

Introduction to economics

Chapter 1: The challenge of economics

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Course objectives

On completion of the course, you will have the ability to:

- **Define** the concepts of Economics and Economics Education
- **Discuss** the importance of teaching Economics
- **Analyze** the challenges of teaching Economics

Lecture 1

Syllabus : The challenge of economics

**Definition &
Scope of
Economics**

**The
Foundation
of Economics**

**The Economic
Agents**

Summary

I- Definition & Scope of Economics

I-1- Some definitions of Economics

I-2- Nature of Economics

I-3- The top 4 definitions

I-4- The scope of Economics

I-4-1- The fields of Economics

I-4-2- The branches of Economics

I-4-3- Problem-Solving Approaches towards Economy

I-1. Definitions of Economics

Economics is essentially a study of the usage of **resources** under specific **constraints**, all bound with an audacious hope that the subject under scrutiny is a **rational entity** which seeks to improve its overall **well-being**.

Economics is the study of how individuals and societies choose to **allocate scarce resources**, why they choose to allocate them that way, and the consequences of those decisions.

Nature of economics refers to whether economics is a **science** or **art** or both, and if it is a science, whether it is positive science or normative science or both.

Science: any system of knowledge that is concerned with the physical world and its phenomena and that entails unbiased observations and systematic experimentation.

Art: expression or application of human creative skill and imagination

- **Economics as an Art of teaching**

Economics is an art that teaches us how to practically implement the laws of nature for the economic well-being of humans and its dependents. Economics tells us how to get out of the problem by implementing the science of Economics. Economics is purely a problem-based subject, be it personal or collective problems.

- **Economics as a base to Identify Problems**

Economics is based on identifying the problem and means to solve it; it can be positive or normative science of business

Economics is both **science** as well as an **art**

- Economics as Science
- Economics as Social Sciences

Samuelson says that Economics is **“the queen of the social sciences”**.



Economics and other subjects/sciences

Economics and philosophy

Should we be concerned with the ethics of the free-market or should economics be value-free?

Economics and politics

How do political pressures affect economists and economic theories?

Economics and psychology

How psychological approaches have challenged the traditional economic view of rational choice theory.

Economics and sociology

How social class and cultural factors affect micro and macroeconomic variables.

Economics and mathematics

How mathematical models are used to underpin economic models and theories.

Economics and physics

The use of physics tools in statistical analysis.

Economics and anthropology

How understanding human culture/society is important to economics.

Economics and biology

How biological science influences economics.

Economics and ecology

Widening economics from impact on humans to long-term environmental sustainability

« Economics is not an exact science. It's a combination of an art and elements of science. And that's almost the first and last lesson to be learned about economics: that in my judgment, we are not converging toward exactitude, but we're improving our data bases and our ways of reasoning about them. »

Paul SAMUELSON

Four definitions, each referring to particular stage of the growth of the subject of Economics, are presented here.

They are:

- a- Smith's **Wealth** Definition
- b- Marshall's **Welfare** Definition
- c- Robbins' **Scarcity** Definition
- d- Samuelson's **Growth** Definition

- a- **Wealth Definition** of **Adam Smith, the father of Economics** (the Classical era)

“Economics as a science which inquired into the nature and cause of wealth of Nations”.

- b- **Welfare definition** of **Alfred Marshall** (the Neo-Classical era):

“Economics is the study of man in the ordinary business of life”.

C- **Scarcity Definition** of Lionel Robbins (the New Age):

« Economics is a science which studies human behaviour as a relationship between ends and scarce means which have alternative uses ».

d- **Growth Definition** of Samuelson (the Modern Age):

Economics is « the study of how men and society choose, with or without the use of money, to employ scarce productive resources which could have alternative uses, to produce various commodities over time, and distribute them for consumption, now and in the future among various people and groups of society ».

