Introduction

Introduction Guide—Questions to Consider

Choices

- What affects how people make choices?
- Why do ECONs study choices?

Supply and Demand

- What does it mean when ECONs say "supply and demand"?
- How can self-interest benefit society?
- Does self-interest always benefit society?
  - Why or Why not?

Economics

- What does microeconomics mean?
- What does macroeconomics mean?

OK! So, you've made progress in Econ. You've opened your Econ book.

Welcome to my world.

My name is Jerry Evensky. I'm an economics professor at Syracuse University.

My goal in these first few pages of introduction is to convince you that it's worth reading all of the rest of the pages –and keep in mind, there aren't that many. As textbooks go this is a pretty short book.

> You are probably wondering:
>
> "Aside from the fact that I was told to, why should I spend my time reading this stuff? I could be _______________ instead [fill in the blank something you'd prefer to be doing – that should be easy]. What's in this for me?"

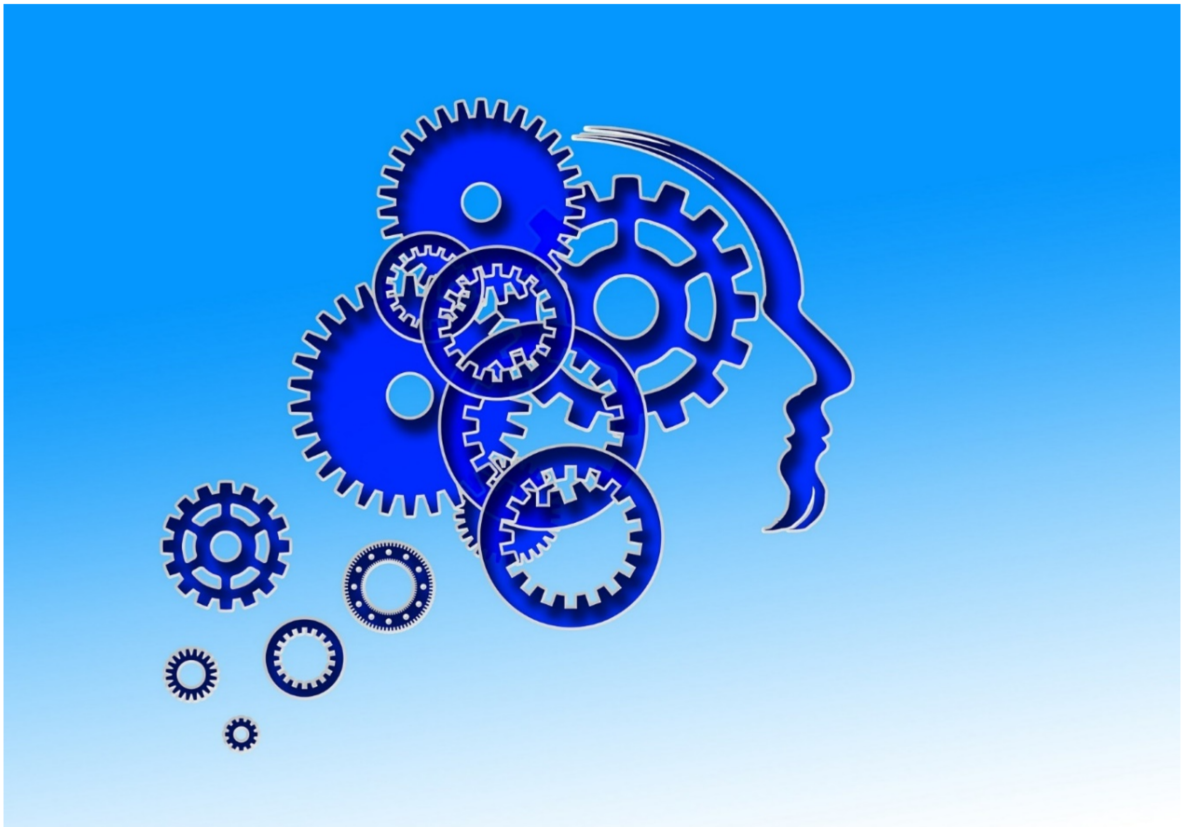
By asking that question, "I could be _[whatever]_ instead. What's in this for me?" you've already hit on a key question in economics.

> That key question is:
>
> How do people in general, and you in particular, make choices when there are lots of options and you can only choose one?

