

ECONOMICS USA
PBS PROGRAM #2

MARKETS: DO THEY MEET OUR NEEDS?

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AIRSCRIPT
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2. MARKETS AND PRICES: DOES THE FREE MARKET RESPOND TO PEOPLE'S NEEDS?

PURPOSE:

To show how a well-functioning free market pricing system determines how producers manufacture goods, what goods will be manufactured, and for whom the goods will be produced.

OBJECTIVES:

1. The meeting of buyers and sellers in a market can be represented by supply and demand curves. The curves show what sellers (buyers) are willing to sell (buy) at various prices. In a perfectly operating market the intersection of the supply and demand curves will be the point at which buyers and sellers agree on the price and quantity.
2. Goods are produced by using resources such as labor, machinery, and materials. The prices of these resources are set by supply and demand in the free market, and the producer is forced by competitive pressures to choose the method of production, which is least costly, i.e. the method which conserves high priced materials.
3. Consumers "reveal" how much they want a good by the way they spend their money. If a great deal of money is being spent on a certain good, producers will try to make more of that good. If consumers change the way they spend their money, producers will respond.
4. There is a difference between "need" and "effective demand." The market system only responds to those who have money to spend. The poor have the need for many goods that the free market system will not provide for them, because the market system only responds to needs that people spend money on.

KEY ECONOMIC CONCEPTS:

supply and demand curves
shift in demand
equilibrium price and quantity

methods of production
market failure

ILLUSTRATIVE EVENTS:

1. How the rise in the price of homes and the change in buyers tastes caused builders to change the types of units they built
2. The rise of steel mini-mills which used low cost production methods
3. The creation of the Food Stamp program to provide basic necessities for the poor

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Final Transcript

Annenberg/CPB Project (Logo and Music)

TEASER

DAVID SCHOUMACHER: World War II was over. The GI's were home, raising the roof and hoping to raise a family. But how could they realize the American dream...a home of their own? When foreign steelmakers were pricing America's largest steel mills out of the market, how could a minimill hope to compete? Baseball...for millions a pastime, for a few, a paycheck. Why was the paycheck of this man half a million dollars a year?

A visit to a modern shopping center yields a bewildering display of goods and services...the products of a free market. But who's to say that any of this is what we want or what we need? Markets: Do They Meet Our Needs? With the help of economic analyst Richard Gill, we'll examine that question on this edition of Economics U\$A. I'm David Schoumacher.

(MUSIC PLAYS – OPENING TITLES)

(MARKETS: DO THEY MEET OUR NEEDS? appears on screen.)

PART I

DAVID SCHOUMACHER: The American economy, the sum total of what goes on in shopping malls, car dealers, supermarkets, stock exchanges, 7-Elevens, and gas stations all around the country. .Millions of buy and sell decisions every day...trillions of dollars worth every year...and those decisions affect every part of our lives from the cars we

drive to the homes we live in. But how are those decisions made? Who decides between a room with a view and a house in the suburbs? In our demand and supply economy, who demands and who supplies?

1945. World War II was over. Millions of x-GI's came home, fell in love, got married, and started families. And there was one thing they all needed...

VETERAN: "Well, of course when I got out of the service I had a young wife and primarily we wanted a place to live. It was like looking for a needle in a haystack...and eventually we found a place...a converted house where the upstairs was converted into an apartment."

DAVID SCHOUMACHER: In 1947, Judge Paul Widlitz was an x-GI and a young Long Island lawyer starting out.

JUDGE PAUL WIDLITZ: "We had the normal problems that you would have when they convert a one-family house to a two-family house and put steps going upstairs...where every time you walk it's heard down below or every time somebody cries upstairs...the baby...when it's heard down below."

DAVID SCHOUMACHER: Newman Baum and Jerry Worthing were also in the flood of x-GI's with young families, combing New York for a place to live.

NEWMAN BAUM: "I left the service in November, 1945 and one of the first things I had to do was to renew my love-life and get married to Helga...but we had to have a place to live. We lived in a furnished room in a single family house, and we had to eat every meal...3 meals out."