Different Definitions Of Economics

WEALTH DEFINITION



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graph TD; A[WEALTH DEFINITION] --> B[WELFARE DEFINITION]; B --> C[SCARCITY DEFINITION]; C --> D[GROWTH DEFINITION];
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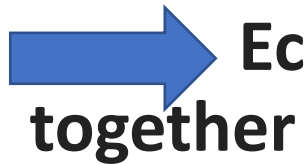
WELFARE DEFINITION

SCARCITY DEFINITION

GROWTH DEFINITION

I-4- The Scope of Economics

- **The scope of economics:** It's the boundary in which the field of study is contained.
- It is a science of human activities in day-to-day businesses
- It is considered an art of persuasion and dealings to buy or sell anything



Economy is the only subject that's considered a science and art

together

I-4-1- - The Fields of Economics

- Behavioural Economics
- Ecological Economics
- Environmental Economics
- Health Economics
- Information Economics
- International Economics
- Labour Economics
- Monetary Economics
- Population Economics
- Public Finance
- Urban Economics

I-4-2- The Branches of Economics

- Economics is divided into two different branches: Microeconomics and Macroeconomics.
- **Microeconomics** is the study of individuals and business decisions
- **Macroeconomics** looks at the decisions of countries and governments.

Meaning

Micro-Economics

- Micro economics studies the decisions made by individual and business concerning the distribution of resources and prices of goods and services.
- It deals with a specific industry or a sector, the connections of firms and households in the market.
- For example, microeconomics would study how a company could lower its prices to increase its product demand in the market.

Macro-Economics

- Macroeconomics, studies the behavior of not only particular company or industries but whole economy.
- It includes understanding how unemployment, price levels, growth rate affects the economy wide aspects such as the Gross National Product (GNP).
- For example, macroeconomics would look at how an increase/decrease in net imports would affect a nation's capital account.

I-4-3- Problem-Solving Approaches towards Economy

- Economics is studied by **two problem-solving approaches**:
 - **The traditional approach** is carried through the five basic principles of **Consumption**, **production**, **exchange**, **distribution** and **public finance**.
 - **The modern approach** is sub-divided into microeconomics and macroeconomics.

II-1- General problems of Economics

II-2- The Scarcity

II-3- 10 principles of Economics

II-4- The factors of Production

II-4-1-The Inputs

II-4-2- Goods & Services

II-The Foundation of Economics

Society has virtually **unlimited wants**...but limited or **scarce resources!!!**

There will always be a demand for **NEEDS** and **WANTS**.

Needs = required for survival

Wants = make life more comfortable and enjoyable

II-1- Central Problem of all Economies

- In case of any economy, whatever the economy required cannot be satisfied fully.
- **Economic resources** or means of production are limited and they can be put to alternative uses.
- Every economy faces some common problems.

II-2- The Scarcity

- **Scarcity** is one of the key concepts of economics.
- It means that **the demand for a good or service is greater than the availability of the good or service.**
- Scarcity can limit the **choices** available to the consumers who ultimately make up the economy.

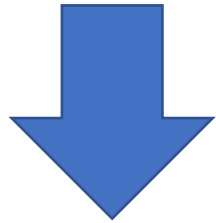
Gregory Mankiw in his **Principles of Economics** outlines Ten Principles of Economics that we will replicate here, they are:

- 1- People face trade-offs
- 2- The cost of something is what you give up to get it
- 3- Rational people think at the margin
- 4- People respond to incentives
- 5- Trade can make everyone better off

- 6- Markets are usually a good way to organize economic activity
- 7- Governments can sometimes improve market outcomes
- 8- A country's standard of living depends on its ability to produce goods and services
- 9- Prices rise when the government prints too much money
- 10- Society faces a short-run tradeoff between Inflation and unemployment.

II-4- The Factors of Production

- The **factors of production** are **resources** that are the building blocks of the economy.
- They are what people use to **produce goods** and **services**.



- The factors of production or **resources** are the **Inputs**.
- The **products** are the **Outputs**.

II-4-1- The Inputs

- Economists divide the factors of production into four categories:
 - **land**
 - **Labor**
 - **capital**
 - **entrepreneurship**

Factors of Production (Factor Inputs)

Factors of production are the inputs available to supply goods and services in an economy.

Natural resources
available for
production

Land

The human input
into the production
process

Labour

Entrepreneurs
organise factors of
production and
take risks

Enterprise

Goods used in the
supply of other
products e.g. tech

Capital



II-4-2- GOODS & SERVICES

- In each economy, we find **GOODS** and **SERVICES**.
- They are called **PRODUCTS**.
- The prices of products are largely determined by **the supply and demand of an economy**.
- What's the difference between them?
- What do they provide?

