1. Introduction to Macroeconomics (part 1)

EE 212

Read: Case & Fair, ch. 5,7 ; LCR, ch. 21

January 2016

Outline

1. What is macroeconomics?
2. What are the goals of macroeconomics?
3. The brief history of macroeconomics
4. Tools for understanding macroeconomic issues
5. Tradeoff between macroeconomic objectives
6. Basic concepts in understanding economic activities

- What "Economics" is about?
  - Economics deal with a central problem faced by all individuals and all societies: the problem of "Scarcity".
- Scarcity
  - Definition of Scarcity: the excess of human needs over what can actually be produced.
- Trade-offs among different alternatives
  - A trade-off implies that having more of one good thing usually it implies having less of another.
- Economics is the study of choice under conditions of scarcity.

- Making choices in the face of scarcity implies a cost
- Economists use the term “ opportunity cost” to highlight the fact that making choices in the face of scarcity implies a cost
- An opportunity cost is the cost of any activity measured in terms of the best alternative foregone

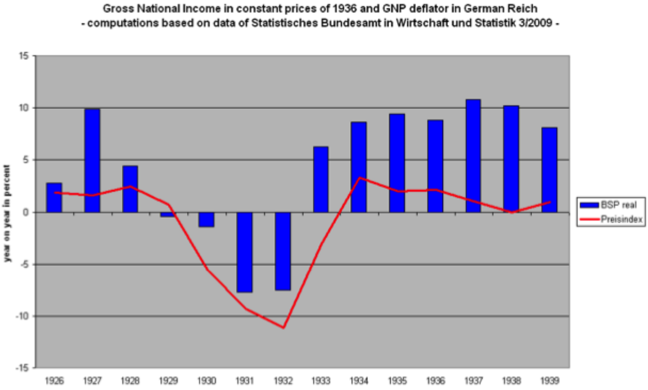
- Microeconomics: the study of the economic activities and interactions of individuals, households, businesses, and other groups at the sub-national level
- **Macroeconomics**: the study of how economic activities at all levels create a national (and global) economic environment
- Links between macro and micro: economic conditions at the aggregate level, such as rates of unemployment and inflation, create the environment in which individual economic actors make their decisions.

How do you think macroeconomic matters?

- To your life?
- To your family?
- To your country?

Why macroeconomics matters?

- The economic crisis of Weimar Republic and the rise of Nazism.



Source: wikipedia
http://www.bbc.co.uk/schools/gcsebitesize/history/tch_wjec/germany1929

Why macroeconomics matters?

- The Thai Revolution of 1932

ตารางที่ 1.1

สถิติข้าว พ.ศ. 2400 - 2457

	พื้นที่ปลูกข้าว (ล้านไร่) ภาคกลาง	ภาคอื่นๆ	จำนวนส่งออกเฉลี่ยรายปี ('000)	อัตราเพิ่มรายปี (%)	มูลค่ารายปี (ล้านบาท)	ราคาข้าวเฉลี่ยต่อตัน
2400-02	5.83		58	-	-	-
2403-07	-	-	115	14	-	-
2408-12	-	-	99	-3	-	-
2413-17	-	-	113	3	5.1	45
2418-22	-	-	213	14	10.1	48
2423-27	-	-	216	-	9.6	45
2428-32	-	-	321	8	15.1	47
2433-37	-	-	438	6	23.8	54
2438-42	-	-	483	2	36.4	75
2443-47	-	-	672	7	61.2	91
2448-52	6.8	2.4	892	6	81.0	91
2453-57	7.2	4.3	919	1	81.2	88
2458-62	8.2	5.7	954	1	108.1	113
2463-67	9.6	6.7	1,068	2	115.3	108
2468-72	10.8	7.2	1,413	6	169.6	120
2473-77	11.8	8.3	1,556	2	91.2	59
2478-82	12.0	9.2	1,534	-	94.6	62
2483-87	14.1	11.3	801	-13	99.3	124

ที่มา : Ingram (1971 : 38, 44, 246); Ishii (1978 : 285, 315).

http://www.economist.com/node/13479303

Why macroeconomics matters?

