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14 • Chapter 2/Thinking Like an Economist

KEY POINTS:

Economists try to address their subject with a scientist's objectivity. Like all scientists, they make appropriate assumptions and build simplified models to understand the world around them. Two simple economic models are the circular-flow diagram and the production possibilities frontier.

The field of economics is divided into two subfields: microeconomics and macroeconomics. Microeconomics study decision making by households and firms and the interactions among households and firms in the marketplace. Macroeconomics study the forces and trends that affect the economy as a whole.

A positive statement is an assertion about how the world is. A normative statement is an assertion about how the world ought to be. Ethical economists make normative statements; they are acting more as policy advisers than as scientists.

Economists who advise policymakers sometimes offer conflicting advice either because of differences in scientific judgment or because of differences in values. At other times, economists are united in the advice they offer, but policymakers may choose to ignore the advice because of the many forces and constraints imposed by the political process.

CHAPTER OUTLINE:

I. The Economist as Scientist

A. Economists Follow the Scientific Method.

1. Observations help us to develop theory.
2. Data can be collected and analyzed to evaluate theories.
3. Using data to evaluate theories is more difficult in economics than in physical science because economists are unable to generate their own data and must make do with whatever data are available.
4. Thus, economists pay close attention to the natural experiments offered by history.

B. Assumptions Make the World Easier to Understand.

1. Example: to understand international trade, it may be helpful to start out assuming that there are only two countries in the world producing only two goods. Once we understand how trade would work between these two countries, we can extend our analysis to a greater number of countries and goods.
2. One important role of a scientist is to understand which assumptions one should make.
3. Economists often use assumptions that are somewhat unrealistic but will have small effects on the actual outcome of the interest.

C. Economists Use Economic Models to Explain the World around Us.

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