JERRY WORTHING: "When we got married, there were very few houses around to rent. We lived in the same house with my parents...then oh, a little more than a year later, we decided, well, we ought to look around and buy a house."

DAVID SCHOUMACHER: Families needed homes. But homes were not easily come by. Depression and war had put homebuilding on hold for almost 20 years. What housing there was was not cheap...beyond the means of most young vets with new jobs and new families. Young families were looking for low-cost housing...Homebuilders needed customers. It was demand in search of supply. For most people the American dream included a house and a car. Henry Ford had made the dream come true for cars. Were there any Henry Fords in the post-war homebuilding business?

WILLIAM LEAVITT: "We believe that every family in the United States is entitled to decent shelter. We believe that private enterprise should provide that shelter..."

KENNETH JACKSON: "The Levitt Organization, I think, was the most famous...It was the prototype...He was the Henry Ford of the housing market. They recognized the housing shortage which was so acute in the late 1940s..."

DAVID SCHOUMACHER: Professor Kenneth T. Jackson of Columbia University, a specialist in the history of the suburbs...

KENNETH JACKSON: "They built upon their experience in the 1930s...They built upon the experience of a couple of Levitts in building warworkers' housing. One of them worked with the Seabees in the Pacific in World War II. All of these things were teaching them how to really mass produce and build quickly."

WILLIAM LEVITT: "I remember distinctly saying to a lot of fellow officers there...'When this war is over, you beg, borrow or steal whatever you can and build housing because there's going to be a huge backlog...and it turned out. It was simple economics, that's all. People have to have roofs over their heads and there weren't any roofs being built."

DAVID SCHOUMACHER: Backed by the promise of VA and FHA mortgages, Levitt put his money where his judgment was. He laid out 6,000 lots on low-cost, Long Island

potato fields and poured 6,000 concrete slabs. Specialized construction teams hit Levittown streets like commandos.

WILLIAM LEVITT: “Instead of having a carpenter do all the carpentry...we specialized. He did only framing...Another carpenter only did roof rafters...we began delivering 150 houses every five days...approximately 18 before noontime and another 18 or 17 after noon.”

DAVID SCHOUMACHER: But as with the Model T, assembly line methods could mean assembly line sameness. In a nation dedicated to individualism, would mass production houses have mass appeal? The houses were built. The ads were placed. The case went to the jury. The verdict was not slow in coming in.

JUDGE PAUL WIDLITZ: “Housing...they needed a place to live. They were coming from all over the country...Coming out of New York and Brooklyn. All over the place they were coming out. Long Islanders were in the minority because they couldn’t get there fast enough.”

DAVID SCHOUMACHER: Newman Baum’s home movies captured the time for people like the Baums, the Worthings and the Widlitzs. New families in a new community.

WILLIAM LEVITT: “Regardless of what the place looked like, it filled a need for these young people that needed housing, needed roofs over their heads...”

KENNETH JACKSON: “For those people who moved to Levittown, and those people who moved to Levittown type developments in every major city in the country...it paid off financially. But the psychological payoff was perhaps even more important. It gave these families a stake in their community, a stake in their country. It gave them an anchor in kind of a restless and rootless world...a little piece of the universe that they could call their own.”

DAVID SCHOUMACHER: Scientists say that nature abhors a vacuum... Well, so does the marketplace. It was the unprecedented demand by World War II veterans for affordable housing that drew William Levitt and thousands of other builders into the low-cost housing market and built the foundation for post-war prosperity. We asked Richard Gill for an economic analysis of the forces that drew William Levitt and the World War II vets together.

