Spring 2012
Auto Industry Looks to Accelerate
Kevin Clark

Since the introduction of the Ford Model T in 1908, the world has never been the same. Society now has more efficient means to get from point A to point B. The Model T only opened the door for what was to come from the automobile industry. However in the recent past, the automobile industry has frequently found itself fighting harsh economic times. Today, General Motors serves as such an example being bailed out by the federal government. However in light of all the hardship, the automobile industry has always managed to recover.

The automobile industry has been the beneficiary of growth for the majority of the 1990s. The economic status of the automobile industry appeared strong until the recession of the late 2000s. The recession caused a drastic falloff in the sales of automobiles. Total sales of passenger cars from 2008 to 2009 dropped nearly 20%, with domestic car sales taking the majority of the hit. General Motors’ faced bankruptcy in 2009 and received funds from the government to maintain business. As a result, GM experienced greater difficulty than its competitors sustaining revenue. Due to the foreign automobile completion, American companies needed to make immediate...
improvements. In order to jump start sales and meet the demands of a developing green economy the Obama administration passed the Car Allowance Rebate System, which allowed individuals to trade in their old cars for newer, safer, and more fuel efficient cars. This took place during the second half of 2009 and resulted in many new car sales. As you can see by the graph, domestic car sales rose. Just as the automotive industry was reviving, a natural disaster literally shook the industry. Some companies experienced the wrath more severely than others. Japan suffered a devastating earthquake in 2011, which put Japanese production at a halt. Though unfortunate for the Japanese, this particular natural disaster proved beneficial to the American auto producers, evident by the 27.5% boost from the previous year. Data shows that Japanese production in the U.S. only increased by 7%, potentially attributed by the shortage of parts coming from Japan due to the earthquake.

The United States auto industry bounced back with the “Detroit Three” (GM, Ford, and Chrysler) staging monumental comebacks. The momentum continued from 2011 to 2012, with auto sales in January of 910,000, an 11.2% increase from the previous year. In 2012, GM continues to roll, earning $7.6 billion dollars in 2011.

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Real Unemployment
Daniel May-Rawding

Sometimes people question the significance of the unemployment rate. However, any individual with an introductory understanding of economics knows that when people are employed, they are more willing to spend their salary, and this is the essential foundation of any industrialized economy.

Similar to an old waterwheel, the flow of money turns the wheel of our economy creating power for our nation. When there is a labor drought and high unemployment, there is typically less money cycling to power our economy. Our current unemployment rate has fallen all the way from 10% to 8.3% following our most recent recession. The unemployment rate attempts to depict the true percentage of the labor force population that is not employed. This figure does not show the full extent of how many Americans are truly out of work. People who are out of work and have not been actively seeking work are considered discouraged workers. Such individuals are not included in the labor force and thus are not counted in the unemployment rate. This implies that the actual unemployment rate consisting of all able body workers would be higher than 8.3%. If the discouraged workers were included in the unemployment rate, it would be closer to 11%. This means that the true number of Americans who are out of work is not accurately displayed by the unemployment statistics. These Americans do not have income to spend, leaving them in more painful financial situations.

The reduction in unemployment is a crucial factor in the recovery of our economy. For us to create wealth, people need to have jobs and opportunity. Then the wheel of our economy can start turning faster once again. Actually, if you add those who are unable to work for economic reasons, and those who settle for part-time rather than full time, the unemployment rate goes to 16%.
Real GDP increased at a rate of 3.0% during the fourth quarter, compared to the third quarter, which experienced an increase of 1.8%. The Bureau of Economic Analysis defines real gross domestic product as "the output of goods and services produced by labor and property located in the United States."

According to the Bureau of Economic Analysis, there was a drop in government spending at all levels and an upturn in imports. These changes slowed down the growth of real GDP during this quarter. Real GDP soared in response to improvement in the sectors of personal consumption expenditures, private inventory investment, residential and nonresidential fixed investment, and exports.

The acceleration in real GDP was stimulated by exports, household expenditures, and business investment.

