

Introduction to Macroeconomics

Macroeconomics is the branch of economics that examines the economy as a whole and tries to determine the forces that cause both good and bad economic performance. Policymakers can use the information gleaned from macroeconomics to better decide what actions, if any, that they should take to correct the course of the economy.

Some Americans—especially younger Americans—may question the need for any serious examination of the workings of the economy, since the U.S. economy has performed quite well for the past decade or so (though we have recently experienced a mild recession). Those who are older know that the U.S. economy has sometimes had a turbulent past. As recently as 1982, the unemployment rate was as high as 11.2 percent, and as recently as 1980 the inflation rate approached 20 percent. In addition, despite recent gains in the 1990s there has been a slowdown in the rate of growth of the purchasing power of the average American; during the period from 1945-1972 the average American's purchasing power doubled, while from 1973-1999 the average American's purchasing power grew only 10%.

Macroeconomics is a fairly young branch of economics, having only been thoroughly developed after World War II. Many believe that our improved understanding of the economy has helped us avoid the serious economic upheavals, such as the Great Depression, that plagued the U.S. economy prior to the 1940s.

The principal tool of macroeconomics is the *scientific method*.; Macroeconomists formulate theories about how the economy works, they use these theories to develop models of the economy (using mathematics), then they test and refine those theories and models. In addition, macroeconomists, in conjunction with statisticians and data analysts, have developed ways to measure how well the economy is performing.

One purpose of this class is, of course, to survey the principles of macroeconomics. We will:

- Examine how the performance of the economy is measured.
- Look at how the various parts of the modern economy, how each part is modeled, and how these parts are combined into an overall model of the economy.

Some questions that we'll try to answer:

- What causes inflation, and what actions (if any) should government take to keep inflation low?
- What causes unemployment, and what actions (if any) should government take to keep it low?
- What causes standards of living to rise over time, and what actions (if any) should government take to keep living standards rising?
- Should government pay down its huge debt?
- What causes an international trade deficit, and should this be a concern?

Macro-economics studies the workings of the economy as a whole.

Economists are scientists, seeking the truth about how the economy works; they are not politicians supporting some agenda.

On our journey, we'll often confront the fundamental truth gained from all economics research: **TANSTAAFL**—There Ain't No Such Thing As A Free Lunch. Improvements in one area often lead to bad things in other areas. In particular, we'll see that:

- Events which keep inflation low often cause unemployment to rise.
- Events which keep unemployment low often cause inflation to rise.
- Events which increase the standard of living of the present generation often reduce the living standards of subsequent generations.
- Events which increase the standards of living of future generations often reduce the living standards of the present generation.

When we're finished, we will understand macroeconomics (though not well enough to become practicing economists—most economists have Ph.D.s). As citizens knowledgeable about the economy, we will be able to participate in deciding the future course of our economy.

Armed with our knowledge of macro-economics, we can hold politicians accountable for their dubious economic proposals.