(MUSIC IN – COMMENT & ANALYSIS I)

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RICHARD GILL: There was a large potential demand for housing in the post-war period and William J. Levitt supplied that demand. Simple question: How does the market system work? Simple answer: Through the great laws of supply and demand. If you go to a professional economist and ask how markets work, you are likely to get a somewhat more complicated response. Even worse, he's likely to draw you a graph. Not just a graph, but the graph... the most famous in our subject. The graph of supply and demand. And there it is. A fairly harmless looking contraption actually, though in fact it took economists quite a long time in the 18th and 19th centuries to come up with this particular diagram. So how would such a diagram help us with the Levittown story? First, what does the graph mean? We measure the quantity of product along the horizontal axis... in this case, number of houses. Along the vertical axis, we measure the price of that product... the price of an average single family home. Our demand curve is here, our supply curve is here. What the law of supply and demand tells us is that the price of the product will be determined where these two curves intersect. At a price of \$9,000 per home, the quantity of homes supplied and demanded in our diagram will be equal. Let us now show how the use of one of these curves clarifies the Levittown story. We have said that there was a great demand for housing in the post-war period as the veterans returned. But that way of speaking is too imprecise. What we really mean to say is that there was a great demand for inexpensive housing. The effective demand for housing in the market-place depends on the price of housing. And this is exactly what our diagram tells us in the simplest possible way. The DD curve slopes downward to the southeast. At a

high price here very few houses are demanded. It is only down here...at a low price...that the effective demand for houses is high. In a market economy, demand...and supply too...depend on price. These curves are nothing but the simplest possible expression of that important principle.

PART II

DAVID SCHOUMACHER: Steel is synonymous with strength. A thousand blast furnaces across America forged ribbons of steel into victory in war. For 75 years, U.S. steel producers had the steel market to themselves. They ran the big so-called “integrated mills”. They made their own steel from iron ore and processed it into a full range of products. They set their own prices and their own rules. In the 60s and 70s, as labor and energy costs rose, steel prices rose even more...until foreign steel began to underbid American steel on American buildings and bridges. In the U.S., plants closed...Workers were laid off.

STEEL WORKER: “Five thousand men laid off. I don’t see how we’d be able to get any more employment, in this area anyhow. I’ll probably have to leave.”

DAVID SCHOUMACHER: The market’s verdict on _ of a century of industrial complacency. What could be done to rebuild the faltering steel industry? With America’s biggest steel companies taking it on the chin, how could a small steel company compete? NUCOR was one of the Americans steel users which had turned away from high-priced American steel to foreign producers. But Kenneth Iverson, President of NUCOR, wondered if low cost steel couldn’t be made in America.

KENNETH IVERSON: “We went to Europe and we spent about 3 weeks roaming through a number of countries and steel mills to find out the way they produced steel and to determine...If we used those methods in the United States, could we manufacture steel as cheaply as we could buy it from overseas? We decided we could...We made a deal to buy this technology...And that’s the way we started in our first steel mill.”

DAVID SCHOUMACHER: Iverson rebuilt NUCOR as a steel minimill, using Europe's latest technology.

KENNETH IVERSON: "A minimill is defined as...First of all we're starting from scrap...We don't start from ore. Secondly, we melt it in electric furnaces and then we continuously cast it to come out with a billet that then is eventually rolled into the rounds, the channels, the flats, the smooth bars that we supply to customers. It's really much more economical than ingot casting."

DAVID SCHOUMACHER: Technology had helped NUCOR lower costs. But what about the cost of labor? The lower prices of foreign steel makers were based on lower wages. Could NUCOR make low price steel with highly skilled and highly paid American workers?

KENNETH IVERSON: "It's not what you pay an employee that's important...It's what he produces. And if he produces a great deal, you can afford to pay him a great deal...If he produces nothing, you can't afford to pay him a dime. The average hourly worker in Darlington, South Carolina, in our steel mill there, had earnings last year of more than \$30,000 a year...and we had melters who earned more than \$35,000...which compares reasonably with what unionized workers in the integrated mills earned last year. Now if you look at what we produced though, we produced last year some 850 tons per employee, where the average for the integrated producers was something like 350 tons per employee."

DAVID SCHOUMACHER: NUCOR wasn't the only steel company using minimill techniques to turn red ink into black. Dr. Robert Crandell, an economist with the Brookings Institution...a Washington D.C. thinktank...

ROBERT CRANDELL: "In the case of the steel industry, a small scale minimill industry is growing up to replace the much less efficient integrated firms. We are likely to

have...10, 15, 20 years from now...50, 75, firms, each producing 2 million tons of steel a year rather than these giant companies which may produce as much as 20 or 25 million tons a year. These smaller firms are more efficient. They'll produce steel more efficiently than the large companies and as a result ought to provide us with a healthier steel industry."

