

Bernard Lonergan

**Notes on Economic Topics - 1
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Lionel Robbins, An Essay on the Nature and Significance of Economic Science MacMillan 1932

p15 "Economics is the science which studies human behaviour as a relationship between ends and scarce means which have alternative uses."

p16 "The conception we have rejected, the conception of Economics as the study of the causes of material welfare, was what may be called a classificatory conception. It marks off certain kinds of human behaviour, behaviours directed to the procuring of material welfare, and designates these as the subject-matter of Economics. Other kinds of conduct lie outside the scope of its investigations. The conception we have adopted may be described as analytical. It does not attempt to pick out certain kinds of behaviour, but focuses attention on a certain aspect of behaviour, the forces imposed by the influence of scarcity. It follows from this, therefore, that in so far as it offers this aspect, any kind of human behaviour falls within the scope of Economic Generalizations. We do not say that the production of potatoes is economic activity and the production of philosophy is not. We say rather that, in so far as either kind of activity involves the relinquishment of other desired alternatives, it has its economic aspect. There are no limitations on the subject-matter of Economic Science save this."

BL 1/classificatory = material object analytical = formal object
2/ scarcity & alternatives one aspect that underlies all generalizations known to Robbins: a synthetic explanatory unity of these generalizations; but are there not other formal objects? e.g. Economics of Exchange

p.17 "...within the wide field of our definition, the attention of Economists is focused chiefly on the complications of the Exchange Economy. The reason for this is one of interest."

p.17 "Now as Prof. Mises has shown, given central ownership and control of the means of production, the registering of individual pulls and resistance, by a mechanism of prices and costs is excluded by definition. It follows, therefore, that the decisions of the executive must necessarily be 'arbitrary.' That is to say, they must be based on its valuations - not on the valuations of consumers and producers."

p.19 "The generalizations of the theory of Value are as applicable to the behaviour of isolated man or the executive authority a communist society, as to the behaviour of man in an exchange economy - even if they are not so illuminating in such contexts. The exchange relationship is a technical incident, an incident indeed which gives rise to all the interesting complications, but still, for all that, subsidiary to the main fact of scarcity."

p. 20 "Prof. Schumpeter ... has attempted ... to vindicate the latter definition by demonstrating that it is possible to conceive all the fundamental aspects of behaviour germane to Economic Science as having the form of exchange" possible construction C criterion N

p. 23 "...in so far as [the achievement of] any end is dependent on scarce means, it is germane to the preoccupations of the Economist"

p. 24 The economist is not concerned with ends as such. He is concerned with the way in which the attainment of ends is limited. The ends may be noble or they may be base. they may be "material" or "immaterial" - if ends can be so described. But if the attainment of one set of ends involves the sacrifice of others, then it has an economic aspect."

p. 25 Let us suppose this reprehensible community to be visited by a Savonarola. Their former ends become revolting to them. The pleasures of the senses are banished, the sybarites become ascetics. Surely economic analysis is still applicable. There is no need to change the categories of explanation. All that has happened is that the demand schedules have changed. Some things have become relatively less scarce, others more so. The rent of vineyards falls. The rent of quarries for ecclesiastical masonry rises. That is all. The distribution of time between prayer and good works has its economic aspect equally with the distribution of time between orgies and slumber. The "pig-philosophy" - to use poor Carlye's contemptuous name for Economics - turns out to be all embracing."

p. 29 "... rejection of material comfort in favour of aesthetic or ethical values does not necessarily bring material compensation ... So far from postulating a harmony of ends in this sense, Economics brings into full view that conflict of choice which is one of the permanent characteristics of human existence. Your economist is a true tragedian."

p. 31 "Economics, then, is in no way to be conceived as we may conceive Ethics or Aesthetics as being concerned with ends as such. It is equally important that its preoccupations should be sharply distinguished from those of the technical arts of production."

e.g. roof of house paper? slate? technology How to build a house?

