Chapter 1

Introduction to Economics

Abstract

Economics plays a vital role in various parts of life. It helps in improving the standard of living of the people and their welfare as well. There are many situations with whom everybody encounters in daily life, economics helps us here, in these circumstances. This chapter explains the introduction to economics in detail including nature and the scope of subject. Different definitions of economics by different school of thoughts are given, and discussed in detail. Methodology and criteria along with types of economics are briefly explained.

Keywords: Economics, methodology, school of thought, economy

1.1. Nature and Scope of Economics

Recently economics is in every aspect of life. Everybody in the society wishes to be prosperous and want to enhance his earning and have productive resources and want to increase his business circle. All society members wish to get more incomes, and want to have significant role in the market and other economic system. They desire to boost up their standard of living and want to optimize the utility from consumption of good and services, they want secure and prosperous future, in these circumstances people want to increase their information of socio-economic problems and get benefit from them. Other than these, society members want to respond the bad situations or at least to properly respond the adverse circumstances. This indicates, their desire to improve their financial conditions. For all this, proper know how of prevailing economic trends is needed and such understandings can be established by formal and informal techniques.

Major part of society learns informally in the society by their overtime practices as they get undertake several life events. However, one want to develop career in these various aspects, he must learn these aspects formally (Gopal et al. 2007). In this regard, people should learn economics in proper way, and it will be possible by pursuing a formal course structure. They will attain a suitable knowledge of these issues. So, economics looks like to be boundless procession of new puzzles, problems, and difficult dilemmas (Samuelson and Nordhaus 2000). In the economics, we are interested in some basic question and core questions asked in the study of the allocation issues are given below:

1) What goods and services should be produced? This necessitates a valuation or grading from most valued to least precious items.

2) How many entities of each good (or service) should be manufactured? As everything that is produced, has an opportunity cost.
3) How should those items be manufactured? There are generally certain methods to manufacture goods. Quantity of items to be manufactured can have effect on the methods of production of goods and services.
4) When selected items should be manufactured? The time at which this specific item should be available can impact its worth. Manufactures of any seasonal goods must have their new apparatus available for selected season. Economists, accountants and others use the idea of present value to adjust the worth of these items or goods that would be required in coming time. Oftenly, items manufactured or used in coming time are taken as low worth.
5) How should items produced be dispersed in the society? Communities define their ways for sharing and dispersing products among the members. Methods by which these items are dispersed, may modify incentives that effect the thinking of consumers. The delivery of these items in the society to its members may also effect the methods in which certain items are valued.

1.2. Definition of Economics

It is not an easy job to properly define economics as it is not a static subject. Its aspects alter overtime and expand as well. But, proper definition is also important for the understanding of any subject. There are different definitions by different school of thoughts and experts, some of them are discussed below.

Economics is a social science that is about production, distribution and consumption of goods and services. The term economics is from ancient Greek word, oikonomia, "management of household, administration" from oikos, "house" + nomos, "custom" or "law", so "rules of the house (hold)". Recent economic models established out of the broader field of political economy, are dependent on the usage of a mathematical techniques, more alike with physical science. It can be said, economics defines, how economies work and how economic agents act together, collectively. Analysis is functional all over communities in; business venture, finance and public sector, even in crime, education, family, health, law, politics, religion, social institutions, war, and in every field of life. Its scope is widening overtime, and it has been described as the imperialism of economics. The introduction of further areas exposes the inner side of economics in recent era. It shows that it could be employed for upgrading the livelihood of society and its prosperity.

1.2.1. Economics: Science of Wealth

Adam Smith gave the first formal definition of economics, according to Adam, economics is the science of wealth, and considered it as a science that focus on the production and consumption of wealth (Smith and Nicholson 1887). However, Mill (1973) describes economics as the science that can have practical implication of the production and the distribution of money. Say (1851) defined it as the science that studies about the wealth. In the classical economics, it was limited to wealth. If the idea of wealth is defined in wider aspect to incorporate limited availability of items being used to attain utility, in this way it would become more plausible. But classical economists did not incorporate other indicators, and it is why this definition becomes quite narrow. This inadequate definition of economics concentrating on wealth, appears to limit the scope of economics.

