

INTRODUCTION TO ECONOMICS



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PREFACE

TO THE INSTRUCTOR

This book provides an introduction to economic *principles*—and how those principles are applied in the real world. It's based on our well-received one-year principles book (*Economics: Principles and Applications*, by Robert Hall and Marc Lieberman, 1st edition, 1998), but redesigned and substantially rewritten for a *one-semester course* in economic principles that combines both micro- and macroeconomics.

Our philosophy is to treat fewer topics, and to treat them fully. We have tried to stick to a simple rule: If a topic can't be covered in a fully satisfying way, don't introduce it at all. The result is a book that provides a comprehensive introduction to economic principles and applications, yet one that can be read and absorbed in one semester.

The overall approach of *Introduction to Economics* can be summed up as follows:

- **We stress the basic principles of economics.** Economic theory makes repeated use of some fundamental ideas that appear again and again in many contexts. To truly understand what economics is all about, students need to learn what these central ideas are, and they need to see them in action in different contexts. We've identified and stressed eight *basic principles of economics* in this text. These are:
 - Maximization Subject to Constraints
 - Opportunity Cost
 - Specialization and Exchange
 - Markets and Equilibrium
 - Policy Tradeoffs
 - Marginal Decision Making
 - Short-Run versus Long-Run Outcomes
 - The Importance of Real Values



A full statement of each principle appears in Chapter 1 (pp. 13–14), and that full statement appears again later when each principle is used for the first time. Thereafter, whenever the principle is used, it is identified with a key symbol shown in the margin.

- **We avoid nonessential material.** When we believed a topic was not essential to a basic understanding of economics, we left it out. We have also avoided interviews, news clippings, and boxed inserts with only remote connections to the core material. The features your students *will* find in our book are there to help them understand basic economic theory itself, or to help them explore sources of information on their own, using the Internet.
- **We explain difficult concepts patiently.** Because we have avoided the encyclopedic approach, we can explain the topics we *do* cover thoroughly and patiently. We try to lead students, step-by-step, through each aspect of the theory, through each graph, and through each numerical example. Moreover, in the process of developing this book, we asked other experienced teachers to tell us which aspects of economic theory are hardest for their students to learn, and we've paid special attention to the trouble spots.
- **We use concrete examples.** Students learn best when they see how economics can explain the world around them. Whenever possible, we develop the theory using real-world examples. When we employ hypothetical examples, because they illustrate the theory more cleanly, we try to make them realistic. In addition, each chapter ends with a thorough, extended application of the material.

SPECIAL PEDAGOGICAL FEATURES. We've chosen features that reinforce the basic theory, rather than distract from it. Here is a list of the most important ones, and how we believe they help students focus on essentials.

- **Using the Theory** sections, which present extended applications, appear near the end of each chapter. While there are plenty of real-world examples in the body of each chapter, helping to illustrate each step along the way, we also felt it important to have one extended application that unifies the material in the

chapter. In the “Using the Theory” sections, students see how the tools they’ve learned can explain something about the world—something that would be difficult to explain without those tools.

- **Dangerous Curves** explanations are designed to eliminate confusion that sometimes arises as students read the text—the kinds of mistakes we see year after year in their exams.
- **Internet references** point students to resources that contain up-to-the-minute information. We prefer Internet references, rather than the traditional approach of including news stories in the text, for two reasons. First, we want to minimize distractions; and second, what is current news at the time of writing may be stale by the time the book is read.

WHAT’S DIFFERENT IN CONTENT, AND WHY. In addition to the special features just described, you will find some important differences in topical approach and arrangement. These, too, are designed to make the theory stand out more cleanly, and to make learning easier. These are not pedagogical experiments, nor are they innovation for the sake of innovation. The pedagogical differences you will find in this text are the product of years of classroom experience.

A few of the differences may require minor adjustments in class lectures, and these are listed below. But we would be remiss if we merely listed them without also pointing out why we believe they are improvements. Please indulge us a bit as you read through this list.