p32 Economics is not the aggregate of the technologies[.] nor is it an attempt to select from each the elements common to several."

p.34 "...the problem how much wood to use for fires and how much for fencing" = Economics - How [to] make a fire, a fence, = Technique

p.37 "Economists are not interested in technique as such. They are interested in it solely as one of the influences determining relative scarcity."

p37 Economic theory set of relationships regarding disposal of scarce means
Economic History instances of such relationships

p.40 Descriptive Economics economic history of today

p.42 Materialist interpretation of history = "History is the epiphenomena of technical changes
The history of tools is the history of mankind"

p.43 "There are no autonomous changes on the demand side. What changes occur are, in the end, attributable to changes in the technical machinery of supply. There is no independent "psychological" (or for that matter, "physiological") side to scarcity. No matter what their fundamental make-up, be it inherited or acquired, men in similar technical environments will develop similar habits & institutions. This may be right or wrong, pseudo-Hegelian twaddle or profound insight into things which at the moment are certainly not susceptible of scientific analysis, but it is not to be deduced from any laws of theoretical Economics."

p44 "From the point of view of Economic science, changes in relative valuations are [given] data.*¹

¹"Given" is added by Lonergan. Hereafter [] sections are additions by Lonergan to quoted text.

p.47 Violent change in demand schedules - Armistice 11 a.m Nov. 11, 1918 ²

"The ends had changed. The scarcity of means was different."

p.49 {"}The mass production of particular things irrespective of demand for them, however, technically efficient, is not necessarily "economical"

p.50 "fallacy of misplaced concreteness" Whitehead's remark applied to production without demand, "disuse of capital that is big but obsolete, etc."³

p.52 Inflation -> 1/ over-expansion of capital α low interest rates reduce fixed costs

β flight from money to goods B.L.

2/ inflation ceases to inflate and not possible to run these undertakings
however technically efficient

p53 "...during times of inflation, the artificially low rates of interest tend to encourage the expansion of certain kinds of capitalistic production in such measure that, when the stimulus is exhausted, it is no longer possible to work them as profitable undertakings. At the same time liquid resources are dissipated and exhausted. When the slump comes the system is left high and dry with an incubus of fixed capital too costly to be worked at a profit, and a relative shortage of "fluid capital" which causes interest rates to be stringent and oppressive. The beautiful machinery which so impressed the newspaper correspondents is still there, but the wheels are empty of profit."

p54 "Reckoning is by "weight and tale" or by valuation - so many tons of coal or so many pounds sterling worth of coal physical computations may be unimpeachable and, in certain connections useful, yet from the point of view of the economist they have no significance apart from relative valuations."

²The example is from the Robbins text.

³Not a direct quote from Robbins.

Relativity of Economic Quantities

p.56 "...the valuations which the price system expresses are not quantities at all. They are arrangements in a certain order. To assume that the scale of relative prices measures any quantity at all save quantities of money is gratuitous metaphysics⁴

p.56 "...the addition of prices or individual incomes to form social aggregates is an operation with a very limited meaning. As quantities of money expended, particular prices and particular incomes are capable of addition and the total arrived at has a definite monetary significance. But as expressions of an order of preference, a relative scale, they are incapable of addition. Their aggregate has no meaning.

p. 57 "If we like to assume that preferences and property do not change rapidly within short periods, and that certain price changes may be regarded as particularly significant for the majority of economic subjects, then no doubt we may assign to the movements of these aggregates a certain arbitrary meaning which is not without its uses.

p.58 Redistribution of incomes - "For a substantial proportion of the high incomes of the rich and due to the existence of other rich persons. Lawyers, doctors, the proprietors of rare sites, etc., enjoy high incomes because there exist people with high incomes who value their services highly. Redistribute money incomes the main initial result would be a rise in the prices of articles of working-class consumption If we compute the proportion of the population now producing real income for the rich who could be turned to producing real income for the poor, it is easy to see that the increase available would be negligible. ["]