> For example, you've probably asked yourself:
>
> - What should I wear today?
> - What do I want to do this weekend?
> - What's the next step in my life?
>
> These are options. You have to choose.

In the first part of this book we're going to unscrew the top of your head (use your imagination here!) and look down into your brain to see how, according to economists –we'll call them ECONs –you actually make choices. You don't often, maybe never, think about how you make your choices …but ECONs do.

How do we make choices?



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Trust me …it's very interesting to think about this. If you understand how choices are made you can manage your own choices more effectively, and possibly even manage the choices of others. That's what advertising does, that's what your parents and teachers have been trying to do with you, and that's what your friends do, too.

Imagine that you have a Regents exam tomorrow. A good friend calls and says, "Hey, we're all going to ________ [fill in the blank with something sweet] ___, you wanna come?" This is right now, and it's sweet. You think to yourself, "The Regents exam is tomorrow, but who cares? If it's gonna matter at all, it'll only matter later and I can deal with later later."

When an ECON looks at this choice she sees you figuring out:

- The sweetness of the invitation factor
- The "How much does it –the Regents exam –really matter?" factor
- The "I care more about sooner than later, and the exam won't matter, if ever, until later" factor

In ECON terms these factors have to do with:

- The satisfaction (or, as ECONs call it, the utility) you'll get from going out with your friends
- The risk that the Regents exam may indeed turn out to matter a lot at some point
- The natural desire for immediate gratification –no one wants to wait for his or her satisfaction

Or consider a choice you might have made or might have to make about work, "How many hours should I work during the school year?"

How many hours should I work?

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For most high school students, the satisfaction from working doesn't come from the work itself, it comes later –when you get paid. What you give up to earn that paycheck is some combination of the immediate satisfaction of doing stuff with your friends, and/or the satisfaction later of getting a better job because you might get better grades and a better future if you didn't work so much now.

But, maybe you need to work because you and/or your family need the income. That gives you the immediate satisfaction of "takin' care of business," and that's big.

There are tradeoffs involved. Econ is about how we make these tradeoffs as we choose.

Or what about buying a car?

Should I buy a car?

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Suppose you're considering borrowing $900 to get some basic wheels. What are the things to consider?

- Wheels now = immediate satisfaction
- Borrowing = giving someone part of every paycheck you get for a long time = less satisfaction in every future month until the loan is paid off
- And there's that risk thing to consider again –a $900 car might not last very long.

There are, according to ECONs, the three keys to your, to my, to everybody's choices:

- Utility –How much satisfaction will I get from the choice? The sweeter the better.
- Time –When will I get the satisfaction? The sooner the better.
- Risk –Will I really get the satisfaction? The surer the better.

Thinking about these three keys can help you make more successful decisions about cars or work hours or college. It can also help you understand why some of your friends make different choices –they have different feelings about utility, time, and risk.

The ECON story is about how we all choose. It's about you and me and everyone. It's about what makes us tick. If you're interested in how you tick, it's a story worth reading –a way of thinking worth learning about. And there's more to it than that. If we're going to think about how the world works it's not enough to understand how you and I and everyone else make choices. We all do lots of choosing and most of those choices depend on other people. (You can't buy something, like a car, if nobody makes it.) That brings us to another important ECON question.

We have many individual choices to make. For example:

- What work to do? (I'll be a plumber, an accountant, a hairdresser, a teacher, an auto mechanic)
- What to buy? (I'd like that dress, the iPhone, this pair of shoes, the chicken nuggets)

How is it possible for all of these choices by so many different people to work out such that the jobs we each choose to do actually produce the stuff that other folks want to buy? How do the folks who make and sell the dresses and phones and shoes and food –Macy's, and Apple, and Nike, and McDonald's –know what to make and how much of it to make? How do they know how many people to hire and for which jobs, to make all that stuff to sell?

With no one in charge of the whole economy, with no one telling everyone what do to, how can all of our individual choices work out so that when people produce stuff, it's what other folks like you and I actually want to buy?

For ECONs it's all about supply and demand.

Walmart stocks its endless shelves with supplies of the stuff it thinks folks will demand. If there's no demand –if some stuff doesn't sell –there's obviously no point in supplying that stuff.