1.2.2. Economics: Science of Material Welfare

Just as the previous economist, Marshall thought this subject is vastly associated with politics but he put attentions towards political economy. After marginalizing the prior work on the subject that take economics as subject of wealth, it was mandatory to give a more plausible definition. Marshall (2009) focused on material welfare rather than wealth and money. Wealth serve as a source to achieve ends and it is not end in itself, and he considered, "End is the human welfare." He defined economics as, political economy or economics is a study of mankind in the ordinary business of life. It studies individual and social action which is very close and interlinked with achievement and use of the material that is basics of well beings. On one aspect, economics is a subject of wealth, and on the other hand, it is a part of man's own study (Alfred 1920). According to this definition, wealth act as agent for the human welfare. According to Cannan (1903) material welfare of human beings in most important factor in the economics. A group of economists like Marshall, Cannan, Pigou, etc. put the economic or material welfare of the people at the center of study, however money have also an important role. These descriptions of economics are also subject to criticism. Robbins (1932) criticized welfare definition as it incorporates physical goods only and it missed the intangible goods. Firstly, according to him, in reality, the difference among material and non-material things are completely uncertain. Secondly, while the welfare method focused upon prosperity, still it considered non-material definition of productivity. Definition by the neo-classical economist faced other criticisms as well.

1.2.3. Robbins Definition

He defined economics as science of limited availability. According to him, "economics is the science that studies human behavior as a relationship between ends and scarce means which have alternative uses" (Robbins 1932). This definition focused on three core sectors; ends (human wants), rare means, and substitutes. Human desires are limitless as several wants are fulfilled and others become of significant important. This is continuous process, it is why consumers rank their desires to fulfil the imperative needs first.

Contrasting the infinite desires, limited resources are available but their supply is scarce. It is why, items at hand should be concurrent with the unending desires. This is an important issue for the economic science. As limited means are also short in supply and such limited resources might be employed for other uses. The scarcity definition explained the scope of economics and it has widened the scope of economics. There is no misunderstanding about the range of economics. Any problem marked by scarceness of resources and multiplicity of ends, becomes in this way an economic problem, and as such, a legitimate part of the science of economics.

Samuelson and Nordhaus (1998) have also defined economics and focused on economics, scarcity and efficiency. According to them, "Economics is the about how societies employ limited resources to manufacture precious goods and services and distribute them among different people." This definition focused on two indicators; goods are scarce, and society should use resources efficiently. So, economics is subject of significant importance subject due to fact and desire of scarcity.

1.3. Economics Schools of Thought

Generally, there are four schools of thought in economics; classical, neo-classical, new classical and Keynesian (Rothbard 1995). These are explained below.

1.3.1. Classical School

This is considered as the 1st school of economic thought, and it is associated with the 18th century well known economist Adam Smith, and others like Robert Malthus and David Ricardo. The key idea of founders of this ideology was, markets performs at optimal level when they are free to move in any direction and state has not much involvement (Ricardo 1965). This idea is very close to laissez-faire and it firmly trust on the efficiency of free markets for economic development. Classical economist said that markets should be left alone to perform based on market force, i.e., demand and supply, as the price mechanism works as strong 'invisible hand' to allocate resources to where they are optimally used. In terms of explaining value, these were quantified based on scarcity and costs of production. In terms of the macro economy, it is considered that the economy would always return to the full employment level of real production through an automatic self-adjustment mechanism. It is widely considered that the Classical period remained until 1870.

1.3.2. Neo-Classical

It is a different from the prior ideology and from this school modern economic theory evolved. Its techniques are clearly scientific, with rules and hypothesis, and tried to derive basic principles regarding the behaviour of firms and customers. For example, neo-classical economics considers that economic agents are rational in their behaviour, and consumers want to optimize utility and firms seek to optimize profits. The contrasting objectives of optimizing utility and profits established the foundation of demand and supply theory. Significant contribution of neo-classical economics was emphasis on the marginal values, such as marginal cost and marginal utility.

1.3.3. New Classical

It is associated with the work of Lucas (1988). This is about the macroeconomics and it dates from the 1970s. It is an attempt to describe macro-economic issues by employing micro-economic principles, like rational behaviour, and rational expectations.

1.3.4. Keynesian School

It widely follows the main macro-economic ideas of British economist John Maynard Keynes. He is considered as one the most significant economist of the 20th century, despite falling out of favour during the 1970s and 1980s, following the rise of new classical economics (Moggridge 1976). Keynesian believe that if left alone, free markets will obviously move towards a full employment equilibrium. This approach is regarding self-interest that governs micro-economic behaviour. And, it does not always lead to LR macro-economic development or SR macro-economic stability (Greenwald and Stiglitz 1987). It is basically a theory of AD, and can be explained through macro-economic policy in a better way.

1.4. Positive and Normative Economics

Different stakeholders use economics in different ways. For example, a practicing economist or a policy practitioner employs economic methods and techniques to draw policy proposals and econometric analysis. Often, these individuals use the economic methods with suitable knowledge and precise prediction of economic indicators. Economics is oftenly used for decision making and precise predictions. So, positive statements are about facts. These are about *what the reality is?* Meticulously saying, economics is firmly positive in character and is related with only positive statements. As positive statements are regarding the evidences, any discrepancy over these account or study can be handled correctly by employing the evidences and their examination. This type of economics is regarding the real life situations. Implications are derived and disputed that are based on these facts.