⁴In the second edition [1935] Robbins replaces "quite unnecessary" where the the first edition text of 1932 reads "gratuitous metaphysics." Lonergan was reading the 1932 edition.

p.62 "...though at every moment⁶ there are tendencies towards equilibrium, yet from moment to moment⁶ it is not the same⁷ equilibrium towards which there is movement"

p.66 "a change in the aggregate of production is not a definite conception"

p. 67 note The theory of money ... has continually employed pseudo-concepts of the sort we have just declared suspect-the price level, movements of purchasing power parities, etc. But it is just here that the difficulties of monetary theory have persisted. And recent improvements in monetary theory have been directed to eliminating all dependence on these fictions."

p69 "The beginning of the change dates from the coming of the Subjective Theory of Value. So long as the Theory of Value was expounded in terms of costs, it was possible to regard the subject-matter of economics as something social and collective and to discuss price relationships simply as market phenomena. With the realisation that these market phenomena were, in fact, dependent on the interplay of individual choice...

p.70 In the modern treatment discussion of "production" is an integral part of the Theory of Equilibrium. It is shown how factors of production are distributed between the production of different goods by the mechanism of prices and costs, how given certain fundamental data, interest rates, and price margins determine the distribution [of factors] between production for the present and production for the future. The doctrine of division of labour, heretofore so disagreeably technological, becomes an integral feature of a theory of moving equilibrium through time. Even the question of "internal" organization and administration now becomes related to an outside network of relative prices and costs; and since this is how things work in practice, what is at first sight the greater remoteness of pure theory in fact brings us much nearer to reality."

⁶"at every moment" is italicized in the Robbins text.

⁶"from moment to moment" is italicized in the Robbins text.

⁷"same" is italicized in the Robbins text.

The Nature of Economic Generalizations

p.73 "...in a free market, intervention by some outside body to fix a price below market price will lead to an excess of demand over supply."

p.74 "history does not proceed by way of generalising abstraction."

"The vulgar notion that the safe methods on political subjects are those of Baconian induction-that the true guide is not general reasoning but specific experience-will one day be quoted as among the most unequivocal marks of a low state of the speculative faculties of any age...Such reasoners ignore the fact of Plurality of Causes in the very case which affords the most signal example [of it]. (John Stuart Mill, Logic, chap X, ¶ 8.)

p. 75 Let us look more closely at the arguments by which it is established. The proposition that a price fixed below the equilibrium point must result in an excess of demand over supply is a simple corollary of the general Theory of Price. According to that theory, the equilibrium price must be conceived as that price which restricts demand to the available supply. It follows quite simply that if the price is lower than this, the necessary restriction will not be effected. Demand which would have been excluded by the higher price will arise and there will be disequilibrium...

"If there were no demand beyond the available supply, and no alternative use for the factors of production involved, there would be no price. The good would not be scarce in relation to the demand for it. It would be a free good."

"In the last analysis, therefore, our proposition rests upon deductions which are implicit in our initial definition of the subject-matter of Economic Science as a whole. Economics is concerned with the disposal of scarce goods with alternative uses."

N.B. "In a free market" equilibrium price - that to which there is a tendency C
-that which actually exists N
"scarce" relation to individuals taken singly C to collectivity N.

p.77 "On the analytical side Economics proves to be a series of deductions from the fundamental concept of scarcity of time and materials"

"...it is not always realized how far the theoretical developments of the last half century have resulted in unifying analytical economics on the laws we have indicated... Unless it is made quite clear that in the marginal analysis we possess the basis for a completely unitary economic theory, it is safe to say that the inner significance of that analysis has not been recognised at all."

p.80 "In the end, subjective valuations govern costs equally with productive prices"

p.81 The intricate interrelationships of the stationary state all resolve themselves into what Pareto called an equilibrium of tastes and obstacles.

