

7.6: Microeconomics and Macroeconomics

Learning Objectives

- Distinguish between macroeconomics and microeconomics

Try It

Economics is such a broad field of study that it is broken down into two subfields: microeconomics and macroeconomics. Microeconomics covers topics related to the actions of individual people or businesses within the economy while macroeconomics examines the larger economy and broader issues like GDP, inflation, growth rates, and trade. Watch this video to learn about the distinction between the two perspectives.



You can [view the transcript for “Episode 4: Micro vs Macro”](#) (opens in new window).



Figure 7.6.1: Vermilion Lake.

It should be clear by now that economics covers a lot of ground. That ground can be divided into two parts: **Microeconomics** focuses on the actions of individual agents within the economy, like households, workers, and businesses; **macroeconomics** looks at the economy as a whole. It focuses on broad issues such as growth, unemployment, inflation, and trade balance. Microeconomics and macroeconomics are not separate subjects but are, rather, complementary perspectives on the overall subject of the economy.

To understand why both microeconomic and macroeconomic perspectives are useful, consider the problem of studying a biological ecosystem like a lake. One person who sets out to study the lake might focus on specific topics: certain kinds of algae or plant life; the characteristics of particular fish or snails; or the trees surrounding the lake. Another person might take an overall view and instead consider the entire ecosystem of the lake from top to bottom: what eats what, how the system remains in balance, and what environmental stresses affect this balance. Both approaches are useful, and both researchers study the same lake, but the viewpoints

are different. In a similar way, both microeconomics and macroeconomics study the same economy, but each has a different starting point, perspective, and focus.

Whether you are looking at lakes or economics, the micro and the macro insights should illuminate each other. In studying a lake, the “micro” insights about particular plants and animals help us to understand the overall food chain, while the “macro” insights about the overall food chain help to explain the environment in which individual plants and animals live.

In economics, the micro decisions of individual businesses are influenced by the health of the macroeconomy—for example, firms will be more likely to hire workers if the overall economy is growing. In turn, the performance of the macroeconomy ultimately depends on the microeconomic decisions made by individual households and businesses.

Microeconomics

What determines how households and individuals spend their budgets? What combination of goods and services will best fit their needs and wants, given the budget they have to spend? How do people decide whether to work, and if so, whether to work full time or part time? How do people decide how much to save for the future, or whether they should borrow to spend beyond their current means?

What determines the products, and how many of each, a firm will produce and sell? What determines what prices a firm will charge? What determines how a firm will produce its products? What determines how many workers it will hire? How will a firm finance its business? When will a firm decide to expand, downsize, or even close? In the microeconomic part of this text, we will learn about the theory of consumer behavior and the theory of the firm.

Macroeconomics

What determines the level of economic activity in a society or nation?—that is, how many goods and services does it actually produce? What determines how many jobs are available in an economy? What determines a nation’s standard of living? What causes the economy to speed up or slow down? What causes firms to hire more workers or lay them off? Finally, what causes the economy to grow over the long term?

An economy’s macroeconomic health can be assessed by a number of standards or goals. The most important macroeconomic goals are the following:

- Growth in the standard of living
- Low unemployment
- Low inflation

Macroeconomic policy pursues these goals through monetary policy and fiscal policy:

- **Monetary policy**, which involves policies that affect bank lending, interest rates, and financial capital markets, is conducted by a nation’s central bank. For the United States, this is the Federal Reserve.
- **Fiscal policy**, which involves government spending and taxes, is determined by a nation’s legislative body. For the United States, this is the Congress and the executive branch, which establishes the federal budget.

To keep the differences between these policies straight, remember that the term *monetary* relates to money, and the term *fiscal* relates to government revenue or taxes.

? Practice Questions

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