You might want to be a hair stylist or a barber –that would make you a "supplier" of hair care services. No matter how good you are, you couldn't make a living at it if no one wanted to pay to have their hair done –if there was no "demand." This highlights a key ECON point: there isn't any reason to supply if there isn't any demand. The flip side of that point is: If the demand for something is high and there isn't much supply …buying it is going to cost you a lot.

Consider tickets to a concert.

When a group gets hot...

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If a group is hot –the fewer the seats, the more the tickets are going to cost. When a group gets hot, suppliers (promoters) see that they can sell more seats at a higher price, so they raise the price and add seats by moving to a bigger auditorium. Supply -in this case, of seats- increases.

If that same group gets less popular its promoters will have to lower ticket prices to sell them, and they'll move the concerts to a smaller place, so supply will decrease.

For ECONs it's all about supply and demand.

It's all about getting the…

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Suppliers like Walmart pick a price and say, "At that price let's put this many on the shelves." Demanders like you and I walk into Walmart and look at that price –some of us will buy, some of us won't. If "the price is right" Walmart will have just the number on the shelves that folks want to buy. If the price is too high Walmart will have an overstock. If the price is too low it'll sell out and people will be asking, "When are y'all gonna get more in?"

For ECONs it's all about supply and demand.

If suppliers overstock they bid for your business by lowering their price. They put the stuff on sale. On the other hand, if there's not enough supplied to meet the demand, demanders bid for the product by offering to pay a higher price to get some. We'll see how this competition among suppliers and among demanders drives the price up and down until their choices to supply and to demand are in balance –the amount the suppliers produce equals the amount the demanders want to buy. When that happens "the price is right."

And it gets better –when markets are free and fair the competition among suppliers and among demanders makes everyone work hard and work smart. Over the long run in a free and fair market, suppliers can only attract demanders by making better products and/or lowering their prices. This requires them to be more quality effective and/or cost efficient, so competition makes the whole economy more and more quality effective and cost efficient. When the market is totally free and fair we can buy high quality stuff at the lowest possible price.

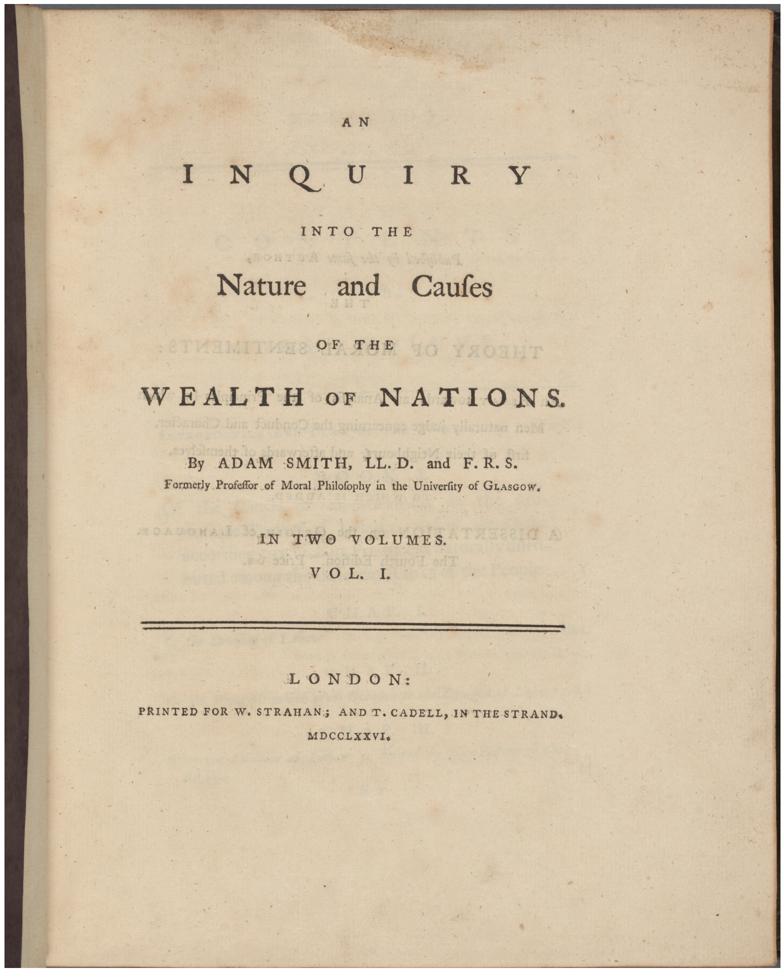
ECONs call this the "magic of markets."