The final sales of computers, adding 0.12 percentage point, and motor vehicle output, adding 0.22 percentage point, contributed GDP growth. The gross domestic purchases price index rose 1.1% this quarter and increased 2.0% in the previous quarter.

Household purchases of durable goods, non-durable goods, and services all surged from the previous quarter. Real nonresidential fixed investment increased at a decelerated rate during the fourth quarter, dropping from 15.7% to 5.2%. Structures, equipment, and software all affected the change in nonresidential fixed investment products. On the other hand, real residential fixed investment continued to increase, from 1.3% to 11.6%.

Exports increased by 2.7%, however imports of goods and services climbed 3.7%, compared to a third quarter of 1.2%. Thus, the United States imported much more this quarter than the previous. Government consumption and investment at the federal, state, and local levels dropped in a dramatic twist from the last quarter, in which consumption actually had risen. From increasing by 2.1% in the third quarter, this quarter declined at a level of 6.9%. National defense was among the attributing factoring that contributed to this decrease. Ironically, non-defense spending actually increased compared to a decreasing third quarter.

On a more positive note, real private inventories, which had a pessimistic showing during the third quarter, added 1.81 percentage points to real GDP. So when all is said and done, real GDP continues to rise which is a good sign for our economy.
Greek Bailouts:
Drawing Blood from a Stone?

Michael Yatison

On Tuesday February 21, the European Union, the ECB, and the IMF agreed to a second bailout package for Greece worth 130 billion Euros (172 billion US dollars). Greece’s government agreed to pass further austerity cuts to receive the bailout and agreed to target a debt to GDP ratio of 120% by 2020. Mark Gilbert from Bloomberg reported the move helped calm investors’ fears of a Eurozone collapse and helped drive down borrowing costs in Spain and Italy. The ten-year yield for Spain dropped to 5.08% from its 2011 average of 5.4%, and the yield dropped in Italy to 5.4% from its December peak of 7.1%. While the bailout helped calm the markets in the short term, many economists, from both the right and the left, agree that the bailout and the terms have little long term sustainability for Greece and that the Eurozone is simply a quick fix that delays any real solutions to the economic crises.

Greece’s economy has only worsened since the first bailout of 2010, worth 110 billion Euros. As a result of the global financial crisis, the Greek economy first hit recession in 2009 and has not been able to climb out since. According to Greek government statistics, the unemployment rate has nearly doubled since the first bailout. From April of 2010 to December of 2011, the unemployment rate climbed from 11.7% to 20.9%. In addition, government statistics show that GDP growth has been negative since the first bailout was passed. 2011 fourth quarter GDP fell at an annual rate of 7% from the previous year.

Many economists agree that the second bailout and the resulting cuts imposed “An Economy Crumbles,” explains that the bailout will not work because of the current noncompetitive nature of the Greek economy. Currently, experts suggest that it is difficult for other countries to do business with Greece. In fact, the World Bank ranked
Greece 100th out of 183 countries for ease of doing business. The government imposes burdensome regulations on businesses, which discourage investment in the country. Additionally, the tax system in Greece is notoriously leaky. Many Greeks simply dodge paying taxes and can easily bribe officials to “cook the books.” The author of the article also attributes the lack of competitiveness to the uncertainty caused by the crisis. Businesses are simply unsure if Greece will remain in the Euro for the long run and have avoided doing business in Greece as a result. Paul Krugman of the New York Times, in the article “Keynes was Right,” argues that austerity during recessions will only worsen the Greek economy.

This is evident by noting that Greece’s economy has only gotten worse since the first bailout recession. Krugman argues that the major cuts imposed by the Greek government are causing consumption and investment to fall due to a drop-off in effective demand. Greece has been spending less money on its people since the austerity cuts. Public sector workers have been laid off and forced to accept pay cuts, education and health care spending have been cut and pensions have been slashed. A drop-off in government spending causes people to feel poorer due to a weaker safety net. As a result, people tend to save money in the economy, lowering consumption. With less customers (including the lost government spending), businesses are less likely to invest and are more likely to produce less goods and services, further driving down GDP. With a smaller GDP and a smaller tax base, Greece’s debt is likely to balloon as a result of the austerity measures.