Innovations in Microeconomics

- **Scarcity, Choice, and Economic Systems** (Chapter 2): This early chapter, while covering standard material like opportunity cost, also introduces some central concepts much earlier than other texts. Most importantly, the chapter introduces the concept of *comparative advantage*, and the basic principle of *specialization and exchange*. We have placed them near the front of our book because we believe they provide important building blocks for much that comes later. For example, economies of scale (Chapter 5) can result from comparative advantage and specialization *within* the firm. International trade (Chapter 18) can be seen as a special application of these principles, extending them to trade between nations.
- **The Theory of the Firm** (Chapter 6): Many texts introduce the theory of the firm within the model of perfect competition. We believe this is an unfortunate choice because it forces students to master the

logic of profit maximization and the details of a rather special kind of market at the same time. Students quite naturally think of firms as facing downward-sloping demand curves—not horizontal ones. We’ve found that they have an easier time learning the theory of the firm in a more familiar context.

Further, by treating the theory of the firm in a separate chapter—before perfect competition—we can group together those concepts that apply in *all* market structures (the shapes of marginal cost and average cost curves, the marginal cost and marginal revenue rule, the shut-down rule, etc.), and distinguish them from concepts that are unique to perfect competition (the horizontal demand curve facing the firm, marginal revenue equals price, etc.)

- **Monopoly, Monopolistic Competition, and Oligopoly** (Chapter 8): Two features of our treatment are worth noting here. First, we emphasize price discrimination, a key feature of imperfect competition. We find that students are very interested in this topic. Second, we have omitted older theories of oligopoly that raised more questions than they answered, such as the kinked demand curve model. Our treatment of oligopoly is strictly game-theoretic, but we’ve taken great care to keep it simple and clear.
- **Description vs. Assessment** (Chapters 7, 8, and 10): In treating each of the four basic product market structures (perfect competition, monopoly, monopolistic competition, and oligopoly), most texts switch back and forth between the *description* of different markets and the *assessment* of market outcomes. In our view, this has several drawbacks. First, students often confuse the two. Second, it can make learning about market structure overwhelming. It is hard enough for first-time economics students to understand what happens in each type of market, let alone learn what is good and bad about each one at the same time. Finally, by mixing description and assessment, the all-important concept of economic efficiency is lost in the shuffle; it is diffused throughout the book, rather than treated comprehensively as a unified topic.

Our book collects the material on economic efficiency into a single chapter. This has several advantages. First, it permits you to focus on *description* and *prediction* when teaching about the four market structures—a full plate, in our experience. Second, having a chapter devoted to efficiency and market failure allows a more comprehensive treatment of the topic than we’ve seen elsewhere. Finally,

our approach—in which students learn about efficiency *after* they have mastered the four market structures—allows them to study efficiency with the perspective needed to really understand it.

Innovations in Macroeconomics

- **Long-Run Macroeconomics** (Chapter 14): This text presents long-run growth before short-run fluctuations. But unlike many other texts, which treat growth in an entirely descriptive way, our treatment is analytical. We use a very simple supply and demand framework to explain the causes—and costs—of economic growth in both rich and poor countries. We believe it is better to treat the long run before the short run, for two reasons. First, the long-run model makes full use of the tools of supply and demand, and thus provides for an easier transition from microeconomics to macroeconomics. Second, we believe that economic fluctuations and their transitory nature are best understood by viewing them as deviations from a long-run trend. This, of course, requires a prior treatment of how that long-run trend is determined.
- **Aggregate Demand and Aggregate Supply** (Chapter 17): One of our pet peeves about other introductory texts is the too-early introduction of aggregate demand and aggregate supply curves, *before* teaching where these curves come from. Students then confuse the *AD* and *AS* curves with their microeconomic counterparts, requiring corrective action later. In this text, the *AD* and *AS* curves do not appear until Chapter 17, where they are fully explained. Our treatment of aggregate supply is based on a very simple mark-up model that our students have found very accessible.