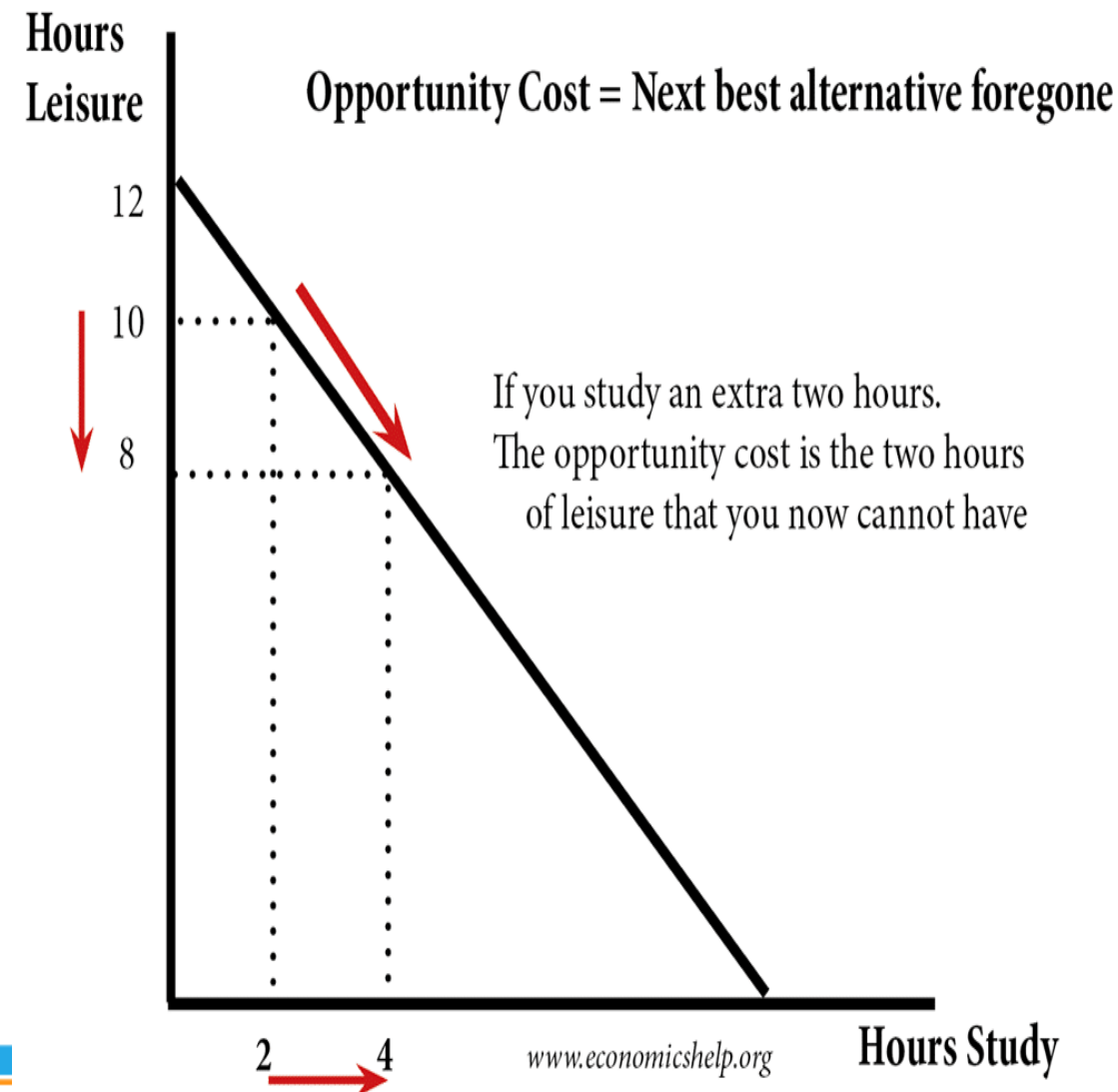
- **Services** are the **non-physical, intangible** parts of our economy, as opposed to goods, which
- **A Service** is a **transaction** in which **no physical** goods are transferred from the seller to the buyer.

- **Goods** are **material, physical, tangible** items that you can purchase.
- They are items that we can touch or handle
- There are 4 types of goods: **private goods, common goods, club goods**, and **public goods**.
- They vary in their level of exclusivity; that is, how many people can enjoy them.

