

Humans in the economy

Vladan Hodulák

This powerpoint serves as a study material for the students of the course Introduction to economics (MEB435/MEBn5035) at FSS MU in Fall 2019. Using this presentation for other purposes without consent of the author is prohibited.

Economics

– Political economy

- Adam Smith: „branch of the science of a statesman or legislator.“
- J. S. Mill: “a science that teaches a nation how to become rich.“

– Contemporary mainstream economics

- Discipline redefined after „marginalist revolution“
- Neoclassical economics and its variants (conservative × neo-Keynesian)
- L. Robbins (1932): „Economics is the science which studies human behavior as a relationship between ends and scarce means which have alternative uses.“
- A science about human decision-making under the conditions of scarcity
- Rational individuals, utility maximizers, market analysis, supply and demand, equilibrium

Return of political economy?

- Alternative schools of economics
 - Marxian economics
 - (post)Keynesian economics
 - Austrian economics
 - Institutional economics
- **Economics as the study of social creation and social distribution of society's resources**
- Political science and international relations
 - is the study of the ways in which political power is acquired and used in a country (among countries)
- Development of political economy and the question of power

Levels of analysis problem

- Neoclassical economics – focus on the individual
- IR – focus on politically organized groups
- Levels of analysis
 - International system × state
 - State × bureaucracy
 - Bureaucracy × individual
- Agency × structure problem: is human behavior influenced by social structure? How and to what extent?
 - This question is irrelevant for neoclassical economics
 - But is obviously very important if one wants to intervene in the real world

Mankiw „Principles of economics“

- The most popular economics textbook
- Microeconomics × macroeconomics
- How people make decisions
 - People face tradeoffs (scarcity)
 - The cost of something is what you give up to get it (opportunity costs)
 - Rational people think at the margin (marginalism)
 - People respond to incentives (prices, competition)

Mankiw „Principles of economics“

- How people interact
 - Trade can make everyone better off (specialization, division of labor)
 - Markets are usually a good way to organize economic activity (invisible hand)
 - Governments can sometimes improve market outcomes (market failure, public goods, externality)
- How the economy as a whole works
 - A country's standard of living depends on its ability to produce goods and services (productivity)
 - Prices rise when the government prints too much money (inflation)
 - Society faces a short-run trade-off between inflation and unemployment (business cycle)

People and the Economy

- Humans are the most important actor in social sciences – we need a theory of human economic behavior on the individual level
- Fundamentals of human economic decision making
 - Preferences
 - Constraints
 - Beliefs
- Origin of preferences and beliefs
 - Genes
 - Culture
- Conscious decision-making × habits

Neoclassical economics

- Most important actor: rational individual, self-interested behavior (utility maximizers) -> **homo economicus**
- Preferences and beliefs
 - exogenous
 - Humans are „complete“ before their enter into relationships with others
- Effects of the society (culture, economic and political system) are unimportant or considered exogenous
- Economics concerns itself with decision-making of rational actors under the conditions of scarcity (constrains, resources)

Behavioral experiments

- Information provided by field studies and behavioral experiments is often contrary to the assumptions of neoclassical economics
- Taking decisions on the margin × Haifa experiment
- Ultimatum game
- Profit sharing and the importance of norms
- People as well as societies differ from each other in very important ways but nowhere is homo economicus even close to being a typical representative of the society
- Probable explanation
 - Relative influence of genes and culture
 - Preferences and beliefs are endogenous
- Economic reproduction
- The scale of cooperation among humans is unique

Economic coordination

- Economic system - a way of organizing human activities (human relations) in production and distribution of their living resources (goods and services).
- Three dimensional economics
 - Competition
 - Command
 - Change
- Neoclassical economics and the three dimensions
 - Homo economicus
 - Complete contracting assumption
 - Irrelevance of increasing returns to scale