state, region, and nation. Furthermore, you should also have some idea of the impact of changing economies in other countries in the world.

Consider the importance of customers for a business. The state of the economy will have an impact on how much money customers will spend and what they will buy. This is just one example of the impact of the economy on your business.

Individuals also have a role in shaping the economy. Entrepreneurs provide an example of how their individual activities can create jobs, new products and services to improve the economy. As individuals become informed they are better able to participate in shaping the economy. Much of understanding economics is to learn to "speak the language".

OVERVIEW OF THE "LANGUAGE"

The **market** for any product or service is composed of a number of **consumers**. These consumers are people or organizations that are willing to buy your product and/or service. Business organizations sell their own products or service, but they are also major consumers of other businesses. For example, if you are selling trucks, for example, you may **target** business owners as your market for the trucks. Most of your **marketing activities** will be focused on those types of businesses that use trucks in their operations. And most of your consumers in your **market niche** will be those business owners.

The **price** you charge for your products and services will depend on a number of factors. First you need to be sure to be able to cover the **costs** of providing those items to consumers. Some of these costs are fixed and do not change no matter how many items you sell. These items include rent, insurance, a truck for deliveries, and the owner's salary. Other costs are **variable**, that is the number you must buy, adding to your costs, vary with the number of items you produce or sell. These items might include packaging materials, production workers' salaries, and shipping charges.

When considering the potential success of your business you must think of **the law of supply and demand**. This means the number of items like yours that are available to the market (**supply**) and the number of consumers who are in the market for this product (**demand**).

When the supply is **scarce** and there is a great need for this product or service in this particular market, you say that the demand is higher than the supply. When this is true, those who already produce this product can charge a high price for it. People will pay a lot for it if they really want it. It can be said that the **demand is high**.

Under these circumstances entrepreneurs often see an opportunity to introduce a new product that fills this same need for the consumer. Or they may merely find a way to increase the supply of the same product or service. In any event, now they have increased the supply of the product for the consumers. The suppliers now find that they cannot charge such high prices because there are more **competitors** for the consumer's money. In this case the supply gets higher and the price gets lower.

When supply gets too high for the demand, business owners drop prices in order to attract consumers. Businesses work hard to make enough sales to cover their costs and then make a **profit**. And some companies may even be forced to go out of business if consumers do not buy from them at a price that will cover their costs and also make a profit.

Businesses also must try to keep their costs as low as possible in order to make a profit. One of the highest costs of providing a product or service is the cost of workers. **Human capital** is the economic term for the people that produce a product or service. An increase in the amount of work produced by the workers without an increase in pay leads to an increase in productivity for the business. The resulting **high productivity** keeps the costs per item low and helps increase profits for the company.

Let's Speak "Economics"

This activity is designed to encourage students to think about business using economics perspectives and language. Read the following case, and then, in small groups, discuss the questions at the end of the story using the economics terms explained on the previous page.

In 1999 the U S economy was experiencing prosperity, and many businesses were experiencing a problem with finding enough workers. George and Jean were trying to decide whether to quit their jobs and start a new business that seemed very promising. They wanted to match the need for workers to the need that some low skilled, inexperienced potential workers had to find work. They owned a rental building in one of the low rent districts in a large city on a main bus route, and felt they could open a business there.

Jean would be responsible for selling their services to companies throughout the area. George would manage the office, finding the potential workers, arranging for them to be driven to work and paid each day they worked, and filling out all the company paperwork.

The only competition for this type of business in the area did not provide transportation to the job and return and did not pay their workers daily. The office for the competition was located in the center city, about 4 miles from George & Jean's location. They ask your advice on the potential for success.

1. Describe the market for the company
2. What fixed costs would they have?
3. What variable costs would they have?
4. What prices should they charge their customers?
5. How many employees would they need? How many would be full time and how many would be temporary?
6. How could they encourage productivity?
7. How would you sell this service to potential clients?
8. How does the law of supply and demand affect this type of business?
9. How do they attract potential workers?
10. What are the major risks of this type of business?
11. What is the potential for profit from this type of business?
12. What advice would you give them about starting the business?

SHARE THE IDEAS FROM EACH GROUP. Then discuss how economics affects business decisions.

Did you notice this interesting language? It is a little like economics terms are to many people.