

What Is Economics?

by Sophia Tutorial



WHAT'S COVERED

This lesson will cover the field of economics, through the definition and discussion of:

1. What Is Economics?
2. Economics as Choice
3. Global Economics
4. Evolution of Economics
5. Economists: Predict or Explain?
6. Economics in Other Disciplines
7. Microeconomics vs. Macroeconomics

1. What Is Economics?

When discussing economics, it is important to define both what it *is* as well as what it *isn't*, because many people have misconceptions as to what the field actually studies.

What do you think economics is all about? Most people generally define economics along the lines of studying money, or financial markets, such as the stock market. Well, this may surprise you, but the basic definition of economics is the study of how people and societies make decisions.

It is not just about money or math, although economists are going to use a mathematical framework to study why people make the decisions they do. However, this is certainly not just a math class.

Economics is a **social science**, which is defined as an academic discipline that requires the examination of variables that affect the quality of human life.

Specifically, the direction that economics takes as a social science is that it focuses on the following:

- Why we as consumers purchase the things that we purchase
- How those things are produced in our society
- How our society allocates or distributes those things once they are produced



BIG IDEA

Economics is not solely a financially-focused field of study; It is a social science that studies how people and societies make decisions.



TERM TO KNOW

Social Science

Academic discipline that requires examination of variables that affect the quality of human life.

2. Economics as Choice

A fundamental idea of economics is that we choose for good reasons. Indeed, we have all made bad decisions, but generally speaking, any time you make a choice, you are weighing costs and benefits and picking the best combination of those things.

Now, when is the last time you reacted to an incentive? We react to incentives every day of our lives.

↪ **EXAMPLE** For example, suppose you are at the mall and looking at a full price pair of jeans that are quite expensive, at \$120 a pair. Should you buy them or not?

Well, you are going to be weighing the costs and benefits. You know the cost, which is \$120, but what are the benefits? Do you look really good in them? Are you able to make a lot of outfits with them? How badly do you need them?

Not everyone is going to make the same decision. Some of us really like expensive jeans, while to others, expensive jeans are not very important.

When we add up our individual choices, those become societal choices.

↪ **EXAMPLE** A societal choice would be whether or not the local government should spend the money to build a new road. If they decide to spend the money to build that new road, they are probably going to have to take that taxpayer money out of another area, such as education. However, the area may really need the new road, so the benefits may outweigh the costs. If that is the case, then they are going to build the new road.



BIG IDEA

A fundamental idea in economics is that people choose for good reasons.

3. Global Economics

As mentioned before, our values are not all the same; not all of us like expensive blue jeans. Similarly, when we are comparing and contrasting countries, values and government systems are extraordinarily different, which means that their economic systems are going to be different as well.

When we change laws, people react in different ways because they have a different incentive structure, and therefore, they behave differently.

➦ **EXAMPLE** An extreme example would be Communist North Koreans. The people living in Communist North Korea are going to have an extremely different incentive structure than the people do in the United States, which is capitalist. We know that these countries are very different politically, but they are also vastly different economically.

4. Evolution of Economics

Do you think any field of study should remain exactly the same over time? Most of us would likely agree that it should not. Economics is no different. It is a continually changing, dynamic field.

IN CONTEXT

Consider the Great Depression. Now, before the Great Depression came about, most economists viewed capitalism as the answer to everything. They anticipated booms and busts but thought that recessions would simply take care of themselves.

The dominating economic theory at the time was a very laissez-faire or hands-off approach, with the assumption that if the government just stayed out of it, the economy would take care of itself.

However, we know now that the Great Depression lasted an extremely, long time. Many economists started questioning how long we should wait, that perhaps government intervention was necessary after all. This brought a whole new way of looking at the economy into play.

Fast forward to today, are we changing right now? Should we be looking at different ways of viewing the economy after emerging from the last recession? Many people think that we should.



BIG IDEA

The field of economics is continually changing.

5. Economists: Predict or Explain?

So, can economists predict the future? Some people feel that economists are just as ineffective as meteorologists who cannot seem to predict the weather. They think that economists should be able to see everything coming in the economy--each recession or fluctuation in the stock market.

However, instead of a predicting discipline, what economics tries to do is to explain.

➦ **EXAMPLE** For example, suppose that store at the mall selling the jeans decides to mark those jeans on sale half off. Some consumers are going to respond to that rationally and will now purchase the jeans, whereas they would not before.

Another example involves the impact on consumers of the lowering of interest rates over the last few years. Some consumers noticed that rates were the lowest they had ever been and decided to take advantage of it and buy a house.

These two examples illustrate that economics does not necessarily predict consumer behavior in either case. Instead, it explains why people reacted the way that they did.

Again, we are coming back to the idea of human behavior and looking at choices that people make, and the role of incentives in those choices. In this case, the incentive for consumers to buy the jeans was a lower price, and the incentive for people to purchase a house was lower interest rates.



More than predicting, economics seeks to explain.

6. Economics in Other Disciplines

When do you usually hear quotes from economists or about economics in general? You likely hear about it on the news, hearing pundits talking about the financial markets and how the stock market performed today.

However, economics is much more than this. We already defined economics as a social science, but it is also related to and studied in many other subject areas, such as, but not limited to:

- Geography
- Government
- Civics

Anywhere there is a cost/benefit scenario in which costs and benefits need to be weighed and decisions need to be made, economists are going to be consulted. This can be in regards to changes in the health care industry, or even the environment.

7. Microeconomics vs. Macroeconomics

Economics is generally divided into two different components: microeconomics and macroeconomics.

Microeconomics is an area of economic study that focuses on specific markets, choices and behaviors that affect price, costs, and demand.

Now, "micro" means small, so therefore, microeconomics is more specific.

🔗 **EXAMPLE** For example, microeconomics would involve looking at a specific industry like the automobile industry, studying the prices of cars and wages in that industry.

"Macro," on the other hand, means big. It follows, then, that **macroeconomics** is an area of study that focuses on the impact of variables on the economic infrastructure in its entirety, on a regional, national, and global level.

Macroeconomics is more general because, as mentioned, it involves taking a step back. Instead of looking at the prices of something specifically--like apples or oranges or cars--we would be asking ourselves if all prices had gone up over the last year in general.



HINT

Here is a helpful analogy: If we are looking at macroeconomics as the overall forest, microeconomics would specifically look at the trees in that forest.



BIG IDEA

Microeconomics is a study of economics in terms of the specific, while macroeconomics focuses on the general.



TERMS TO KNOW

Microeconomics

An area of economic study that focuses on specific markets, choices, and behaviors that affect price, cost, and demand

Macroeconomics

Area of study that focuses on the impact of variables on the economic infrastructure in its entirety on a regional, national, and global level



SUMMARY

Today we learned **what economics is**, as well as what it is not. It does not just involve banks and financial markets and the stock market. Economics is a social science. Its purpose is not to **predict** the economy; instead, it focuses on **explaining** behaviors, **choices**, and incentives. We briefly discussed **global economics**, and how economics varies across different countries. We also discussed the **evolution of economics**, and how it is still evolving today. We touched upon **economics in other disciplines**, such as geography, government, and civics. Lastly, we learned about the difference between **microeconomics vs. macroeconomics**.

Source: Adapted from Sophia instructor Kate Eskra.



TERMS TO KNOW

Macroeconomics

Area of study that focuses on the impact of variables on the economic infrastructure in its entirety on a regional, national, and global level.

Microeconomics

An area of economic study that focuses on specific markets, choices, and behaviors that affect price, cost, and demand.

Social Science

Academic discipline that requires examination of variables that affect the quality of human life.