Market competition is like sports competition. When it is free and fair (fair is crucial, that's why we have refs) it brings out the best in each of us because we have to perform our best to "win." Our best effort as workers or entrepreneurs drives us to produce a quality product at the lowest price that makes us a living. If you want folks to buy at your bakery, you'd better put out a good product at a good price. You'd better serve the public. By doing what's best for ourselves to "win" in the free and fair market competition, we are driven by that competition to do our best to serve one another. When the competition is free and fair, it all works out to everyone's benefit with no one in charge. It just happens naturally. This is not a new idea.

In 1776, Adam Smith, the parent of modern ECONs, wrote in his classic book *The Wealth of Nations* that:

> by directing that industry in such a manner as its produce may be of the greatest value, he intends only his own gain, and he is in this, as in many other cases, led by an invisible hand to promote an end which was no part of his intention. …By pursuing his own interest, he frequently promotes that of the society.

Adam Smith wrote about the "invisible hand" in 1776.



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But, as Smith was quick to point out, "society cannot subsist unless the laws of justice are tolerably observed." In other words, markets are not magical if the competition isn't fair. If people cheat or somehow use advantages to win –and unfortunately, as you and I both know, some people do –it mucks up the competition and makes the markets less efficient.

So, as we study economics we'll have to look at not only the good, but also the bad and the ugly of markets –why and how people cheat or take advantage of others.

This will bring us to the role of government. Is government like a fair ref –there to ensure that the competition is free and fair? Or is government a "tool" that individuals or groups use for their advantage to get an extra big "win" at others' expense –making the competition unfair? The answer to both questions is yes. It can be either, depending on how representative and inclusive and fair the government is.

All this stuff about individuals' choices and the role of markets in balancing these choices is the subject ECONs call Microeconomics (Micro). We'll learn about that first. When we finish Micro, we'll look at the same subject, the economy, from a different perspective –the Macroeconomic (Macro) perspective.

In Micro, we see all of the economy in detail. We see all the individuals and their interactions with one another through lots of markets. In Macro, we look at the economy as one big thing. In Macro we don't ask, "How are the various individuals and markets doing?" We ask, "How is the whole economy doing?"

We measure how the economy is doing by looking at things like:

- How many people want a job but can't find one (the unemployment rate)?
  OR
- Is it getting more expensive for a family to pay its bills (inflation)?

Clearly, we'd like both unemployment and inflation to be low. "Low" unemployment is historically considered to be about 4-5%. "Low" inflation is historically about 2% per year. But there have been very bad times for unemployment and for inflation in U.S. history. During the Great Depression (the 1930s) unemployment went to over 25% and in the Great Recession it was over 10%. During the 1970s, inflation was over 10%. These were tough times for your family members who lived through them. Ask them about it.

These tough times happened once and they can happen again. We all live in this economy together. We all have an interest in avoiding these tough times.

Dealing with the whole economy is way above your or my pay grade. "Economic Policy" is in the hands of the President and Congress, or in the hands of the people the President appoints and Congress approves to make and enforce economic policies.

Economic policy is not directly in our hands, but it matters BIG TIME to our lives (Can I get a job? Will I be able to afford a decent life?), and we do have the last word on government economic policy because we elect the President and our members of Congress. (Maybe you can't vote yet, but you'll have plenty of opportunities in the future.)

When we get to Macro we'll look at what causes unemployment and what causes inflation. We'll look at the tools of government policy and how they could be used. We'll see that there's a big debate about whether these tools should be used. Is active government policy a part of the solution (makes things better) or a part of the problem (makes things worse)?

Government: Part of the problem? Part of the solution?

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The policies the government chooses (or doesn't choose) will determine the answer to some pretty important questions in your life:

- Can I get a job?
- Will I be able to afford a decent life?

This stuff is really interesting, but more importantly …IT MATTERS to your life! One very practical "it matters to your life" issue we'll focus on in Chapter 2 is "Personal Finance." How should you manage your money so that you get the most satisfaction today, tomorrow, and beyond out of your money? You're going to work hard to earn it. It's important to manage it wisely so that you get the most out of it. As we explore economics, we'll see how to do that. So that's where we're going in the pages that follow. It's a story about your world, your life, and your future. It's a story that matters.