There are two popular alternatives to the Greek bailouts. One of these alternatives is the departure of Greece from the Eurozone back to its original currency (the drachma) and default on its loans. This path would theoretically give Greece the power to inflate its way out of the crisis by regaining the power to print money. However, according to Landon Thomas of the New York Times, this option would lead to dire consequences. UBS predicts that a return to the drachma would lead to an almost immediate 60 percent devaluation of the drachma. The anticipation of a severe devaluation would cause investors, citizens, and bank account holders to flock to other currencies to protect the value of their assets. Additionally, the Greek government would find it next to impossible to finance any further debt, since most financial companies would avoid doing business in Greece. Thomas suggests that a return to the drachma could ultimately lead to hyperinflation, unrest, and possibly civil war.

The other major alternative would be difficult to achieve in the short term. This would be to “federalize” Europe. A fully federalized Europe would theoretically be able to bail out Greece, provide “federal” aid to the Greek people, and calm investors’ fears of the long-term sustainability of Greece in the Eurozone. The Eurozone has already taken steps towards this path. Angela Merkel, Chancellor of Germany, has called for fiscal integration by giving the E.U. the power to apply a debt brake on countries. This would effectively give the E.U. the power to reject budgets of Eurozone members if they exceed a certain percent of GDP. Carsten Volkery of Spiegel argues that the proposal has too many legal barriers to overcome and would have little impact on the Greek crisis today.
The Global Economy and Entrepreneurship
Roxanne Pennington

It may not be obvious to some, but entrepreneurship has been a driving force behind the development of the world’s growing economy and increasing technological innovation. An entrepreneur is someone who can take an idea or a product and turn it into a viable and profitable business plan. More than that, an entrepreneur is one who can effectively execute and carry out that plan. Those with entrepreneurial minds are important to our global expansion and we can see examples of their efforts all over the world; in fact the most important and prominent companies in today's international markets are entrepreneurial start-ups. Take for example companies like Google, Apple, E-bay and the entrepreneur golden child Zack Zukerberg and his start-up Facebook. All of these companies have changed the face of how the world interacts and how we get business done. Without great innovators and thinkers, like Steve Jobs or even Henry Ford, the quality of life world-wide would not resemble what it is today. You also have to consider how many people are employed by these companies and how they drive local economies. In fact small and medium enterprises account for 60-70% of employment in 34 of the leading and economically stable countries in the world. The Organization for Economic Co-operation and Development (OECD) has conducted extensive research on the interdependence of entrepreneurship and the global economy. In one of their more recent publications, they clearly stated the importance of the spirit of entrepreneurship in individuals and firms alike:

"Technological progress is not translated into economic benefits ... but by innovative firms. Innovative firms are not superior algorithms to maximize production functions, but efficient learning organizations that seize technological and market opportunities creatively in order to expand production frontiers. The single most important finding of recent economic research might be that new evidence from longitudinal microeconomic data reveals that firms that innovate more consistently and rapidly employ more workers..."²

Before moving on, it is important to clarify how entrepreneurship is measured in an economic sense. The above statements show their effects in a more business management perspective. The OECD–EIP has gone to great lengths to create a measureable and comparable scale to effectively create indicators of entrepreneurship, so that proper policy can be made. One of the biggest issues they had from the get-go was to determine factors to which all countries within the OECD spectrum could relate. They relied heavily on the National Statistic Offices; however there is too much information for the results to be high in quality so they relied on monthly and quarterly register-based statistics. Admittedly some drawbacks of this approach are that having a single source causes limits and incomplete information for employment. Another is that is doesn’t allow for a single legal definition for ‘start-ups’, ‘creation’, and ‘failure’ concepts related to the entrepreneurial process and business growth cycle.