- **Private Goods:** They're **excludable** Goods. The consumers cannot use them without paying for them. They are also **rival goods**, which reduces availability for other consumers, resulting in Scarcity.
- **Common Goods:** **non-excludable** Goods, so everyone can use them without paying. They are **rival**.
- **Public Goods:** Public goods are non-excludable and non-rival. They are available to everyone and are not in danger of running out.
- **Club Goods:** subtype of public goods that are **excludable** but **non-rivalrous**

- **Opportunity cost** is the next best alternative foregone.

- If you decide to spend two hours studying on a Friday night, The opportunity cost is that you cannot have those two hours for leisure.



- We can also classify them according to if they're free or economic Goods.

Free Goods	Economic Goods
A free good is a good with zero opportunity cost . This means it can be consumed in as much quantity as needed without reducing its availability to others.	An economic good is a good or service that has a benefit (utility) to society. Also, economic goods have a degree of scarcity and therefore an opportunity cost

Goods	Services
They can be seen and touched.	They cannot be seen and touched, but felt.
They can be stored.	They cannot be stored.
There is a time gap between the production and consumption of goods.	There is no time gap between the production and consumption of services.
Example: Pen, paper, notebook.	Example: teaching, medical care, plumbing.

III- Economic Agents

III-1- The economic decision-makers

III-1-1- The Households

III-1-2- The Firms

III-1-3- The Governments

III-1-4- The « Rest of the World »

III-2- Consumers Vs Producers

III- The Economic actors

Who makes decisions in the economy ?

- 4 (broadly defined) economic actors exist in each economy. They're its actors.
- Each one of these actors has a specific role.
- They are interdependent

1. Households: All those people living under one roof are considered a household.

Households do two fundamental things vital to the economy:

- **Demand goods and services** from product markets
- **Supply labor**, capital, land, and entrepreneurial ability to resource markets.

2. Firms:

They're Economic units, formed by **profit-seeking** entrepreneurs who employ resources to **produce** goods and services for sale.

3. Governments

- a. Establish and Enforcing the Rules of the Game.
- b. Promote Competition
- c. Regulate Natural Monopolies
- d. Produce public goods (goods that, once produced, are available for everyone to consume, regardless of who pays and who doesn't)

4. "The Rest of the World"

Rest of World means **all countries of the world outside the Territory.**

A- The Households will be what we call Consumers.

- A consumer is a **person who buys and uses goods and services**

Households are rational utility maximizers.

Economists assume that individuals, and thus households, attempt to maximize their utility.

B- The firms are the producers

- Producers **make the goods and services that are sold in the economy.**
- They also provide jobs for people who make the products or who provide the services.
- Producers include businesses, the government, and individuals.

One of the hypotheses of Economics is that Each Consumer and Producer is **rational**. They would not make choices that would make them worse off: they are **rational**.

Rationality

The decision-makers (customers and firms especially) act in their own best interest

- **Customer's** own goal
- **Producer's** own goal

Consumer's Goal

- maximizing his utility

Utility:

- The satisfaction received from consumption; the sense of well being.
- Utility is subjective (not objective).

Producer's Goal

- maximising his profit

Profit:

a financial gain, especially the difference between the amount earned and the amount spent in buying, operating, or producing something.

