

RESULTS FROM A NATIONAL SURVEY OF AMERICAN ECONOMIC LITERACY

William B. Walstad, University of Nebraska;
Max Larsen, The Gallup Organization

William B. Walstad, Department of Economics, University of Nebraska-Lincoln,
Lincoln, Nebraska 68588-0402

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The American public is confronted daily with economic issues related to such topics as unemployment, inflation, economic growth, Federal budget deficits, taxes, government spending, monetary policy, corporate profits, trade deficit, the value of the dollar, and many others. Unfortunately, most Americans know very little about economics. That conclusion is based on a national survey study that was jointly conducted by the National Center for Research in Economic Education at the University of Nebraska-Lincoln and The Gallup Organization (Walstad & Larsen, 1992).

The study had three basic objectives. First, it assessed the economic knowledge of the American public about basic economic topics that arise in discussions of the national economy and economic events. Second, it measured American public opinion on important economic issues that are frequently discussed by national leaders and the news media. Third, it documented the public's economic education, including formal coursework in economics and current sources of information about the economy.

Three national random samples were drawn in March, 1992. The first was a sample of 1,005 adults (weighted: n=1,006). The second was a sample of 300 high school seniors. The third was a sample of 300 college seniors. The margin of error in the responses of the adult sample was plus or minus (+/-) 3 percentage points. The margin of error in the responses of the high school and college samples was plus or minus (+/-) 5.6 percentage points.

ECONOMIC KNOWLEDGE

The American public, high school seniors, and college seniors showed significant deficiencies in their knowledge and awareness of basic economics. The general public correctly answered only 39% of economic knowledge questions on the survey. High school seniors were correct only 35% of the time. College seniors scored higher, in large part because some had more education in economics, but even this group could answer correctly only 51% of the basic economic questions.

Reported below are some economic topics included

in the survey and the percentage of the general public that could answer correctly the questions. The responses of high school seniors and of college seniors are not discussed below because of space commitments. Basically, those results show that high school seniors knew slightly less about economics than the general public, and that college seniors knew somewhat more. A summary of the results from knowledge questions for each group are found in Table 1.

Table 1: % of Correct Responses to Economic Knowledge Questions

Response	GP	HS	C
Unemployment rate	22%	10%	26%
Inflation rate	11	4	12
Inflation measure	35	35	56
Economic growth	40	37	56
Budget deficit definition	51	38	66
Budget deficit size	19	22	24
Federal Reserve purpose	46	38	58
Monetary policy set by	33	25	47
Monetary policy example	21	17	42
Fiscal policy set by	50	50	55
Fiscal policy example	23	28	48
Economic policy example	48	39	55
Productivity/wages	68	69	77
Purchasing power/inflation	60	53	81
Purpose of profits	36	42	52
Profit rate on investment	13	12	22
Supply & demand	64	72	79
Value of dollar/exports	50	38	61
Quotas and employment	49	37	50
Mean % correct	39	35	51

GP = General Public; HS = High School; C = College

Unemployment is an issue of great concern for the national economy and was important topic for the Presidential election; yet, only 22% of the general public knew the national rate of unemployment when the survey was taken. Thirty-nine (39%) thought the rate was much higher than it was, and 30% did not know the unemployment rate.

Inflation affects the level of prices in the economy

and the purchasing power of people's incomes, but only 11% of the general public knew the national rate of inflation when we surveyed. Thirty-four percent (34%) thought it was greater than it was and almost half (46%) did not know. Also, only 35% could identify the consumer price index (CPI) as the most widely used measure of inflation. Forty-six percent (46%) believed inflation was measured by the prime rate, the index of leading economic indicators, or the Federal funds rate.

Economic growth is vital for improving the standard of living in the United States. Just 40% of the public knew what is meant by economic growth. Sixty percent (60%) thought economic growth was assessed by a change in the producer price index, the money supply, the balance of payments or something else, rather than a change in the gross domestic product.