- The crisis of 1997

Why macroeconomics matters?

- Why "poor" countries rarely have successes at sport?

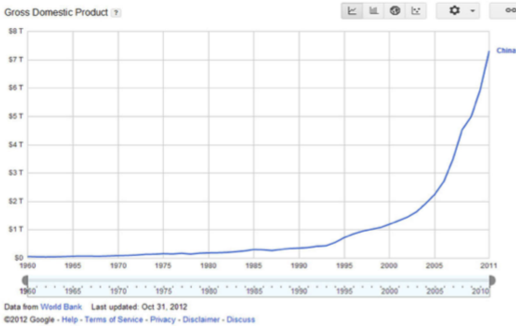
Source: www.laureaus.com

Why macroeconomics matters?

- Why “poor” countries rarely have successes at sport?

Medals by Summer Games [edit]

Games	Athletes	Gold	Silver	Bronze	Total	Rank
1932–1948	*as part of the Republic of China (ROC)*					
1952 Helsinki	1	0	0	0	**0**	–
1956–1980	*did not participate*					
1984 Los Angeles	216	15	8	9	**32**	4
1988 Seoul	273	5	11	12	**28**	11
1992 Barcelona	244	16	22	16	**54**	4
1996 Atlanta	294	16	22	12	**50**	4
2000 Sydney	271	28	16	14	**58**	3
2004 Athens	384	32	17	14	**63**	2
2008 Beijing	639	51	21	28	**100**	1
2012 London	396	38	27	23	**88**	2



China (host country 2008)

2. What are the goals of macroeconomics?

- **General goals Giving good life to everyone**
- **But a question remains: what is good life?**
- **Three major macroeconomic goals**
  1. **Raising living standards**
  2. **Creating stability**
  3. **Ensuring sustainability**

What are the goals of macroeconomics?

1. Raising living standards

- Improving what are important to life Consumptions, housing, health, education, entertainment, etc.
- The crucial means to achieve this objective is “economic growth” (i.e. growth in GDP per capita).
- But in the context of developing countries, concerns are also with “economic development” issues such as poverty and inequality

What are the goals of macroeconomics?

2. Creating stability

- Yet, the unpredictability of economic conditions can be very harmful to your life.
- Another major macroeconomic goal, therefore, is to deal with economic fluctuations
- Stability enables individuals and families to enjoy economic security and to be able to make reasonable predictions about their future.

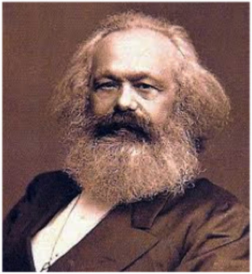
What are the goals of macroeconomics?

3. Ensuring sustainability

- How about the future generations?
  - Economic sustainability can be made in the following ways
    - Financial sustainability
    - Ecological sustainability
    - Socially sustainable
  - Do you think there are other goals?

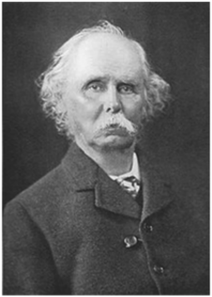
3. The History of Macroeconomics

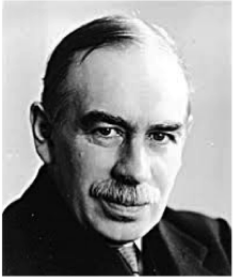
- Different historical periods brought about different concerns that underpinned development in macroeconomic ideas
- From classical to Keynesian
- And from Keynesian to monetarism, and finally to neo-classical economics