With these methods identified, we can move on to looking at the statistical effects that the global economy and entrepreneurship have on each other. In the graph to the right you will see a variety of countries and the percentage change in enterprise creation for years 07-08 and 08-09. You’ll notice that a majority of the countries had deep cuts in enterprise start-ups, especially those that practice austerity. Those countries that saw growth in 08-09 either were spending money to get out of their
and acquisitions, where entrepreneurships could combine with well-established companies to gain funding. This option was just as risky. In 1994, OECD recorded that there had been an annual total of $90 billion spent in venture capital, so it is easy to see how this trend can lead to a terrible downward spiral. The cycle continues, causing more and more uneasy feelings about any kind of participation in entrepreneurships. Since start-up companies depend on venture capital and loans to fund their operations, these events cut the legs out from so many start-up companies. Those who had begun their businesses were stuck with a lot of fixed costs (land, machines etc.) and nothing to show for it.

When one considers all of these elements, along with long term effects of tightened regulation and new government policy limiting new enterprise growth, it is easy to see how the world, as a whole, will suffer. Not only is there a global economic trauma, but also a lack of innovation and groundbreaking spirit. It is evident that the global economy and entrepreneurship are tightly wound together and greatly affect each other. Eventually there will be someone, somewhere who will break this cycle and begin circling back towards expansion, allowing for more people to carry out their ideas and business prospects. Sadly we will likely have to wait until economies around the world over begin to see serious improvement.

References:
It’s no secret that the majority of the products we use on a daily basis gets manufactured somewhere outside of the United States. I can probably bet you that one in every ten items you use daily has a tag that says, “Made In China” or the name of another foreign country. Most of our economic classes teach us about supply and demand and why we import and export with other countries. But unless you do independent research or a professor shares a little personal knowledge, we don’t know to whom or what the U.S. trades.

Lets start with our northern neighbor, Canada. As of August of 2011, the U.S. trade with Canada has been on a slight decline. Despite the decline, the U.S. Census Bureau has Canada listed as the top trading country for the United States, with a little over $48 billion in combined imports and exports. The only problem with this number is that there is nearly $5 billion more in Canadian imports than U.S. exports to Canada. Those are the numbers, but what is so significant about Canadian imports? Well, to say the least, Canada is the single top foreign energy supplier for the U.S., providing close to 40% of oil and natural gas imports.

Enough about Canada though, the even bigger picture is the Trade Agreements with other countries. The U.S. Department of State acknowledges 9 Free Trade Agreements with a total of 14 countries, which excludes the progress of implementation of four more FTA’s between six countries. To get a better picture, some of these countries include Australia, Columbia, Israel and 6 of the Central American countries.

So now that I covered the basics of whom the U.S. trades with, the last question remaining is, what is traded? Germany and Japan top the leader board when it comes to automotive imports, reaching almost $60 billion in 2010. Crude oil is another large import, which mostly comes from Canada, Saudi Arabia, and Mexico. Although we import most of our crude oil supply, the U.S. also exports a fair share of crude oil to
other smaller countries. Our country isn’t just about imports (although numbers favor imports) the U.S. is the world leader in exporting aerospace parts, airplane assembly and military equipment. Some other key U.S. exports include automotive accessories, agriculture, and steel (which is highest in Pennsylvania).

To sum up the story, the U.S. is one of the top international trading countries, with nearly $2.5 trillion of combined imports and exports each year. Not only does the United States provide for others, others provide even more for the United States.

The Latest on the Consumer Price Index
Godfried Osei Twumasi

The consumer Price Index, reported by the Bureau of Labor Statistics, showed that Consumer Price Index for the Philadelphia, Wilmington, and Atlantic City areas upturned 0.7 % from December of last year to February of 2012. The Graph below shows all items less food and energy index that average% growth 1.6 since February 2011.