The Federal budget deficit is a worry for all Americans; yet only half the public (51%) recognized a correct definition of the Federal budget deficit. Forty-two percent (42%) confused the Federal budget deficit with the money supply or with the trade deficit. The remainder did not know. Also, most people had no idea of the size of the budget deficit. Only about one-in-five (19%) were aware of the expected size of the deficit for fiscal year 1992. It was estimated to be about \$400 billion at the time the survey was conducted. Sixty-three percent (63%) of the public incorrectly thought the size was \$700 billion and \$1 trillion.

The Federal Reserve is one of the nation's most important economic institutions because it is responsible for monetary policy. Just one-third (33%) knew that monetary policy was set by the Federal Reserve, not by the Congress, the President, or the U.S. Treasury. In further probing with another question, only 21% could identify a correct example of monetary policy (a change in the discount rate) despite the fact that changes in the discount rate make front-page news. Seventy-nine (79%) incorrectly thought monetary policy was a change in corporate profits, Federal government spending, or did not know.

Fiscal policy receives the constant attention of the President and Congress. Only half (50%) of the American public knew that the President and Congress were responsible for fiscal policy. Moreover, in another question, only 23% could identify a change in Federal income tax rates as a correct example of fiscal policy from a list that also included a change in the prime rate or a change in the discount rate.

Corporate profits are critical to the economic health of business and the nation. Just 36% knew the

basic purpose of profits in our economy. Half of the American public thought the purpose of profits was to transfer income to the wealthy or just to pay for the wages and salaries of workers. In addition, just 13% knew the percentage rate of profit as a return on investment earned by major American corporations. It has averaged about 13% percent for the past decade (range 10% to 16%). The average response of the American public was a 32% profit rate -- about two and a half times what it actually was.

The value of the dollar affects our international trade, but only half the American public knew how: an increase in the value of the dollar is most likely to lead to a decrease in U.S. exports. The other half thought it would increase exports, have no influence, or did not know.

Trade barriers are commonly thought to create jobs, but from an economic perspective they are not effective in increasing domestic employment in the long-run because they diminish world trade. Only 49% of the American public recognized this fallacy of protectionism. Forty-seven percent (47%) incorrectly thought that import quotas would increase the number of American jobs in the long-run.

Higher Knowledge Areas. In three questions, the general public showed a somewhat higher level of economic knowledge. These questions tended to be on topics that had the most direct effect on people's lives: wages, purchasing power, and prices. **Wages and Productivity.** About two-thirds (68%) of the public recognized that an increase in productivity was the factor most likely to increase the wages of American workers. **Purchasing Power.** Three-fifths (60%) understood that the inflation rate has the most effect on the purchasing power of people's incomes. **Supply and Demand.** Sixty-four percent (64%) understood that the prices of most products in competitive markets are determined by supply and demand and not by government, business monopolies, or the consumer price index.

Self-Evaluations. People were also asked for a self-evaluation of their economic knowledge. Among the general public, high school seniors, and college seniors, there was clear awareness of deficiencies in economic knowledge. About half of the respondents in each group would rate their understanding of economics and economic issues as only fair and about one-third would rate it as poor, on a scale that ranged from excellent to good to fair to poor. Thus, the self-evaluations show that over 80% of each group recognize a lack of economic understanding, and confirm the knowledge results that show that most Americans don't know much about economics and the national economy.

OPINIONS ON ECONOMIC ISSUES

All respondents had strong opinions about economic issues despite having limited economic knowledge. The discontinuity between economic knowledge and opinion can be illustrated with the following examples:

Unemployment. The dominant economic issue identified by the American public was the job market (unemployment) with 46% citing it as an important issue. The respondents recommended a number of actions that should be taken by the Federal government to reduce unemployment, such as a jobs training program or more public works projects. Nevertheless, only 22% of the American public knew the rate of unemployment and many (39%) were likely to overstate it or did not know (30%).

