

Micro and Macro Economics

The terms 'micro-' and 'macro-' economics were first coined and used by Ragnar Fiscer in 1933. Micro-economics studies the economic actions and behaviour of individual units and small groups of individual units. In micro-economics, we are chiefly concerned with the economic study of an individual household, individual consumer, individual producer, individual firm, individual industry, particular commodity, etc. Whereas, when we are analysing the problems of the economy as a whole, it is a macro-economic study. In macro-economics, we do not study an individual producer or consumer, but we study all the producers or consumers in a particular economy.

Micro-Economics or Price Theory:

The term '*micro-economics*' is derived from the Greek prefix '*micro*', which means small or a millionth part. Micro-economic theory is also known as '*price theory*'. It is an analysis of the behaviour of any small decision-making unit, such as a firm, or an industry, or a consumer, etc. For micro-economics, in contrast to macro economic theory, the statistics of total economic activity are valueless as far as providing clues to policy decisions. It does not give an idea of the functioning of the economy as a whole. An individual industry may be flourishing, whereas the economy as a whole may be suffering.

In respect of employment, micro-economics studies only the employment in a firm or in an industry and does not concern to the aggregate employment in the whole economy. In the circular flow of economic activity in the community, micro-economics studies the flow of economic resources or factors of production from the resource owners to business firms and the flow of goods and services from the business firms to households. It studies the composition of such flows and how the prices of goods and services in the flow are determined.

A noteworthy feature of micro-approach is that, while conducting economic analysis on a micro basis, generally an assumption of '*full employment*' in the economy as a whole is made. On that assumption, the economic problem is mainly that of resource allocation or of theory of price.

Importance of Micro-Economics: Micro-economics occupies a very important place in the study of economic theory.

- 1. Functioning of free enterprise economy:** It explains the functioning of a free enterprise economy. It tells us how millions of consumers and producers in an economy take decisions about the allocation of productive resources among millions of goods and services.
- 2. Distribution of goods and services:** It also explains how through market mechanism goods and services produced in the economy are distributed.
- 3. Determination of prices:** It also explains the determination of the relative prices of various products and productive services.

4. ***Efficiency in consumption and production:*** It explains the conditions of efficiency both in consumption and production and departure from the optimum.
5. ***Formulation of economic policies:*** It helps in the formulation of economic policies calculated to promote efficiency in production and the welfare of the masses.

Thus the role of micro-economics is both positive and normative. It not only tells us how the economy operates but also how it should be operated to promote general welfare. It is also applicable to various branches of economics such as public finance, international trade, etc.

Limitations of Micro-Economics: Micro-economic analysis suffers from certain limitations:

1. It *does not give an idea of the functioning of the economy as a whole*. It fails to analyse the aggregate employment level of the economy, aggregate demand, inflation, gross domestic product, etc.
2. It *assumes the existence of 'full employment'* in the whole economy, which is practically impossible.

Macro-Economics or Theory of Income and Employment:

The term '*macro-economics*' is derived from the Greek prefix '*macro*', which means a large part. Macro-economics is an analysis of aggregates and averages of the entire (large) economy, such as national income, gross domestic product, total employment, total output, total consumption, aggregate demand, aggregate supply, etc. Macro-economics is the economic theory which looks to the statistics of a nation's total economic activity and holds that policy change designed to alter these total statistical aggregates is the way to determine economic policy and promote economic progress. Individual is ignored altogether. Sometimes, national saving is increased at the expense of individual welfare.

It analysis the chief determinants of economic development, and the various stages and processes of economic growth. Different macro-economic models of economic growth have been suggested, one of which most famous is Harrod-Domar Model. It can be applied to both developed and under-developed economies.

Importance of Macro-Economics:

1. It is *helpful in understanding the functioning of a complicated economic system*. It also studies the functioning of global economy. With growth of globalisation and WTO regime, the study of macro-economics has become more important.
2. It is very *important in the formulation of useful economic policies* for the nation to remove the problems of unemployment, inflation, rising prices and poverty.
3. Through macro-economics, the *national income can be estimated and regulated*. The per capita income and the people's living standard are also estimated through

macro-economic study. It explains the fluctuations in national income, per capita income, output and employment.

Limitations of Macro-Economics:

1. *Individual is ignored altogether.* For example, in macro-economics national saving is increased through increasing tax on consumption, which directly affects the consumer welfare.
2. The macro-economic analysis *overlooks individual differences.* For instance, the general price level may be stable, but the prices of food grains may have gone spelling ruin to the poor. A steep rise in manufactured articles may conceal a calamitous fall in agricultural prices, while the average prices were steady. The agriculturists may be ruined. While speaking of the aggregates, it is also essential to remember the nature, composition and structure of the components.