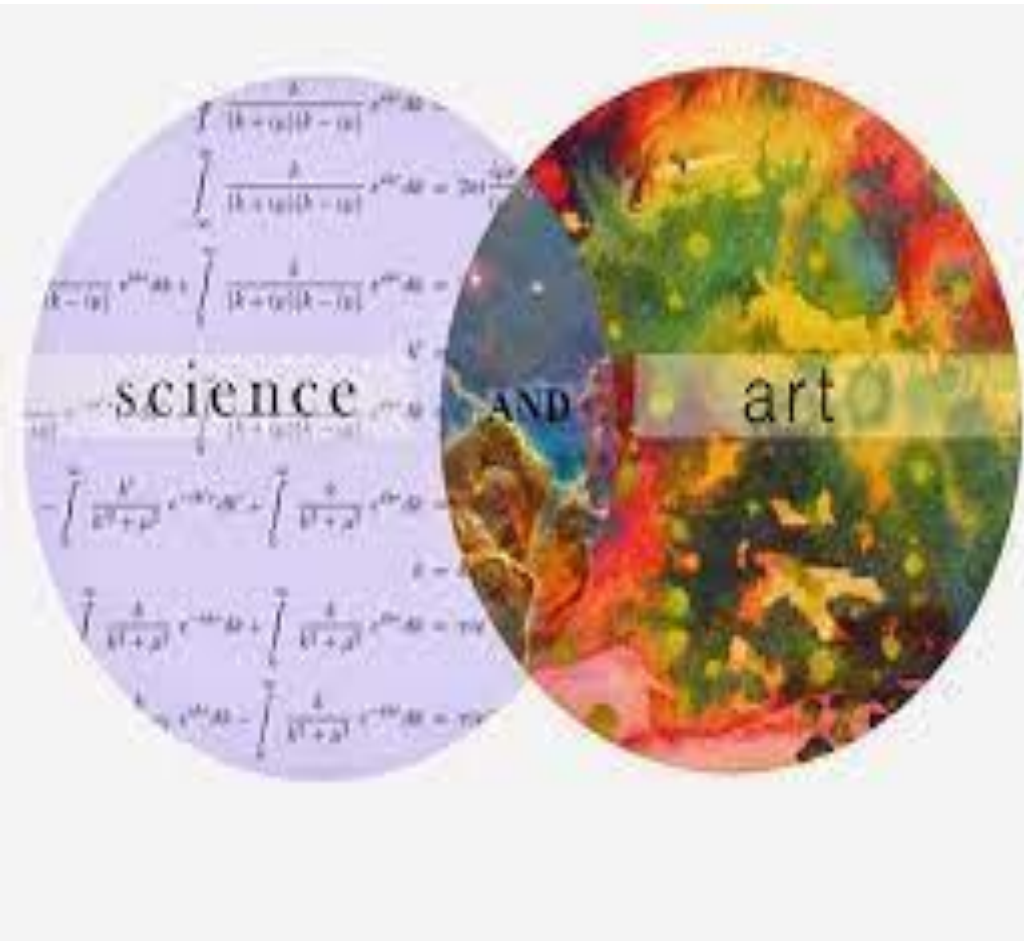
Review

Summary



Lecture 1

The nature of Economics -1-



NATURE OF
ECONOMICS

SCIENCE

ART

SOCIAL SCIENCE



Economics Definitions

Emphasis on	Contribution by
Wealth	Adam Smith (1723 – 1790)
Welfare	Alfred Marshall (1842 – 1924)
Scarcity	Lionel Robbins
Growth	Paul Samuelson

Lecture 1

The 2 branches of Economics -3-

Microeconomics

Individual markets

Effect on price of a good

Individual labour market

Individual consumer behaviour

Supply of good

Macroeconomics

Whole economy (GDP)

