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BOOK REVIEW

THE ECONOMIC WAY OF THINKING

By Paul Heyne, Peter Boettke and David Prychitko, Prentice Hall, 2010. 405 pp., ISBN: 978-0-13-603985-3.

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The tribute by Douglass C. North (a Nobel Prize Winner in Economics Sciences, 1993) in the opening of this book drew my attention to it. Within a mere 405 pages, which is considered moderate by the standard of economics books, the authors have successfully arranged the building blocks of economics in a nutshell. The content is cleverly divided into 16 chapters, beginning with the basic feature of economic theory as all social phenomena emerging from actions and interactions of individuals who are choosing in respect to expected benefits and costs to themselves. Discussions revolve around the emphasis on indivdual choices, economizing process and the pro- market preference, concluding that although facts can be observed, it takes a theory to explain the causes.

Too much teaching is said to make abstract economic theories appear dull to students. On the contrary, the book is designed to act as basic kit of intellectual tools to master the art of applying the theories sensibly to actual social problems in their infinite complexity.

Chapter 2 explains the relevance of efficiency, exchange and comparative advantage in general. Profits made by merchants without value addition are seen as the epitome of inefficiency, whereas exchange is productive because it avails more of what people value. Economic efficiency is said to depend on marginal decisions, with the least cost producers to gain from specialization by expanding production possibilities. The evolution of division of labor without a blueprint and the establishment of rules of law for a commercial society is necessary for successful development.

Chapter 3 looks at the Concept of Demand, whereby our choices are said to depend on the situations with the marginal values mattering the most. Topics covered range from the fundamentals of the Law of Demand, the shifts, elasticity, and rationing criteria. This chapter concludes that economizing is indeed natural. Chapter 4 on Costs and Choices deals with the concept of supply. Evidently, market prices help economize more effectively, by informing producers of alternative production plans. Costs are tied to actions not things. Chapter 5 combines the forces of market enabling society to become wealthy through division of labor. The market consisting of consumers and producers overcomes the basic problem of massive ignorance through coordination not necessarily through the commonly said self-adjusting process. The importance of clearly defining property rights and the ability to exchange is also a key role of the market. Chapter 6 is an extension on the unintended consequences of demand and supply, disclosing principles that work with regard to people's choices and the neglect of previous rules of the game and government imperfections blamed for social disorder. The classic example being the Sudanese slavery trade system which reflects that even the best intended action can bring about adverse consequences.

Chapter 7 discusses Profit and Loss from a purely mathematical perspective, whereby wage, rent and interest are taken as earned income established in advance by contracts to reduce uncertainty. Profit as the residual between revenue and cost is also differentiated in accounting and economics. The function of the futures market is as a hedging tool because a society that prohibits profit is said to undermine responsibility.

Chapter 8 maintains that the popular Theory of Price is insufficient to explain many unwarranted incidents including bankruptcy. The choice of price discrimination either via special discount coupons or proper use of price elasticity information is to increase net revenue, conditional upon certain factors.

Chapter 9 elaborates on Competition and Government Policy and their complementary roles. Strict defining of the degree of competition has the tendency to ignore the function of enterprises. Restrictions are supposed to aim for fair and not free competition although the use of mergers and Antitrust Laws are meant to protect key industries, such as banking and finance. Furthermore, there are costs (substantial normally) involved in changing market structures and business practices.

Chapter 10 discusses Externalities and Conflicting Rights in general. Costs and benefits not taken into account when making decisions are known as externalities. Internalizing the negative externalities through means of negotiations (in the case of managerial issues), policies (taxation) and other legislative measures will help minimize social problems and clarify rights.

Chapter 11 addresses Market and Government with focus on the key question in constitutional political economy. The author cautions that making the right choice is not as clear cut as our public policy debates often make it seem. The concepts of self-interest, competition and individualism are presented to show that the distinction between the two institutions can be blurred upon close scrutiny in practice, with an exception. Governments possess a generally conceded and exclusive right to coerce people, particularly when transactions costs become high to exclude non taxpayers from the free riding.

Chapter 12 on Measuring the Overall Performance of Economic Systems previews the widely used gross indicators in macro analysis together with the factors causing their fluctuations, the limitations of national income accounting and the dangers of aggregation.

The final chapter, 13, themed The Wealth of Nations: Globalization & Economic Growth discusses why some economic systems accomplish much more than others. The differences of natural endowments are unable to explain the disparities in wealth, nor the ratios of population to land. Unprecedented phenomenon of sustained economic growth emerged in human history because some nations managed to create conditions under which the majority could specialize and exchange. However, economic development is a function of people, resource and institutions. Another pre-requisite is the possibility of exchange at low cost, accumulation of capital stocks and technological innovation. Ideas and resources from the minds of people are said to be lacking in poor countries. The chapter discusses globalization as an issue deserving due attention and finally brings up the mostly long term benefits of international trade.