BUILDING A SYLLABUS. We have arranged the contents of each chapter, and the table of contents as a whole, according to the order of presentation that we recommend. But we've also built in some flexibility. For example, Chapter 4 develops consumer theory with both marginal utility and (in an appendix) indifference curves, allowing you to present either method in class. If you wish to highlight international trade, you could assign Chapter 18 immediately after Chapter 3.

Finally, we have included only those chapters that we thought were both essential and teachable in a one-semester course. But nothing in Chapter 9 (Labor Markets and Wages) or Chapter 10 (Economic Efficiency and the Role of Government) is required to understand the other

chapters in the book. And the treatment of macroeconomics could, in a pinch, end with Chapter 16, leaving out Chapter 17 (Aggregate Supply and Demand). Finally, an instructor could drop Chapter 18 (International Trade and Comparative Advantage), since comparative advantage as a general concept is fully treated earlier, in Chapter 2.

TEACHING AIDS FOR THE INSTRUCTOR

- The Instructor's Manual contains chapter summaries, lecture ideas, teaching tips and activities, ideas for interactive teaching, and solutions to end-of-chapter problems and exercises.
- The Test Bank contains thousands of multiple-choice questions. It is available in both printed and electronic forms.
- Full-color transparencies are available for most of the key graphs and illustrations in the text.
- Our Web site gives students access to a variety of perspectives on economic issues of the day. It contains a series of accessible position papers that explain competing viewpoints on key policy issues. The site also contains news updates linked to the text, teaching and learning resources, and a variety of other interesting features. (<http://hall-lieb.swcollege.com>)
- Tutorial software allows students to create, modify, and use key graphs.
- A CNN video provides a variety of short video clips on various aspects of economics.
- Many of the text's figures and tables are available as Microsoft PowerPoint files.

A REQUEST. Although we've worked hard on this book, we know we'll be able to improve it further in future editions. For that, our fellow users are indispensable. We invite your comments and suggestions wholeheartedly. We especially welcome your suggestions for additional "Dangerous Curves" and "Using the Theory" sections. You may send your comments to either of us care of South-Western College Publishing.

Marc Lieberman
Robert Hall

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This book is a case study of the principle of specialization and exchange. So many people contributed their valuable skills and expertise, especially the staff of South-Western College Publishing. As with our previous text, our largest debt of gratitude is owed to our development editor, Dennis Hanseman. Not only does

he hold a Ph.D. in economics, but he also possesses a rare ability to take the viewpoint of someone new to the field. His knack for spotting potential areas of confusion, his stubborn insistence on absolute clarity at every turn, and his innumerable contributions in planning and executing the project were immensely valuable. Jack Calhoun, now team director at South-Western, originally signed us as authors, so it is fair to say that this book would not exist without him. He was a relentless advocate for South-Western as a superior publishing company (a description that turned out to be entirely accurate), and a great problem solver once the project was under way. Keri Witman, the acquisitions editor for this project, worked hard to make it a reality, and showed tremendous patience and creativity in breaking through the inevitable logjams that arise when not every contingency can be anticipated in a contract. Lisa Lysne—with a combination of exceptional talent and long hours—did a superior job of marketing and advertising this book and coming up with creative ways to explain what it was all about. Joe Devine created the design features for the text, and accomplished a near impossible task: designing a cover that both authors like a lot.

In addition to those at South-Western, we would like to thank the staff of Pre-Press Company, who turned our manuscript into a beautiful book. Bruce Watson and Jennifer Stephan contributed many of the end-of-chapter questions. Geoffrey Jehle, of Vassar College, and Heinz Kohler, of Amherst College, also made important contributions. Chaitan Narsule deserves special thanks for reading every page of the manuscript, and showing remarkable skill and taste in suggesting changes.

Finally we would like to thank the instructors who provided numerous suggestions that we found most helpful in developing this book. While we had no intention of writing a book that would be “all things to all people,” and could not incorporate every suggestion, these individuals helped us make the book “more things for more people.”