p. 82 "For the community as a whole, the quantity of money may be a matter of indifference. But for the individual with given resources, to keep a certain proportion of these resources available in the form of free cash is in itself a convenience. Hence there arises a demand for money to hold - a relative valuation of cash and other resources which is expressed "in" the system of prices... the old conception of velocity of circulation can be derived from modern conception of demand for money: the thing has been done very frequently (Pigou, Essays in Applied Economics pp. 174-8)

p.83 "In pure Economics we examine the implications of the existence of scarce means with alternative uses"

p.83 "The borderlands of Economics are the happy hunting-ground of the charlatan and the quack."

p. 84 "It is well-known that certain of the founders of the modern Subjectivity theory of Value did in fact claim the authority of the doctrine of psychological hedonism as sanctions for their propositions," This is not true of the Austrians (Menger, Böhm-Bawerk) "True of Gossen Jevons, Edgeworth.

p.85 "no one who was acquainted with modern value theory could honestly continue to argue that it has any essential connection with psychological hedonism

p.86 "...all that is assumed in the idea of the scales of valuation is that different goods have different uses and that these different uses have different significances for action, such that in a given situation one use will be preferred before another and one good before another. Why the human animal attributes particular values in this behavioristic sense to particular things, is a question which we do not discuss."

p.87 "The fundamental concept of economic analysis is the idea of scales of relative valuations; and, as we have seen, while we assume that different goods have different values at different margins, we do not regard it as part of our problem to explain why these particular valuations exist. We take them as given data. So far as we are concerned, our economic subjects can be pure egoists, pure altruists, pure ascetics, pure sensualists, or what is much more likely - mixed bundles of all these impulses."

p.89 "If it is assumed -that - I always buy from the cheapest seller, it is not assumed that I act for egotistical motives."

p.91 "It is the most elementary implication of the idea of scarcity that if a price is lowered the demand tends to increase."

p.92 Change in price: primary effect, demand A for that good.
secondary effect, demand B for other goods [if A unaffected, B must be more or less income left]⁹

p. 93,4 "In the first place it can deal with changes in the distribution of goods which occur as a result of the equilibrating tendencies. This indeed is the function of the Theory of Equilibrium. ...

"In the second place

"And, secondly, it can assume changes in the given structures and describe the difference between the new equilibrium and the old. It can assume the removal of a tax, the importance of a new obstacle, the effects of change in certain property relationships. As is well known this is one of the main foundations of the Theory of Variations

"But can it not describe the laws of change in the given data themselves?--

⁹[] are Loneragan's.

Re Statistic - average elasticity of demand, etc.

p101 "However accurately they describe the past, there is no presumption that they will describe the future...Important as such investigations may be, at the moment at which they are made and perhaps for a short time after, there is no justification for claiming for their results the status of so-called "statistical" laws of the natural sciences" cf Ross

p.106 Empirical studies reveal discrepancies between theoretical terminology and facts e.g what is money now, 100 yrs ago. p107 Empirical studies expose areas where pure theory needs to be reformulated and extended. They bring to light new problems.

p107 "Pure equilibrium theory, as is well known, does not provide any explanation of the phenomena of booms and slumps"

p109 "Realistic studies may suggest the problem to be solved. They may test the range of applicability of the answer when it is forthcoming. But it is theory and theory alone which is capable of supplying the solution. Any attempt to reverse the relationship must lead inevitably to the nirvana of purposeless observation and record."

p111 " ...Economic Science knows no way of predicting what will be the given data at a particular point of time. It cannot predict changes in valuations. But given the data in a particular situation, it can draw inevitable conclusions as to their implications. And if the data remain unchanged, those implications will certainly be realised. They must be for they are implied in the presence of the original data."

p113 Note "The alleged advantage of economic "planning: - namely that it enables greater certainty with regard to the future-depends upon the assumption that under "planning" the present controlling forces, the choices of individual spenders and savers, are themselves brought under the control of the planners. The paradox therefore arises that either the planner is destitute of the instrument of calculating the ends of the community he intends to serve or, if he restores the instrument, he removes the *raison d'être* of the "plan". Of course, the dilemma does not arise if he thinks himself capable of interpreting these ends or ...if he has no intention of serving any other ends but those he thinks appropriate... Scratch a would be planner and you usually find a would-be dictator."