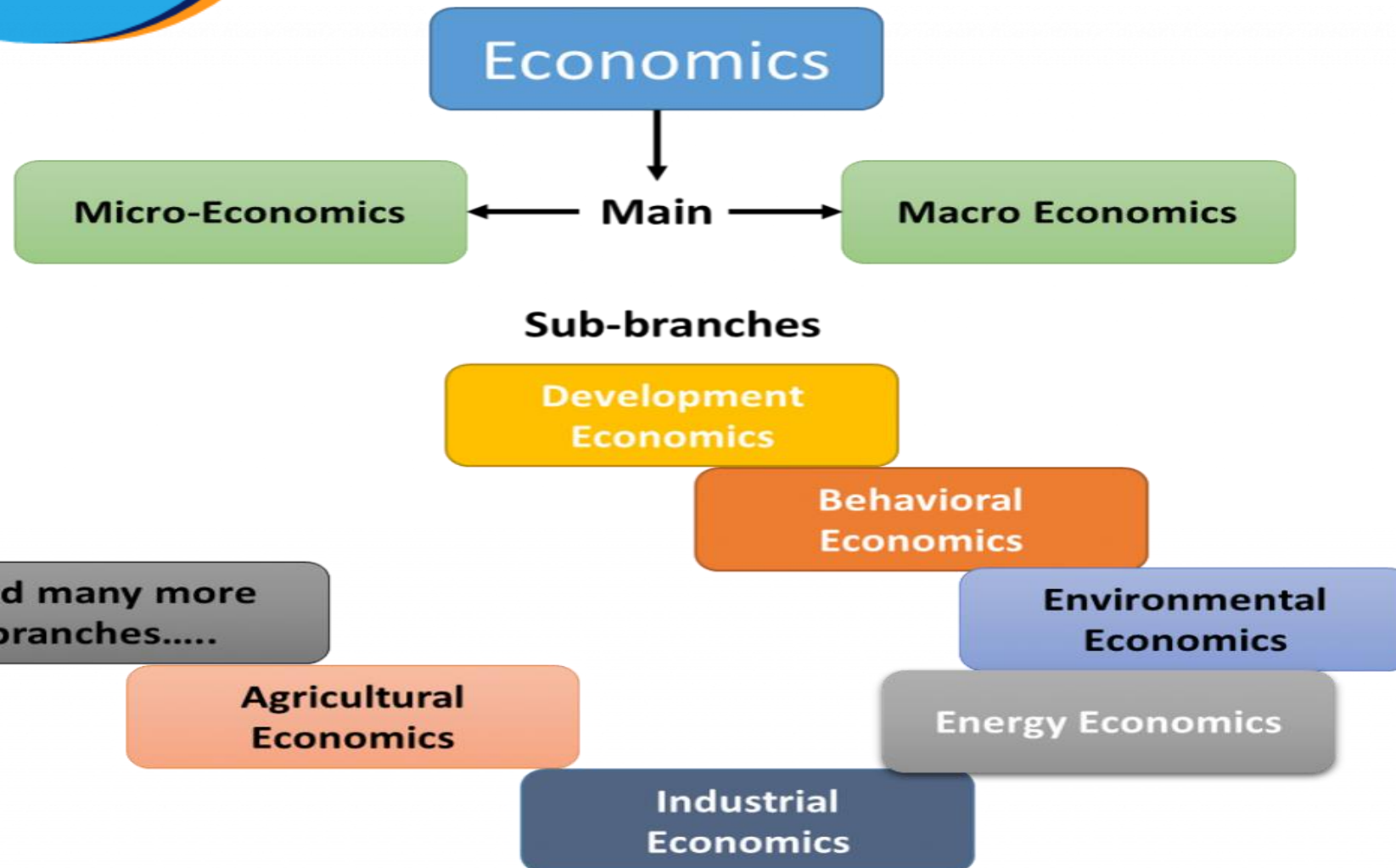
Inflation (general price level)

