Macroeconomics and Microeconomics

**Key Concepts**

- **Microeconomics** is the study of the decision-making process of individuals.
- **Macroeconomics** is the study of aggregate decision making.
- The players in the economy include households, businesses, government, and foreign trade.
- **Nominal variables** are measured in terms of actual dollar values.
- **Real variables** are measured in terms of physical goods and services.

The analogy illustrated on the left explains the difference between microeconomics and macroeconomics.

Microeconomics answers questions such as, “If wages rise, will households supply more or less labor?”

Macroeconomics addresses questions like, “What happens to employment when overall productivity increases?”

Macroeconomics also examines the Federal Reserve’s decisions to control the money supply and their effects on the economy.

Consider the chart on the left. This chart shows the players in the economy—households, businesses, government, and net exports—and the way in which they are studied in microeconomics and macroeconomics.
When we place dollar values on goods and services, the values are **nominal variables**. We use **real variables**, however, to measure actual, tangible goods and services.

Look at the example on the left. When we add the nominal values of an apple and a cup of coffee, we calculate a total value of $1.75. It is much more difficult, though, to calculate the total value of an apple and a cup of coffee based on real values.

<table>
<thead>
<tr>
<th>Nominal vs. real variables</th>
<th>Nominal variables are measured in monetary terms.</th>
<th>Real variables are measured in terms of goods and services.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Example</td>
<td><img src="apple_cup_nominal.png" alt="Diagram of apple and cup with nominal values" /></td>
<td><img src="apple_cup_real.png" alt="Diagram of apple and cup with real values" /></td>
</tr>
</tbody>
</table>

It is easier to calculate nominal variables than real variables.