On the other hand, second type is based on the normative statements. These statements discuss, *what ought to be?* These are not related with reality of life but concerned with, how things ought to function. Contrast to positive, normative economics cannot be challenged based on fact. For example, if a political leader announces his party's vision in election that the unemployment rate should be brought down to 2%, this is not based on any calculation but it is just a future goal announced by a party. After coming to power, policy maker must tune the system to realize this target. Despite dissimilarities between positive and normative economics, it is a science having both positive and normative features because economics is a social science.

1.5. Methodology of Economics

Economics is similar to science and it is taken as a social science. It is concerned with the human conduct. It is why some of the economists says that it cannot be as exact a science as the natural sciences; like physics, chemistry etc. Basic sciences can be studied in the laboratory conditions, where indicators can be simply measured during examination. Though, social sciences like economics cannot be simply controlled. With the passage of time, this subject has attained development to establish its standard procedures and it has proved itself efficient, and these techniques can be employed for well-organized study of analysis. Forecasting can be made with suitable precision that produce a sense of confidence and faith. There are two widely used approaches in the economics.

1.5.1. The Deductive Method

This technique is about moving from general to specific. Several theories or assumptions about human behavior are taken to be true. With the aid of logical rationale and analysis, cause and effect relationship are established among the selected indicators. The following steps are undertaken in the deductive method.

At first, issue is raised and it is suitably specified for the study. Hypothesis and suitable assumptions are made as these are viable for any economic analysis. When assumptions have been formulated, then hypotheses are developed and these should be clearly framed. This step requires likely correlation among the several economic indicators. Hypotheses are then tested with the help of various tools like mathematical, economics and econometrics approaches. With the help of above analysis, proper interpretations for decision making are made.

1.5.2. The Inductive Method

Though this technique has significant points of merit to depend upon, but this this procedure has some flaws. Classical economists liked this method and it is based on going from specific to general. Here the appeal is fact, rather than reasoning and an attempt is made to arrive at conclusions from the known facts of actual life (McConnell and Brue, 2005). This technique involves following steps:

- Identification of problem
- Data collection regarding the problem under study
- Classification and analyzing data by suitable methods
- Results are drawn from the statistical examination and these are shown in the way of economic generalization.

1.6. Micro vs. Micro Economics

Distribution of limited available resources to attain optimal utility is called economics, it is divided into two parts i.e. micro and macro,

1.6.1. Micro Economics

It is about discrete or solo consumer, producer, firm, industry or market. It is also called price or income theory. It discusses the ingredients of total production. In accompanying investigation, micro economic method is on micro basis, oftenly hypothesis of full employment for entire economy is maintained.

1.6.1.1. Importance of Micro Economics

Micro Economics has both theoretical and applied implications. From the theoretical aspect, it describes the role of free intense economics. It explains, in which way consumer and producer do decision making regarding millions of products and services for consumption and production. It also discusses how items are dispersed. It elaborates, how to find the prices of several items. For practical worth, micro economics supports in establishing economic policies measured to promote efficiency in production and welfare of the masses. Its theory helps in understanding, what would be a hopelessly complicated confusion of billions of facts by constructing simplified model of behaviors.

1.6.1.2. Limitation of Micro Analysis

a) It misses the idea of complete functioning of the economy.
b) It considers fall employment which is not common event, it is therefore an unrealistic assumption.

1.6.2. Macro Economics

It assesses the economy as whole (i.e. how the activities of all the entities and firms in the economy interrelate to produce a particular level of economic performance).

1.6.2.1. Limitation of Macro Analysis

a) It ignores the micro level units like individuals
b) Macro quantifications over looks individuals difference
c) While speaking about the aggregate it is also essential to remember the nature compound and structure of the components.

1.7. Is Economics a Dismal Science?

It is a derogatory alternative name for economics coined by the Victorian historian Thomas Carlyle in the 19^{th} century. The term drew a contrast with the use of the phrase "gay science" to refer to song and verse writing. The phrase "the dismal science" first occurs in Thomas Carlyle (1853) in favor of reintroducing slavery for regulating the labor market in the West Indies. According to him, it was dismal in supply and demand, and declining the duty of human governors to that of letting men alone. It is not oftenly described correctly that Carlyle gave economics the as a response to the late 18th century publications of Thomas Malthus. He poorly forecasted that starvation would result as projected population growth that would be beyond the rate of increase in the food supply. Carlyle's view was attacked by John Stuart Mill as making a virtue of toil itself, stunting the development of the weak, and committing the error which he finds among human beings to an original difference of nature (Persky 1990).

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