

economist may prescribe a different set of remedial measures. You should remember that in both positive and normative economics, we make use of propositions, theories and laws. Moreover, in positive economics we stop at their derivation while in normative economics we use them for achieving chosen goals.

The argument in favor of normative economics is that we are concerned with our material well-being and we must try to improve our lot and the working of the economy. Accordingly, we should not study economics for its own sake. Instead we should put economics to a practical use and therefore prefer normative economics to the positive one.

A positive statement

*“An increase in price of petrol leads to a fall in its quantity demanded.”*

A normative statement

*“Government should take steps to cut the consumption of Petrol”*

More generally, normative statement uses the verb “should”

---

## 2.6 MICROECONOMICS AND MACROECONOMICS

---

The terms microeconomics and macroeconomics are used in connection with the level of aggregation, that is the extent to which economic units and variables are covered in economic analysis. At one end, the analysis may cover the behaviour and responses of a single economic unit and at the other extreme it may cover the entire economy. These two terms (micro and macro) are derived from Greek words ‘mikros’ and ‘makros’ which mean small and large respectively.

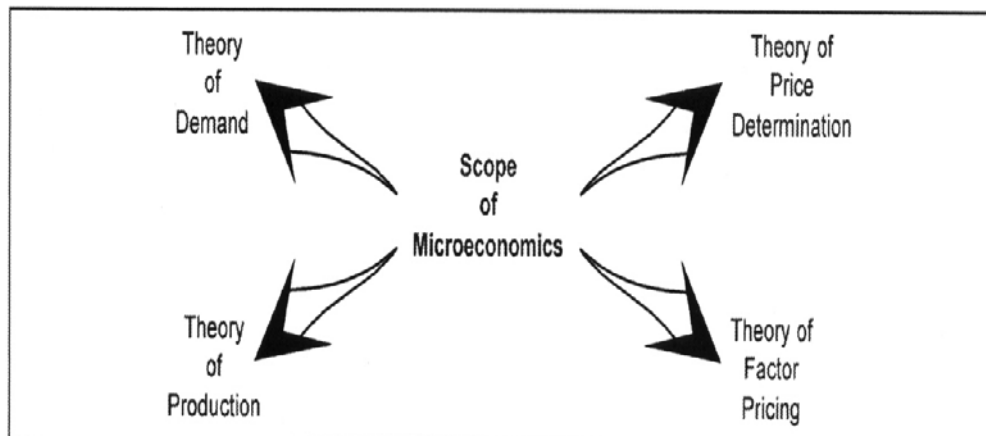
**Microeconomics deals with the behaviour of individual elements in an economy such as the determination of the price of a single product or the behaviour of a single consumer or business firm.** You may take the example of a typical individual consumer of a certain good.

In microeconomics, you try to find out change in his demand for goods in response to the price of those goods, prices of other

### For More Clarity!

**Microeconomics** (from Greek prefix micro meaning "small" + "economics") is a branch of economics that studies the behaviour of how the individual modern households and firms make decisions to allocate limited resources. Typically, it applies to markets where goods or services are being bought and sold. Microeconomics examines how these decisions and behaviours affect the supply and demand for goods and services, which determines prices, and how prices, in turn, determine the quantity supplied and quantity demanded of goods and services.

goods, his own income, his tastes and so on. Similarly, in microeconomics the determination of price of an individual good is studied. The determination of the price per unit of a factor of production also forms a part of microeconomics.

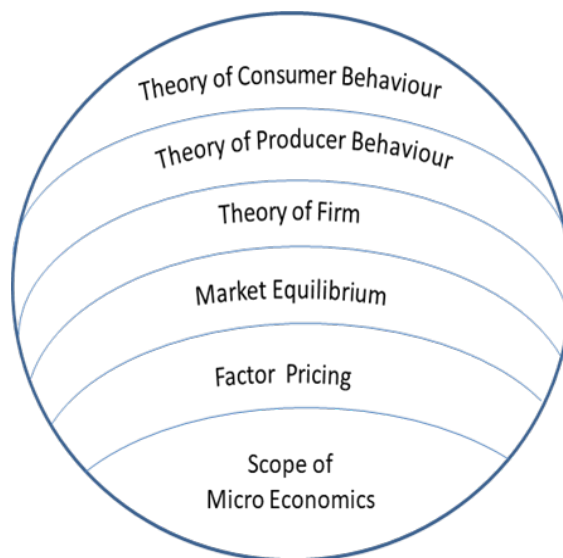


As against this, macroeconomics covers large aggregates or collection of economic units which may extend to the entire economy. In the words of Kenneth Boulding, “**Macroeconomics covers the great aggregates and averages of the economic system rather than individual items**”. Here we study collections of variables and economic units (i.e., macro variables) such as national income, employment, level of prices in general, intersectional flows of goods and services, total savings and investment, and the like. **While the study of an individual firm or an industry lies within the scope of microeconomics, an entire sector falls within the scope of macroeconomics.**

To use a metaphor, macroeconomics studies elephant as one object; microeconomics (like five blind men in a folk tale) studies individual parts of a whole body. Each study leads to different result or, to use another metaphor, one enjoys the macro view of a cricket test match while one enjoys a ball-by-ball description when sitting in before a TV.