DAVID SCHOUMACHER: The high technology used in the minimill revolution couldn't save the whole steel industry. Steel for I-beams and auto bodies still must be made in the larger integrated mills...But there was a lesson the big steel companies could learn from the minimills.

KENNETH IVERSON: "If we modernize our steel mills, then we can have a steel mill that can compete with any steel company in the world. We'll have a somewhat smaller, but much more efficient and much more productive steel industry than we've had in the last 15 or 20 years. People in the steel industry...executives...say 'We can't compete.' And I don't care what reason they give...lower labor costs, government subsidies, more high, better technology, more efficient. That's not important. We can compete. We have all the elements here in this country to compete with foreign countries. We just have to realize that we can and dedicate ourselves to doing it."

DAVID SCHOUMACHER: For years the American steel industry assumed it was strong enough to sail through the market storm warnings, and it almost foundered. But NUCOR and other minimills paid attention to the signs and used new technology and creative management to follow the market's beacon to the high seas of higher profits. What kept NUCOR on the right course when its competitors lost the way? We asked economic analyst Richard Gill.

(MUSIC PLAYS – COMMENT & ANALYSIS II)

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RICHARD GILL: One of the most interesting things about markets is that they can produce the unexpected. They can stimulate innovations...new products or new ways of producing products. The introduction of the minimills in the steel industry was such an unexpected innovation. The supply and demand curves for our domestic steel industry in the 1970s looked something like this. Because of foreign competition, demand for domestic steel was low. We have illustrated this by placing our demand curve far to the left in the diagram. The price of steel was here, the quantity produced here, both low by historical standards. Why, we might ask, didn't the domestic steel industry simply lower its prices and sell more steel? After all, as we know from the Levittown story, the quantity of a product demanded usually increases at lower prices. The basic answer is that they couldn't expand like that because of costs. In most industries, as you expand your production, your costs tend to go up. This, in fact, is why we have drawn the supply curve for steel as we earlier did for houses, sloping upwards toward the northeast. Because of higher costs it isn't generally possible for business to supply more of a product unless they can get a higher price for it. Or unless they can lower costs. And this is where the minimills came in. The minimills lowered the costs of making steel and this produced a downward shift in the whole supply curve of domestic steel producers. Price now could be lowered and the quantity of steel produced domestically increased. Of course, minimills haven't been the complete answer to the problems of our woefully ailing steel industry. Such innovations do, however, represent an important way in which markets can respond to economic pressures.

PART III

DAVID SCHOUMACHER: Baseball...For the fans, a game...But for the players, a job. For the star, rare talents meant high pay, but for the average player or for the minor leaguer, it was a different story. Thousands of high school, college and minor league players were waiting in line to play "big league" ball. And like everywhere else, a big supply equaled low prices...starting minor league salaries, less than \$6,000 a year. Even in the major leagues, salaries were held down by a player's inability to take his services elsewhere. Then, in 1975, a contract dispute, an arbitrator's ruling, and the birth of the

free agent. It was a new ballgame. Most of us take for granted the freedom to look anywhere for a job and to negotiate for higher salaries, but for major league baseball that was a brand new idea. How would the first real players' market set salaries? Some thought the first test would come in New York, home of the team whose name was synonymous with winning baseball...the New York Yankees. The Yankees had had the proudest names in baseball...a seemingly endless string of Hall of Famer's...men like Babe Ruth, Lou Gehrig, Joe DiMaggio, Yogi Berra and Mickey Mantle. They had led the Yankees to a seemingly endless string of World Series titles. But with the great names gone, the Yankees had fallen on hard times. After 29 pennants in 44 years, winning had moved out of reach. Then, in 1972, George Steinbrenner came to New York. Steinbrenner, a wealth shipbuilding executive, was used to winning and to winners.

