

Course: Macroeconomics  
(HS 101: Economics)  
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# 1. Macroeconomics and its scope

- The study of macroeconomics is the study of the “big picture.” It is the study of how entire economies make decisions about using resources.
- It analyses the sources of growth, inflation, unemployment, and business cycles.
- It deals with the ability of governments to help (or hinder) their economies by manipulating a wide variety of policy instruments.
- It investigates why some policies work and why some fail.

## 2. Closed vs Open, Small vs Big Economies

- Closed economy macroeconomics (no or insignificant economic exchanges of the domestic economy with the rest of the world)
- Open-economy macroeconomics (domestic economy linked through trade of goods and services and capital inflows)
- Small vs Big Open economies: Small economies take the prices in the global markets as given whereas, big economies can influence the global markets.

### 3. Major approaches to economics

- Positive Economics: Describes and presents facts
- Normative Economics: Deals with prescriptions as to what should be done.
- Difference: facts vs fairness

# 4. Main Objectives of Economic Policy

1. Promoting economic growth and improvement in standard of living (through more production).
2. Bringing about a change in the structure of the economy (economic development).
3. Sustainable Development as economic growth can have conflict with nature and environment. Sustainable development, improving the standard of living of the present generation without compromising on the needs of the future generations.
4. Stable Prices
5. Reducing (poverty) inequalities in income and wealth
6. Reduction of unemployment
7. Viable Balance of payments
8. Financial stability

# 5. Economic and Political System to achieve these Objectives

- Two polar economic systems
  - Capitalism (rule of markets)
  - Command Economy (Rule of the government)
- Role of Government (state) vs Markets in solving socio-economic problems:
  - Economic systems: Command economy, capitalism, mixed economy, etc.
  - Political systems: democracy, dictatorship, communism, socialism, welfare state, etc.

- Utopia (dream about the ideal situation) vs Realism: Necessary to understand the selfish instinct in human beings. Failure of communism and socialism due to utopian ideas rather than reality. Human beings need incentives for increasing production. A judicious combination of state and market required.



## 6. Economic Systems

- **Market Economy:** Laissez-faire (no interference of government in economic matters of production, consumption and distribution. These are determined by the market. It is the law of demand and supply which are supposed to ensure equilibrium in the market.
- **Command Economy:** All economic matters are decided by the government. No individual freedom in economic matters.
- **Mixed Economy:** Both government and private sectors co-exist. Those activities which may not be necessarily profitable but are considered to be essential for welfare of societies are provided by the state. Govts may also participate
- No Economic systems can be pure systems in the long run.

# 7. Market Failure and Govt Intervention

Failure of market economy	Government intervention	Examples of government policy
<b>1. Inefficiency:</b>		
Monopoly	Encourage competition	Antitrust laws, deregulation
Externalities	Intervene in markets	Antipollution laws, antismoking ordinances
Public goods	Encourage beneficial activities	Provide public education, build roads
<b>2. Inequality:</b>		
Unacceptable inequalities of income and wealth	Redistribute income	Progressive taxation of income and wealth, Income-support or transfer programs, (e.g., subsidize health care)
<b>3. Macroeconomic problems:</b>		
Business cycles (high inflation & unemployment)	Stabilize through, macroeconomic policies	Monetary policies (e.g., changes in money supply and interest rates)
		Fiscal policies (e.g., taxes and spending programs)
Slow economic growth	Stimulate growth	Improve efficiency of tax system
		Raise national savings rate by reducing budget, deficit or increasing budget surplus

# 8. Major Schools of thought in Macroeconomics

- Classicists:  
Adam Smith
- Neo-classicists
- Monetarists
- New Classicists
- J.M. Keynes: *The General Theory of Employment, Interest and Money* in 1936
- Keynesians
- New-Keynesian

Major debates: (i) what is the relationship between money, output and prices and (ii) what should be the role of market versus government

# Main ideological difference

## Classicist and followers

1. Markets clear
2. Prices and wages are flexible
3. Monetary policy should be rule based
4. Fiscal policy should be restricted to minimum
5. Govts should not intervene in economic activity

## Keynes and Keynesians

1. Markets may not clear
2. Prices and wages are not always flexible, especially downwards
3. Monetary policy can be discretionary
4. Fiscal policy has an important role to play in economic activity
5. Governments have an important role to play to promote growth and reduce inequalities

Thank You!