Federal deficit. The general public suggested actions to be taken by the Federal government to reduce the Federal deficit, such as increasing taxes on business (40%) or passing legislation to require a balanced budget amendment (78%). The American public may not fully understand the economic consequences of these actions because only 51% could define a budget deficit and only 19% knew the expected size of the budget deficit this year.

Supply and demand. Although many people (64%) recognized that prices are determined by supply and demand in a competitive market, even that understanding is shaky when opinions are asked. Given a situation where the supply of oil is reduced by a crisis in the Middle East, almost two-thirds (65%) wanted government to stop the price rise rather than let supply and demand determine the price.

Federal Reserve. Only a third of the general public knew that the Federal Reserve was responsible for monetary policy and even fewer could recognize an example of monetary policy, but two-thirds thought some organization such as Congress (38%) or the U.S. Treasury (13%) should be responsible for conducting monetary policy.

These results suggest that the economic knowledge base of the American public is sadly deficient for understanding or making decisions about most economic issues. Economic illiteracy has the potential to misshape public opinion on economic issues, and lead to policies that have negative or perverse effects on the economy and on our economic institutions.

Knowledge and Opinion. This last example on the Federal Reserve can be used to illustrate in more detail the effect of economic knowledge on public opinion. The knowledge question asked: "What is an example of monetary policy? Would it be a change in: (a) the discount rate; (b) a change in Federal government spending; or (c) a change in corporate

profits." Only 21 percent of the general public knew that a change in the discount rate was an example of a change in monetary policy. Despite this lack of knowledge, the general public answered the following opinion question: "Who should set monetary policy? Should it be the: (a) the President; (b) the Congress; (c) the Federal Reserve; or (d) the United States Treasury."

In Table 2, responses from the monetary policy knowledge and opinion questions are cross-tabulated. They show that there were significant differences in the support for the current institution that controls monetary policy in the United States -- the Federal Reserve -- based on respondents' correct or incorrect responses to the knowledge question. Among adults who could give a correct example of a change in monetary policy, 41 percent thought monetary policy should be set by the Federal Reserve. Among adults who gave incorrect examples, only 16 percent thought that monetary policy should be set by the Federal Reserve.

Table 2: Opinions on What Institution Should Set Monetary Policy by Knowledge

	<u>By Response to Question</u>		
	<u>Overall</u>	<u>Correct</u>	<u>Incorrect</u>
FED	21.0%	41.1%	15.8%
Other	79.0%	58.9%	84.2%
(N)	(1,006)	(207)	(799)

	<u>By Knowledge Score</u>		
	<u>Overall</u>	<u>> Mean</u>	<u>≤ Mean</u>
FED	21.0%	41.3%	12.4%
Other	79.0%	58.7%	87.6%
(N)	(1,006)	(298)	(708)

Shown in the lower half of Table 2 are the cross-tabulation of results from the monetary policy opinion question with overall economic knowledge scores based on the 19 economic content questions in the survey. The responses are shown when the knowledge scores are divided at the mean (>9 versus ≤9). Forty-one percent of adults with scores above the mean, but only 12 percent who scored at or below the mean, thought that the Federal Reserve should set monetary policy. The differences in opinions between high and low knowledge scores parallel the differences in opinions based on the correctness of response to a

single knowledge question related to the issue. Both analyses demonstrate that there are significant effects of economic knowledge on economic opinion, whether the knowledge is specific or general.

Other Examples. Similar cross-tabulations of opinion and knowledge questions on the Federal budget deficit, economic growth, government controls on gasoline prices, or trade protectionism could be performed to demonstrate the same point. For the sake of parsimony, only the knowledge scores and only the percentages not supporting a proposition are reported in Table 3.