Marginal theory does not compare Jones scale of values with Smiths and say that Jones is greater, more important, -- Jones alone, Smith alone
Hence fallacy to argue --marginal utility to poor greater than to rich, \therefore more even distribution.

p125. "...all that part of the theory of Public Finance which deals with "Social Utility" goes by the board."⁹

p.127 "To show that, under certain conditions, demand is satisfied more adequately than under any alternative set of conditions, does not prove that that set of conditions is desirable. There is no penumbra of approbation round the Theory of Equilibrium. Equilibrium is just equilibrium."

p129 "We cannot say that the pursuit of given ends is uneconomical because the ends are uneconomical; we can only say it is uneconomical if the ends are pursued with an unnecessary expenditure of means."

"...there are no economical ends."

p130 "It is a well-known generalization of Theoretical Economics that a wage which is held above the equilibrium Level necessarily involves unemployment and a diminution of the value of capital."

i.e. more leisure or less to support leisure

p133 "Propositions involving the verb "right" are different in kind from propositions involving the verb "is."

p139 "...It is clear that many of our most pressing difficulties arise ... because our aims are not co-ordinated. As consumers we will cheapness, as producers we choose scarcity....We call for cheap money and lower prices, fewer imports and a larger volume of trade.

⁹In the second edition [1935] Robbins replaces "goes by the board." with "must assume a different significance."

Knight, F.H. Risk, Uncertainty, and Profit Houghton Mifflin Company, Boston and New York, 1921.

"Law of Choice" p.93 = correct form of principle of utility

p.64 "When confronted with alternative, quantitatively variable laws of action or experience, we tend to combine them in such proportions that the physically correlated amounts or degrees of each are of equal utility to the person choosing."

"The phrase 'equal utility' -- should be taken to refer to the fact of indifference of choice and not a comparison between quantities in the true sense."

p.65 "...if a given unit of a given resource is yielding in one use a want satisfaction preferable to that which a similar unit is yielding in another, the yield of that resource can be increased by transferring some of it from the second use to the first until the importance of the one is increased and of the other decreased to the point of equivalence."

p.64 Note all utility is relative - this is more useful than that - problem of choice between alternatives because of scarcity - if choice, then preference no matter what the motives may be [philosophic & ethical neutrality] of Robbins

hence a subjective equilibrium is the subject's law of choice

Re p.65 if he does not effect transfer, then he does not "prefer"

pp.5,6,7,8,9,10,13,15

73,75,77,86,90,93,100ff.

p.93 "that 'goods' are largely alternative to each other in production (involving the use of the same ultimate resources) is the condition of our having an economic order, an organization of want satisfying activities based on free production and exchange."

F.H. Knight

p122 "The equilibrium condition or long-run tendency for the static state has now been formulated in three ways from as many different standpoints. From the stand-point of distribution, every agency must be in the situation where it can make the greatest possible value contribution to the social income and be valued by the contribution which it makes. From the stand-point of consumption goods, prices must be such that rates of production and consumption are equal or that costs and selling prices per unit are everywhere the same. It is important to see clearly that these statements are logically equivalent, presenting different aspects of the same phenomena. It is self-evident that costs of goods are identical in the aggregate with distribution shares, and both with prices of goods; all these are in fact different names for the total income of scarcity. A formulation including all these statements would be that consumption goods and productive sources would be so priced that equal price amounts of the second make equal price contributions of the first which have equal utilities to all persons in the system. It is really self-evident that this condition alone can be stable, that any other gets forces to work to bring it about."