Food prices decreased by 0.2% last October to December, but later rebounded 0.2% over the last two months. This made domestic and foreign food prices each rise 0.2%. For instance, prices for cereal increased while prices of food, such as pork, dropped .Overall, the food index rose by 2.5%, with foreign food prices predominantly responsible for the change. Also, the energy index for household and transportation fuels augmented 3.8% from December to February, triggered by higher gas prices. Energy prices for electricity and utility gas service went down 2.5% and 1.6% respectively. This is known as core inflation. BLS reported “the index for all items less food and energy increased 0.3% from December to February” The February core inflation increase by 1.6%, despite education and communication prices indexes decreasing by 3.4%.
Tohoku Earthquake: Effect of Japanese Car Market in U.S.
William Hines

The earthquake that hit Japan’s Tohoku region, in March of 2011, has had repercussive effects on one of the largest production exports from Japan, automobiles. Tohoku is the basis for many of Japan’s global automobile producers (Toyota, Nissan and Honda), which took a heavy toll in the aftermath of the earthquake, tsunami, and the resulting power outages. The combination of these disasters accounted for about 1 trillion JPY (12 billion USD) worth of damages to the area and brought about a shortage in supply-chains for many of these companies. The colossal disaster created problems for Honda, in particular, with the recent announcement of a new Civic model at the 2011 New York Auto Show.

The company’s most popular model is covered in a cloud of uncertainty on possible problems with its availability. The damage done to parts and material factories in Japan adversely affected Honda’s assembly plants in the U.S. This is not good news for Honda, which has experienced less than stellar growth in U.S. sales, reporting only a 5% sales growth in 2010. As a result, Honda was replaced by Nissan as the number two Japanese automaker (Economist). In the last Japanese fiscal year, Honda’s operating profit dropped dramatically by 68% to 52.5 billion Yen ($683 million).

The Tohoku disaster could not have come at a more inopportune time for Honda, especially with the price of their cars in the U.S. skyrocketing due to supply shortages from the Japanese imports. The effects of the earthquake created a great opportunity for American and other carmakers to make a big push in the market with similar offerings from their companies (Ford Focus, Toyota Camry, Chevy Cruze, Nissan Altima). Honda’s share in the U.S. automobile market declined considerably, falling behind Chrysler in the past year.

It is clearly evident that the Japanese natural disaster is responsible for Honda’s recent sales woes and their current position in the U.S. car market. If Honda recovers and regains its former prestige as one of the most popular car companies, it will have to do so in a market that is fiercer than ever.

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Japan is the world’s 5th largest economy, with a GDP of $4.389 trillion (2011 estimate). A Japanese government stimulus helped the economy recover in late 2009 from the global economic crisis of 2008. As result of the earthquake, tsunami, and ensuing nuclear disaster, the economy quickly contracted again in 2011.

Japan has made headlines again within the past few weeks, with concerns over their rather large trade deficit – nearly 1.475 trillion Yen ($19 billion). For those keeping track, that is more than 50% larger than the 967.9 billion Yen deficit from the financial crisis in January of 2009. Shipments dropped 9.3% compared to the beginning of last year, and energy imports surged according to Japan’s Ministry of Finance. This can be attributed to the shutdown of nearly all of the country’s nuclear reactors. Utility providers were forced to turn to traditional power stations to generate electricity as a result. How do these power plants operate? They need natural gas and coal, which is why there is such a surge in imports of these commodities. Natural gas imports rose by 74% in January as compared to last year, and coal imports were up 26%.

Exports to China, which is Japan’s largest market, are down by an astounding 20%. This is the largest decline in exports since August of 2009. Shipments to Europe also declined by 7.7%, and shipments to the US advanced by only 0.6%. After the natural disaster in Japan, many companies, such as Toshiba, Sony, Honda, and Toyota, had to slow down or cease production of their goods. Electronics from Toshiba and Sony are used in everything from the iPad to televisions to automobiles. Without output from these companies, the manufacturers cannot produce these goods for the consumer. Just days after the disaster in Japan, the price of digital chips rose to $10, from $7.30 before the earthquake. Honda, a Japanese automobile manufacturer, had their quarterly profits plunge by 90% following the disaster.

A weaker Yen would benefit the Japanese economy, because foreign countries could afford to buy more of their products. A weaker Yen would be a beneficial starting step for Japan to alleviate its deficit. In addition, market watchers expect further asset purchases by the Bank of Japan, which would decrease the Yen’s value even more so.
This year is an Olympic Year. London is currently preparing for its hosting of the Games of the XXX Olympiad. The great event has taken place worldwide for over two centuries and has been practiced for thousands of years. But will hosting this great event bring economic stability to London and the United Kingdom? When Los Angeles hosted the 1984 Summer Games, the city turned the Olympiad into a profit for the first time in history, bringing in roughly $335 million in revenue. Do such revenues improve economic conditions to a country or region?