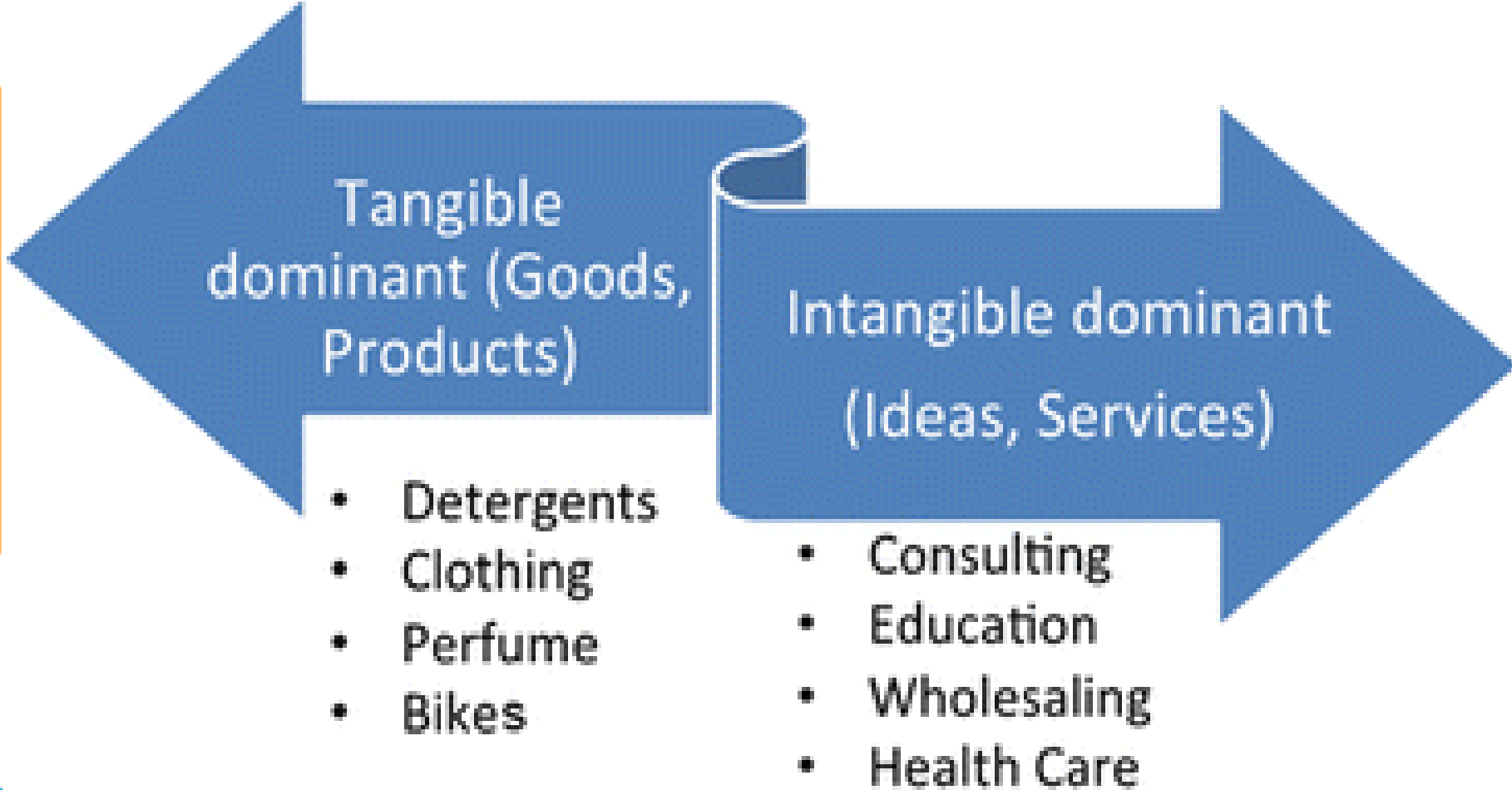
Employment/unemployment

Aggregate demand (AD)

Productive capacity of economy

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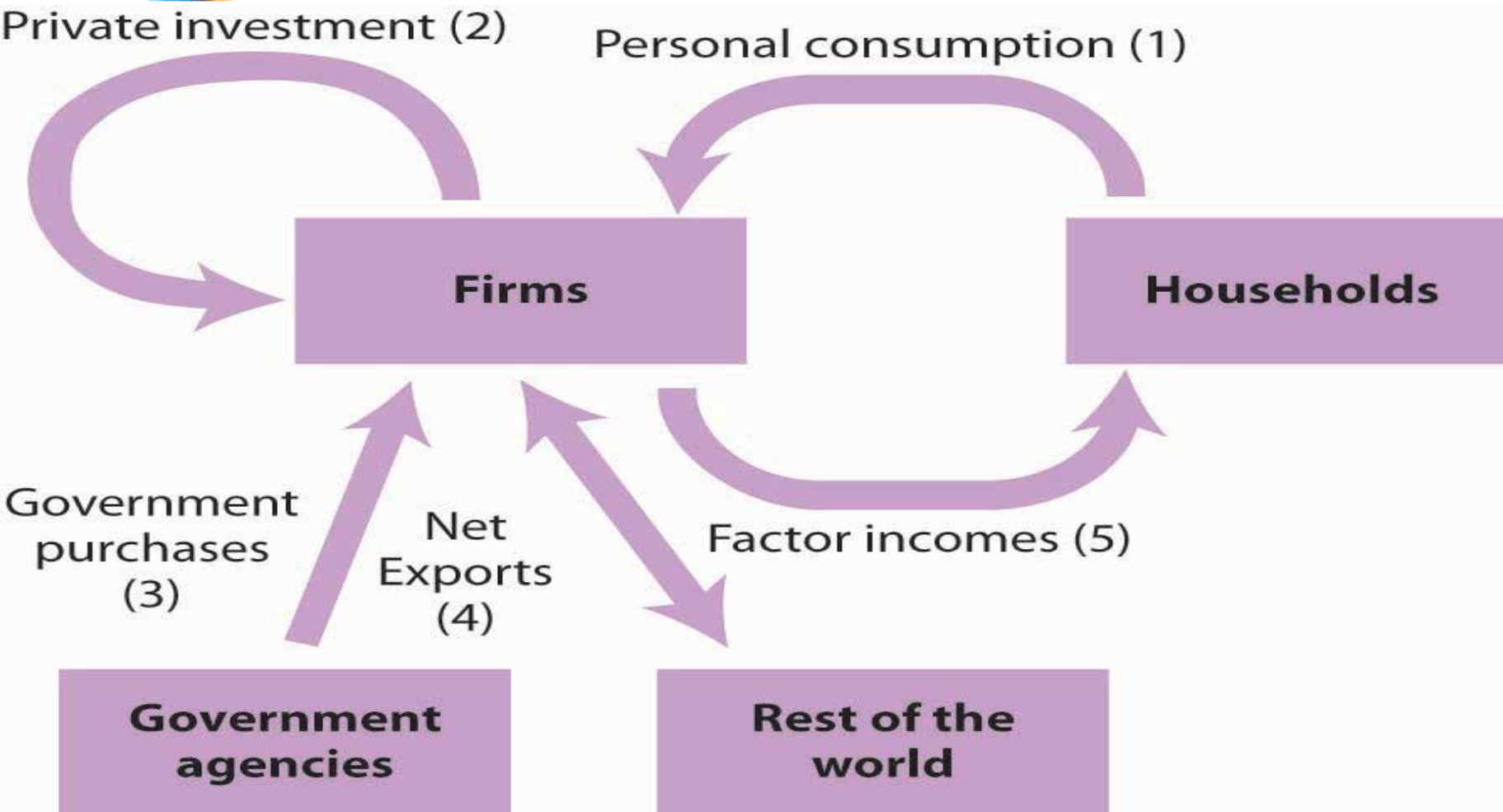