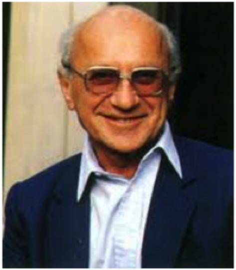


1723-1790

1818-1883







1842-1924

1883-1946

1912-2006

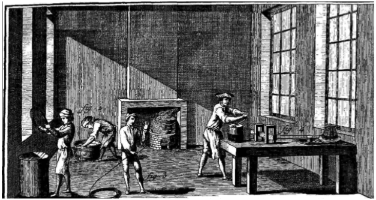
1. Classical period

- Adam Smith and "An Inquiry into the Nature and Causes of the Wealth of Nations“
- In the context of the beginning of industrialisation Division of labour (specialisation) is crucial to raising production Market can help coordinate self-interested actions of individuals so that they would ultimately serve the social good.
- Through the market system, “the invisible hand” bring the benefits to everyone.
- Have to remember that Smith was a reaction to the prior “mercentilism” (controlled economy)

Adam Smith's view of the poor

- "He has all the inconveniences of the soil and the season to struggle with, ... Thus he who as it were supports to the whole frame of society and furnishes the means of the convenience and ease of all the rest is himself possessed of a very small share and is buried in obscurity". (A.Smith, Lectures on Jurisprudence)

Adam Smith’s view of the poor



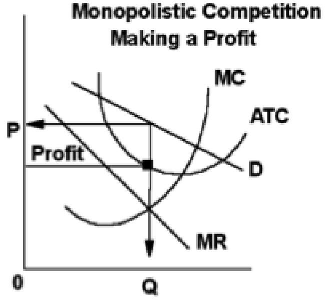
- Presenting the poor as “people with the same native abilities as everyone else”, Smith said; “the difference in natural talents in different men is, in reality, much less than we are aware of” (Smith, WN)

2. Marxist Economics

- In contrast to the pro-market view, Karl Marx raised a crucial observation on the (unfair) distributions of benefits from industrialisation
- The concern for Marx on the exploitation that occurred from "capitalism"
- And the way Marx sees the world is not just bounded to the working of the markets. He sees the whole society as proceeding through the systematic plot of history.
- History is the history of "class struggle", i.e. conflicts between ownership class that controls means of production, and labour. In the modern context, this conflict arises between the capitalists and the working class.

3. Neo-classical economists

- The revived belief in “markets”
  - Market as the most efficient, and also self-regulating
- Alfred Marshall
  - The “father” of modern economics
  - Founded theories explaining “demand”, which underpins the modern microeconomic understanding of “markets”
  - More importantly, Marshall also introduced the concept of “homo-economicus”(economic human), posing the understanding of economic agents as individuals seeking to fulfill “self-interests”



$$\text{(31)} \qquad HDI_r = \sum_{j \in FC} PF_{jr} \times \overline{FS_{jr}} - dr_r \times \overline{FS_{k,r}} + GTRANS_r$$

$$\text{(32)} \qquad SAV_r = \frac{HDI_r \times - \sum_{i \in I} PC_{ir} \times C_{ir}}{CPI_r}$$

$$\text{(33)} \qquad GR_r = PTAX_r + CTAX_r + TARRIF_r + ETAX_r$$

$$\text{(34)} \qquad PTAX_r = \sum_{i \in I} tp_{ir} \times P_{ir} \times Q_{ir}$$

$$\text{(35)} \qquad CTAX_r = \sum_{i \in I} tc_{ir} \times PX_{ir} \left(C_{ir} + GC_{ir} + ID_{ir}\right)$$

$$\text{(35)} \qquad TARRIF_r = \sum_{s \in R} \sum_{i \in I} tm_{isr} \times ER_r \times PWM_{isr} \times X_{isr}$$

$$\text{(36)} \qquad ETAX_r = \sum_{r \in R} \sum_{i \in I} te_{isr} \times PE_{ir} \times X_{isr}$$

$$\text{(38)} \qquad GTRANS_r = GR_r - GSP_r - GSVA_r$$

$$\text{(39)} \qquad BOT_r = \sum_{s \in R} \sum_{i \in I} PWE_{irs}\, X_{irs} + \frac{P_{trs}}{ER_r} \times TRQS_r - \sum_{s \in R} \sum_{i \in I} PWM_{isr} \times X_{isr}$$

- Neo-classical economists tend to see the market system as the most efficient in allocating resources.
- Even most economists accept the advantages of the market, there are still different views on the degree of regulations needed for markets to work,
- In addition, we may also place different values to other economics-related objectives
  - Growth, stability, and even inequality.