GEORGE STEINBRENNER: "I can't buy a newspaper or a loaf of bread anymore without paying a lot more than I used to...so,

DAVID SCHOUMACHER: So, how much would the wealthy Steinbrenner pay to bring winning baseball back to Yankee Stadium? \$300,000 for Catfish Hunter, after Hunter's contract was declared void on a fluke. And he hired the man some thought was the best manager in baseball, Billy Martin...the manager who could make winners out of losers. By 1975, attendance was up more than 50% and the Yankees were back in the World Series. But they lost that series...four straight...to Cincinnati's "Big Red Machine".

GEORGE STEINBRENNER: "That's alright. We're the second best team in baseball this year...That's nothing to be ashamed of, and it wouldn't do me any good to be critical of anybody right now."

DAVID SCHOUMACHER: Something was still missing...The Yankees still lacked what Ruth, DiMaggio, and Mantle had given them...a slugging outfielder who could put the ball into the seats and fans into the stands. In 1976, that meant Reggie Jackson, Jackson was clearly the biggest prize in that first free agent market. With 282 homeruns in 10

years, he had led the lowly Oakland Athletics to 3 straight World Series titles. Reggie Jackson was on the market and the Yankees were shopping. When the dust settled, Reggie Jackson was a Yankee. Then came the inevitable question, ‘How much did you get, Reggie?’

REGGIE JACKSON: “Well, now come on Maury, will you,

REPORTER: “I want to know how much you got.”

REGGIE JACKSON: “I don’t have anything to hide, Maury, but I believe that it’s offensive to talk about things of that nature, and things of that matter, and it’s very personal to me. My financial matters are my business...”

DAVID SCHOUMACHER: If Reggie wouldn’t tell, the papers would. Former Baseball Commissioner, Bowie Kuhn...

BOWIE KUHN: “Reggie puts people in ballparks. He has some of the elements of a Ruth...He has a certain strut and style that makes him a great ball player...He’s Casey at the bat. If he stays healthy, and you can play him enough...a problem with a better ball player...then you can probably generate this many extra people in your ballpark. Therefore, he is worth something.”

DAVID SCHOUMACHER: Steinbrenner’s investment paid off. Reggie Jackson took the Yankees to the World Series his first year in New York and this time they came out on top. The Yankees and Jackson were back in the Series 3 out of the 5 years of the contract Jackson and Steinbrenner had signed. Yankee home attendance, up over 100,000 in Jackson’s first year in New York...They even named a candy bar after him. The multi-million, multi-year contracts player’s sign today take our breaths away just as Reggie Jackson’s did back in the 1970s. It’s a lot of money for playing a game. But the calculations on both sides are strictly business...An employee offering a rare skill and a following of paying customers can demand a high salary. And when hiring an employee

means higher profits, most employers can see the higher salary as a good investment. But why is there such a difference between the incomes of different people? We asked Richard Gill.

(MUSIC PLAYS – COMMENT & ANALYSIS III)

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RICHARD GILL: Why does Reggie Jackson earn so much more than an economic analyst? Don't all raise your hands at once. The answer, sadly, is rather obvious. There are fewer Reggie Jackson's around and the product Reggie Jackson produces is more highly valued by the market. One important underlying lesson is this. The laws of supply and demand that we have been talking about in connection with the prices of products like steel and houses can also be applied to the prices of our services...our wages and salaries, our incomes. If public demand is high for certain kinds of rare skilled labor...long-ball hitters, rock stars, neuro-surgeons...then customers and employers will be willing to pay extra...in some cases, a great deal extra...for their services. In a market economy, supply and demand affect the prices and quantities not only of produces...but of the factors that produce products...labor, natural resources, machinery and other capital goods. A second underlying lesson is that the market, operating in this way, does not always produce a result we find personally agreeable. Should, for example, an agile 7-footer who can throw a ball through a hoop earn four or five times as much as the President of the United States? Markets are potent but not always ideal. Ask any economic analyst!

DAVID SCHOUMACHER: We speak of the market's decisions, but no market really makes any decisions. We...manufacturers, merchants, consumers, employers, employees...we make the decisions in response to the forces of supply and demand. The market takes our decisions, pulls them together and renders the ultimate judgment on economic success or failure...profit or loss. For Economics U\$A, I'm David Schoumacher.

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