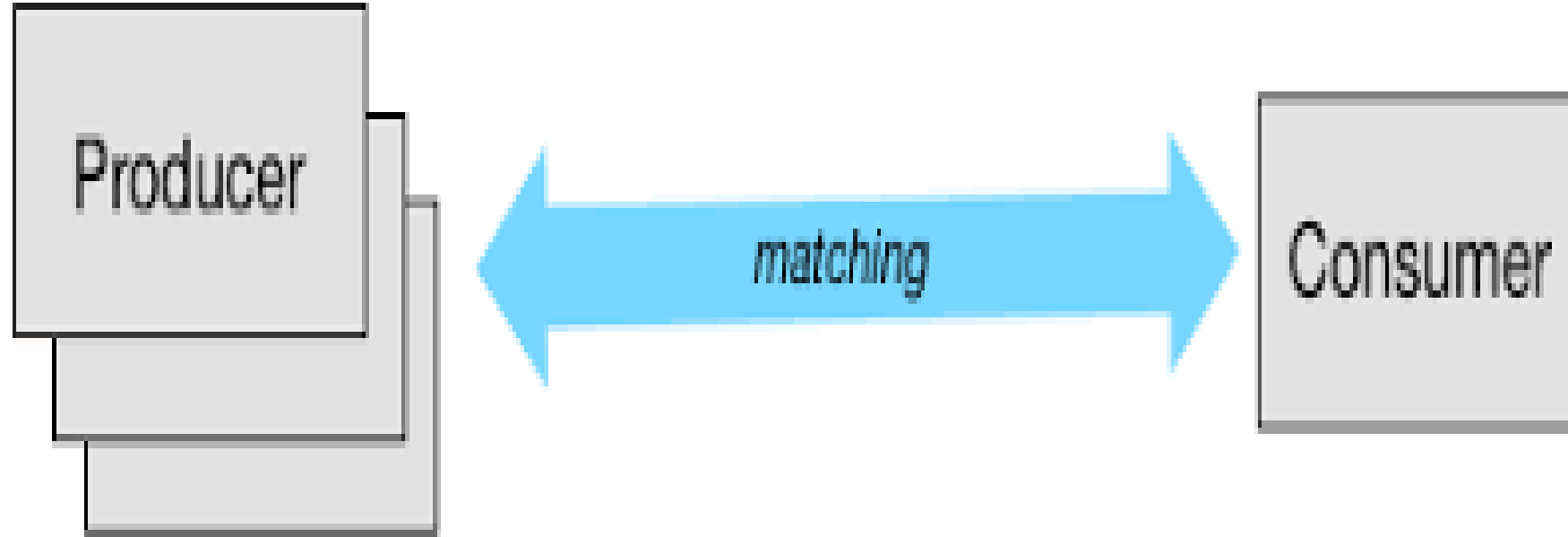
Tangible
dominant (Goods,
Products)

- Detergents
- Clothing
- Perfume
- Bikes

Intangible dominant
(Ideas, Services)

- Consulting
- Education
- Wholesaling
- Health Care





Business



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**See you
next class!**