4. Keynesian economics

- In the context of “the great depression”
- Recognize that classical economics, which sees the market as self-regulating, is not adequate in dealing with economic fluctuations
- Keynes offer solutions: boosting aggregate demand
  - Through encouraging domestic consumptions, raising government spendings, and lowering interest rates
  - Particularly through government investment


"My wife's a Keynesian - she's
always spending herself out
of depressions."

5. The Monetarists

- Led by Milton Friedman
- Put the emphasis on the roles of bad monetary policies as the major factor behind economic crisis Suggest that the gov't should leave the goods market alone, acting rather through controlling the money supply Neo-liberalism (following Friedman) Keeping the trend of the"neo-classics"
- Arguing for reducing the government roles and privatising public services Pro "free-trade"

6. Neo-liberalism (following Friedman)

- Keeping the trend of the"neo-classics"
- Arguing for reducing the government roles and privatising public services
- Pro "free-trade"

Synthesising Classical and Keynesian perspectives

- **Classical view**: economics will naturally settle at full-employment, as wages and price manage to adjust to changes in money supply or unemployment
- **Keynesian view**: unemployment arises from failure of the labour market to adjust fast enough, leaving room for fiscal and monetary policies to be effective means in coping with fluctuations
- Classical is often seen as "long-run" perspective, while Keynesian is seen as the "short run" perspective.

Debates remain:

- Classical and neo-classical macroeconomists tend to emphasize market efficiency and argue for the small role of the government.
- While Keynesian macroeconomists emphasise persistent effects of unemployment, and argue for a more active role of the gov't.
  - Famous Keynes's quote: "**in the LR we are all dead.**"

Present challenges

- The integration between national economy and the creation of "globalised economy"
- The fuel-based economy is reaching the end. Climate change has got nearer.
- The persistency of global poverty and inequality. Is a more inclusive growth possible?
- What about Thailand? What do you think is our current challenges?

- Thai Economy Struggles to Grow as Exports Wilt : May 18, 2015
  - Thailand's gross domestic product expanded 3.0% from a year earlier in the first quarter
  - Economists say Thailand's GDP growth in the first quarter was amplified by a low base.
  - Thailand's exports, which account for around two-thirds of GDP, look less likely to help propel the recovery after data showed a 4.3% on-year contraction in the first quarter.
    - http://www.wsj.com/articles/thai-economy-struggles-to-grow-as-exports-wilt-1431938353
- Thai economy to strengthen in 2016-17: World Bank
  - In the "Global Economic Prospects" report released today, the World Bank forecasts 4 per cent growth rate in 2016 and 2017, on the assumption that oil prices remain low and the recovery in high-income economies strengthens.
  - The World Bank projects Thailand's real economic growth this year at 3.5 per cent, being among the countries with lowest growth rate in Asia Pacific.
    - http://www.nationmultimedia.com/business/Thai-economy-to-strengthen-in-2016-17-World-Bank-30262138.html

- SET senior executive sees positive signs for Thai economy : Nov 20, 2015
  - “Pakorn Peetathwatchai, chief strategy and finance officer of the Stock Exchange of Thailand, told CNBC that he expects growth in the next quarter to be around 3 percent."Next year, the government plans to [roll out] a lot of new investments and that would be the major factor to drive the economy," said Peetathwatchai in a CNBC interview.”
    - http://www.cnbc.com/2015/11/20/set-senior-executive-says-positive-signs-for-thai-economy.html
- Thailand sees little prospect of economic pickup : Nov 6, 2015
  - The country’s export-driven economy has suffered nine consecutive months of contraction in overseas sales, while private consumption struggles under record levels of household debt.
  - The country’s export-driven economy has suffered nine consecutive months of contraction in overseas sales, while private consumption struggles under record levels of household debt.
    - http://www.ft.com/intl/cms/s/3/49d0a188-84a5-11e5-8095-ed1a37d1e096.html#axzz3xIxIYj00