Tien, et. al (2011) conducted a study asking that question. In their study, they employed cross-sectional time series regression analysis to determine if the hosting of an Olympiad (both Summer and Winter Games) had an positive impact on GDP, unemployment, and investment in the host country. Nine years of data were collected in analyzing each of the Summer and Winter Games, starting with the Summer 1964 Games, to the Summer 2008 games.

Their study proved to bust the myth that hosting an Olympiad has positive, long term economic benefits to the host’s region. All three of the factors (unemployment, GDP, and investment in the host country) boasted positive results, but only in the Pre-Games phase. This results from the immediate need of temporary positions in setting up the great event. However, the Games and Post-Games phase showed no positive economic impact with the hosting the Olympiad. Does this mean that a country or city should not host the Olympic Games? Of course not. But they shouldn’t host and expect to come out with excess economic benefits.

References:
Recently, the subject of our national debt has been a major concern. Throughout the last century, the United States has been considered a major debtor nation, and recently the federal debt has been climbing to levels we have not experienced since the 1940s. During periods of economic recessions and times of war, it is common to experience increasing national debt. Currently, the national debt has hit a staggeringly large amount, and now the debate is whether to try to balance budgets in an attempt to lower the national debt or to continue spending to promote economic growth.

Historical data shows the United States has experienced periods of large debt due to wartimes and recession. At the turn of the 19th century, the national debt totaled about 20% of GDP. After World War I, federal debt rose to approximately 35% of GDP. During the Great Depression, President Roosevelt increased government spending to attempt to pull out of the depression, causing the debt level to rise to 70% of GDP. With the outbreak of World War II, excessive government spending was crucial for victory but ultimately increased national debt to 122% of GDP. For the next 35 years, the debt began to decrease to levels as low as 40% of GDP. In the early 1980s, President Reagan increased defense spending in the attempt to end the Cold War, which resulted in increasing of national debt to over 50% of GDP. Shortly after the Cold War, debt began to decrease slightly until 2001, when the War on Terror began. This was closely followed by the Iraq War, causing national debt to yet again rise. Adding to the already increasing level of national debt due to defense spending, the Financial Crisis of 2008 required a massive government stimulus to keep the struggling financial system functioning. As a result of two costly wars and a latest economic crisis, the current national debt has risen to 15 trillion dollars, nearly equaling the current gross domestic product.
Federal government deficits are also a contributing factor to the excessive national debt. The current federal deficit is roughly 1.3 trillion dollars or 10% of GDP. Throughout the last century, the main cause of large government deficits has been war. During World War I, the 1919 deficit was 16% of GDP. During the aftermath of World War II, the 1949 deficit rose to 24% of GDP. The deficits of the Great Depression only totaled to 5% of GDP. In comparison to the previous deficit to GDP ratio, the current deficit of 1.3 trillion is not as serious as it seems.

When comparing the current debt with other historically high debt levels, it now seems very similar to what was experienced during the Great Depression and World War II. The similarities between these two periods of war could explain why the debt levels are so comparable. Wars are expensive, especially when increased defense spending is accompanied by a major financial crash. We would expect the economic impacts to be similar and that debt will increase significantly.

Historical data shows that the large amount of government spending, during the Great Depression, revived the economy and stimulated growth leading to a decrease in debt. Data also shows that, even with the significantly large amount of debt caused during World War II, an economy can recover and create long periods of decreasing debt levels and government surpluses.

Overall, it is obvious that the debt issue in the United States needs to be addressed, but it may not be as serious as it sounds. By comparing the current data with historical data, the United States has been in this debt state before, and the situation was corrected, resulting in 35 years of diminishing national debt. A long-term plan needs to be established to address the issues of excessive government spending in an attempt to slowly reduce the debt, as well as allocating enough government spending to promote strong economic growth.
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