Table 3: Opinions on Selected Economic Issues by Economic Knowledge Scores

(% Responding No to statement)

1. Reduce the Federal budget deficit by increasing taxes on business.	<u>Overall</u> 55.0%	<u>> Mean</u> 63.7%	<u>≤ Mean</u> 49.9%
2. Encouraging economic growth by increasing government spending to provide jobs.	<u>Overall</u> 29.3%	<u>> Mean</u> 43.6%	<u>≤ Mean</u> 23.3%
3. The U.S. government should prohibit an increase in oil and gas prices, if the supply of oil is reduced by a crisis in the Middle East.	<u>Overall</u> 31.8%	<u>> Mean</u> 48.1%	<u>≤ Mean</u> 25.0%
4. Limit imports from other countries to reduce a trade deficit.	<u>Overall</u> 29.3%	<u>> Mean</u> 49.4%	<u>≤ Mean</u> 20.8%
(N)	(1,006)	(298)	(708)

In the case of the Federal budget deficit, 55 percent of the public oppose increasing taxes on business to reduce the deficit. Among those with more economics, the opposition is stronger compared to people with less knowledge (64 percent versus 50 percent). Even larger differences (20-29 percentage points) were found between high and low knowledge respondents on issues concerning economic growth, government intervention in oil and gas markets and import quotas, as also shown in Table 3.

The findings from the survey of American economic literacy suggest that knowledge factors must be used in interpreting public opinion on economic issues. Most economic issues require a minimal amount of economic knowledge for people to understand, but too often survey results are presented only in the aggregate. Analysis of economic opinions is perhaps best performed by sorting responses by knowledge. Among the informed, of course, there will still be differences of opinion about what should be done on an issue, as the examples above illustrate, but the knowledge breakdown gives better insight into public opinion. This analysis is especially important on public issues that require knowledge of the subject.

EDUCATION IN ECONOMICS

The survey also asked people questions about their economic education. The answers both substantiate and explain the problem of economic illiteracy in America.

Education. The low evaluation of economic knowledge stems from deficiencies in prior economic education. Only 30% of the general public, 43% of high school seniors, and 40% of college seniors reported taking an economics course in high school. Only 20% of the general public have taken an economics course in college.

Information. Most information about the economy comes from the news media. The source cited most often by all groups was television (70-79%). The second major source of information was newspapers, but this source was read more by the general public (77%) and college seniors (78%) than high school students (62%). Media cited less often were magazines (14-27%) and radio (9-16%).

The problem with media information, especially for the general public, is that it is not sufficient for preparing people to think about economic issues. Without the formal economic education, what is read in the newspaper or seen on television is difficult to understand and is not meaningful.

High school seniors and college seniors recognized the contribution of education as a primary source of information about the economy. Almost four of five (79%) high school seniors cited school, an economic class, textbook, professor or teacher as important sources of information. The corresponding percentage for college seniors was 48%. In addition, educational categories were most often cited by high school seniors and college seniors as steps taken to understand economic issues.

CONCLUSION

The need for more education in economics was

recognized in all groups despite any differences in the sources of information about the economy. In fact, the only issue in the survey on which there was a near unanimous agreement (96-97%) among all respondents was that schools should teach more about how our economy works.

We are a nation that asks our citizens to participate actively in the affairs of the nation. When it comes to economic matters, most Americans are ill-informed and ill-prepared to participate because economics is not considered to be a vital part of the school curriculum. The recent calls for national reform of education gives strong attention to the need for such subjects as math, science, English, history and geography. There is no mention of economics as one of the subjects that is critical for schools to teach. The cost to the nation of this oversight is continuing economic illiteracy and great confusion among the American public -- young and old -- about how the economy works.

Survey researchers should also be more attentive to the effects of economic knowledge on public opinion on economic issues. People will state an opinion about an economic issue despite having no knowledge of the topic. Reporting only overall responses can mask significant differences in informed and uninformed opinions, and has the potential to mislead policy makers on economic issues.

REFERENCE

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