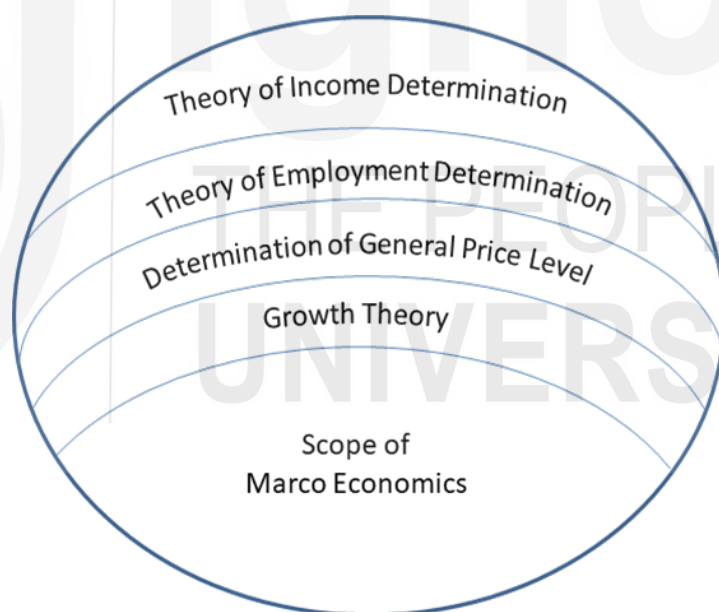
**Complementarity of Microeconomics and Macroeconomics:** Both microeconomics and macroeconomics have a place of their own and none can be dispensed with. It is useful to study both.

Firstly, a modern economy is a highly complex system in which a very large number of forces are at work in an interdependent manner. It is not possible to take into account all of them simultaneously. For studying it in bits and parts and then 'move on to the study of the economy as a whole, the necessity of studying individual units and their small groups establishes the usefulness of microeconomics.



**Figure 2.2: Scope of Microeconomics**

Secondly, the necessity to study the working of the economy as a whole establishes the usefulness of macroeconomics. Health and prosperity of the constituent elements of the economy (i.e., the individual economic units and their groups) can be ensured only if the performance of the economy as a whole is excellent.



**Figure 2.3: Scope of Macroeconomics**

However, you should remember that it is not always possible to extend the conclusions of microeconomics to macroeconomics without modifying them. This is because in many cases the outcome of the activities of individual economic units cannot be added up. Instead, they come in conflict with each other and modify the final result. For example, if an individual increases his savings by reducing his expenditure, he adds to his accumulated wealth. But if everyone does so, there would be a fall in demand and prices. Consequently, output may also fall. Similarly, an individual can buy more of a commodity at a given market price. If a large number of such individuals try to buy more, the price would go up. Take the example of bank deposits.

An individual deposit holder can close his account with the bank and withdraw the entire deposit. If all the depositors try to do so, the bank will not be able to pay them all and may even fail.

To sum up, it may be stated that microeconomic behaviour cannot be added up in a linear fashion to derive macroeconomic behaviour. There may be conflict among the units as stated above. However, the study of microeconomic unit does help in many situations to understand a macroeconomic phenomenon. For instance, there is wide spread sickness in Indian small scale industry. To comprehend this phenomenon, it is important to study the causes of sickness of individual units, formulate a set of causes, identify major causes and then suggest remedial action.

---

## 2.7 STOCKS AND FLOWS

---

Economic variables are of two kinds: 1) Stocks, and 2) Flows. **A stock variable is the one which can be measured only with reference to a point of time and not over a period of time. As against this, a flow variable is the one which can be measured only with reference to a period of time and not a point of time.** You have already come across numerous economic variables which belong to one category or the other. Take the examples of the supply of money and magnitude of wealth. They have reference to point of time. They are, therefore, 'stock' concepts. Correspondingly, examples of flow variables are production, saving, expenditure, income, sales, purchases, etc. All these variables can be measured only over a period of time. A factory can produce so much during, say, a month and not at a given moment of time. A person does not have an income at a point of time. But he has it only for a period of time. A flow concept can assume some value only with the passage of time, not otherwise. You are already familiar with the concepts of demand and supply. These two are also flow variables. Demand for goods is always its quantity which the buyers would like to buy at a stated price during a given period of time. Similar is the case with supply. You would note that **stock and flow variables are often used together in economic analysis.**

---

## 2.8 STATICS AND DYNAMICS

---

These two terms differentiate different techniques of economic analysis. In static analysis (also called static economics), the basic elements of the economic system are taken to be given and non-changing. They are known as **parameters of the economy** and include population, tastes, techniques of production, the organisation of the markets, and so on. With given parameters, an equilibrium position is selected and one or more specified variables are allowed to change subject to the usual condition of **ceteris paribus**. They are allowed to work out their effect to a new equilibrium position. The technique of estimating new equilibrium position subject to the two conditions mentioned viz., a) no change in parameters, and b) ceteris paribus, is called **static analysis or static economics**. Since in this technique two equilibrium positions are compared, it is also known as comparative static. In a refined form of this technique, the condition of a fixed parameter