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Personal Note from Bob Hall. Charlotte Pace, who keeps my office humming at Stanford, contributed in many ways, especially raising the art of copy checking and proofreading to new levels of excellence. My son Chris served as college culture consultant for the book. My wife, Susan Woodward—a financial economist—helped in so many ways, and happily tolerated the domestic dislocations that inevitably accompany a project like this one. She read and commented on many of the chapters and drafted material in her areas of interest. And she made Marc very happy by cooking dinner for him.

TO THE STUDENT

You may have already noticed that this note is substantially shorter than our note to instructors. And for good reason. The entire book has been written with you in mind. Here, we just want to give you some advice on using some special features of this book, and suggest some helpful supplements.

- **Getting started:** The first chapter tells you what economics is, and gives some tips on how to study it.
- **The Basic Principles:** As you will see, much of economic theory boils down to a small number of fundamental ideas, which appear again and again in many contexts. In this book, we've identified eight of them, and we call them the *basic principles of economics*. The entire list is presented in Chapter 1, and each principle is discussed, in more detail, in a later chapter when it is first used. Throughout the



book, each time the principle appears again, it is identified with a key symbol, as shown at left. When you see one of these keys, it's a signal to stop and think about how the principle is being used.



- **Dangerous Curves:** Professors *do* talk about other things besides the mistakes their students make on exams. But when the subject comes up, it is surprising that our experiences are so similar. Year after year, no matter how hard we try, the same confusions pop up. We've tried to identify the most common ones in our "Dangerous Curves" feature, which you will find throughout the text. You may want to skip them as you read through the chapter the first time, and concentrate on them later—especially before exam time.



- **Using the Theory:** Each chapter ends with an application that demonstrates how the tools you've learned can help you understand something new about the world, something that would be hard to understand *without* those tools.



- The Lieberman/Hall **Web site** contains a variety of helpful features that will enrich your study of economics. Check it out on a regular basis at <http://hall-lieb.swcollege.com>.
- **Mathematical Appendix:** For the most part, the only math you need to understand this book is what you learned in high school—and only a small part of that. The required math, as well as the basics of graphs, are reviewed in the mathematical appendix at the end of the book. If you are very rusty, you

might want to read the appendix in its entirety, early on. Otherwise, just know that it's there, and refer to it when you need it.

LEARNING AIDS. The following items are also available to help you learn economics:

- **The Study Guide:** Learning is different from memorizing. This textbook has been written to help you understand each concept. Nevertheless, to really master the material, there is nothing like repeated problem solving. Much as practicing helps a pianist, the Study Guide written to accompany this book will help you strengthen your knowledge of economics. (ISBN: 0-324-00880-5)
- **ECONOMICS ALIVE!** is a pair of exciting CD-ROMs that contain animated lessons, economic tool-building exercises, and simulations that will help you learn economics interactively. (For microeconomics, ISBN: 0-538-84650-X. For macroeconomics, ISBN: 0-538- 85471-5.)

These learning aids can be ordered through your campus bookstore.

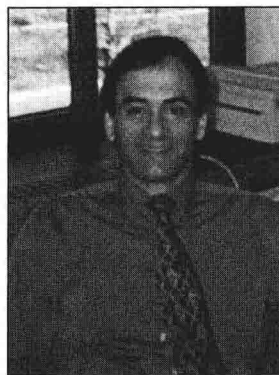
We are honored to help your instructor welcome you to the field of economics. We hope you find the experience of reading this book a fulfilling one—as fulfilling as the experience we had writing it.

Marc Lieberman
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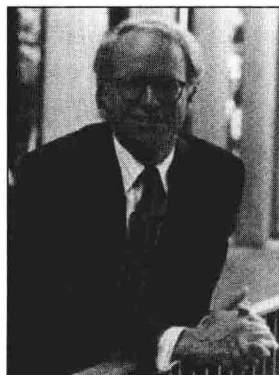


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