Economics: the word and the act

Can you come up with a definition for:
1. “The economy”
2. “Economics”
3. “Microeconomics”
4. “Economist”

The textbook definition says that economics is about the allocation of scarce resources...

Economies

- What are a person’s resources? How does a person allocate her resources?
- What are a household’s resources? How does a household allocate its resources?
- What are a firm’s resources? How does a firm allocate its resources?
- What are a country’s resources? How does a country allocate its resources?
- What are the world’s resources? How does the world allocate its resources?

What our course is about

Markets, money, and things can dominate our lives (if we let them).
- Markets are weird and scary and amazing!
- How on earth do they work?
- Does it all seem unfair sometimes?
- Can we do better? How?
- Technology and trade mean that we have it easier than ever before in human history.
  - Macro will take care of the first one, and we’ll take care of the second.
- Trade kind of makes sense—some of mine for some of yours—but the sprawling octopus of interconnected markets is very, very complicated.
- What’s it all about? People getting what they want? Is that a dream come true or offensive and odd?
- We’ll try to draw a line from our wants and our struggles, through individual and collective decision-making, to the way we live now.

Green

Economics is about stuff, not money

“What sex is to the biology classroom, stocks and investment riskiness is to the sophomore economics lecture hall. That chapter on personal finance, put there to keep hard-boiled MIT electrical engineers awake, helped make introductory economics the largest elective course at hundreds of colleges.” - Paul Samuelson
Economics is hard

- Popper: conjecture and refutation
- Falsifiability

“... It is the first task of modern economic science to describe, to analyze, to explain, to correlate these fluctuations of national income. Both boom and slump, price inflation and deflation, are our concern. This is a difficult and complicated task. Because of the complexity of human and social behavior, we cannot hope to attain the precision of a few of the physical sciences. We cannot perform the controlled experiments of the chemist or biologist. Like the astronomer we must be content largely to ”observe.” But economic events and statistical data observed are unfortunately not so well behaved and orderly as the paths of the heavenly planets. Fortunately, however, our answers need not be accurate to several decimal places; on the contrary, if only the right general direction of cause and effect can be determined, we shall have made a tremendous step forward.” - Samuelson

How we’ll do things in this course

In this course we will be doing **modeling**.

- Making models is telling stories
- A fable has a point, but don’t take it too seriously
- “All models are wrong, but some are useful.” (Box and Draper 1987)
- All else equal...
- Math, pictures, words

“... If there is one hypothesis that is consistent with the available evidence, there are always an infinite number that are.” - Friedman

On modeling

**On Exactitude in Science**

...In that Empire, the Art of Cartography attained such Perfection that the map of a single Province occupied the entirety of a City, and the map of the Empire, the entirety of a Province. In time, those Unconscionable Maps no longer satisfied, and the Cartographers Guilds struck a Map of the Empire whose size was that of the Empire, and which coincided point for point with it. The following Generations, who were not so fond of the Study of Cartography as their Forebears had been, saw that that vast Map was Useless, and not without some Pitylessness was it, that they delivered it up to the Indecencies of Sun and Winters. In the Deserts of the West, still today, there are Tattered Ruins of that Map, inhabited by Animals and Beggars; in all the Land there is no other Relic of the Disciplines of Geography.

—Suarez Miranda, *Viajes de varones prudentes*, Libro IV, Cap. XLV, Lerida, 1658

Positive and normative economics

“... At every point of our analysis we shall be seeking to shed light on these policy problems. But to succeed in this, the student of economics must first cultivate an objective and detached ability to see things as they are, regardless of his likes or dislikes... there is only one valid reality in a given economic situation, however hard it may be to recognize and isolate it. There is not one theory of economics for Republicans and one for Democrats; not one for workers and one for employers... This does not mean that economists always agree in the policy field... Ethical questions each citizen must decide for himself, and an expert is entitled to only one vote along with everyone else.” - Samuelson

If you were in charge, what would you do?

- What is possible?
- What is right?
The ultimatum game

Two players, 1 and 2. $5.
- Player 1 proposes a division of the $5 between the two players.
- Player 2 has two choices:
  - *Accept*: the proposed division happens, and the game ends.
  - *Reject*: neither player gets anything, and the game ends.

What do you predict will happen?

Evidence

- In experiments, proposers in the ultimatum game make “large” offers.
  - Responders frequently reject offers that are “too small”.
- In the dictator game, proposers still make “large” offers.
- Preference for fairness, preference for punishment

Is this rational?

The dictator game

Two players, 1 and 2. $5.
- Player 1 proposes a division of the $5 between the two players.
- The proposed division happens, and the game ends.

What do you predict will happen?

Our course

- **Read the syllabus**
- Do the math refresher problems—if you have difficulty, you’ll need to brush up

All stuff will appear at:

http://www.brown.edu/Departments/Economics/Faculty/James_Campbell/

This includes syllabus, lecture notes, news and practice problems.