[in the margins]

lp. 180 It is important that we bear in mind that the serpent's tail is always in the serpent mouth, that what the competitive system tends to give back is just what is put into it in the way of human motives and human powers, natural, acquired, or conferred and has in itself no moral attribute whatever."

p. 168 "It is quite unnecessary to believe that there will be any progress toward equilibrium"

p. 292 There is only one end finally, to business activity and this is already decided upon before the business is founded; that is, to make money."

p.124, 128, 139, 141

p. 150 "In accordance with the law of diminishing returns and the specific productivity theory based upon that law, a relative increase in the supply of labour will increase the product of industry less than proportionally and decrease the relative productivity of labour. Both effects tend to lower wages per man. The same reasoning applies to any other productive service as well as to labour. "

157, 163n 165, 167, 168, 172, 176F, 179ff -183, 187, 189, 191, 192, 193, chap IX, 240, 252, 254.

p297. "The crucial decision is the selection of men to make decisions; any other sort of decision - making is automatically reduced to a routine function."

Prices

Free goods & services

- { vs. permanent scarcity relative to any individual
- { no incidental scarcity relative to any regular series of individuals

Scarce objects

- I Authoritative - Orders of Rationing - Paternalism, Slavery, Socialism
- II Free Consent

Two solutions of problems of | when does who give, do, sacrifice how
| much of what & whether this is in
| return for or in anticipation of how great
| much of what reward

Market equilibrium

What is it? Balancing of present supply against past, present or future supply

How does it work? α Uniform prices caeteris paribus no reason to give A
more than one would B asks or to take
less from C than D will give.
General because equilibrium solution

future β At level where supply equates w[ith]¹⁰ demand [demand - past present supply]
i.e. one assumption of equilibrium solution
i.e. price is the deterrent restricting demand to supply
 α short term supply fixed
 & deficient - urgent buyers bid up price to get goods at once
 & excessive - urgent sellers lower price to get rid of goods
 β long term supply potential
 { rising prices encourage production
 { falling prices discourage production

Ultimate basis Law of diminishing utility

- 1) Utility is decisive as to necessity etc. of scarce object
- 2) The greater the supply the lower the utility that is served at the margin
- 3) The valuation of the marginal utility holds for the category under uniform price

¹⁰alternate reading "At level where supply equates to demand"

Theoretical Background of Market Equilibrium

Economics deals with "scarce" objects of choice - where scarcity is elastic, it can be reduced by greater effort - when scarcity is multiple alternative, the same resources can yield different products by being combined in different ways.

Tendency to equilibrium = scissors of selling price decreasing from decreasing utility and costs increasing from increasing effort required to reduce scarcity still more (diminishing returns).

Law of Diminishing Utility

Any object first is used meet max. needs, desires, & then a descending scale of lesser needs & desires --(individual)

Different uses in descending scale $U_1, U_2, U_3, U_4, \dots$

Increasing rates of use in each category DQ_1, DQ_2, DQ_3, DQ_4

When DQ is so much every so often of fungible goods & services & so intensive a use (1 hr a wk, 24 hrs a day) of durable goods.

Because price is uniform for any unit, price of object will not be greater than valuation placed on marginal use-unit used.

Laws of Diminishing Returns (increasing costs)

Object is product of labour & land

From a given quantity of land (any non human factor) the product first increases more rapidly than increase of labour, then less rapidly & finally there is no product at all from totally insufficient or totally excessive application of labour. the proposition is reversible - from given quantity of labour & varying quantities of land -

Where increasing returns, better to use less land -total product could be greater when diminishing returns, rent on land of better quality equivalent to less labour required - value of labour of additional product resulting from additional unit of labour applied - Importation

Disturbance of Equilibrium i.e. setting up totally new equilibrium to which to tend

- 1 New utilities
- 2 New productive combinations

Diminishing utility (productivity as particular case)

1 With respect to rates of flow "dq"

intensity of use of durable goods [piano, [1 hr. a wk.], 24 hrs -day etc.]
so much every so often of fungible goods and services

2 Arrange different categories of use of same object in descending scale of utility

$U_1, U_2, U_3, U_4 \dots U_n$

where U_n is the marginal type of use

3 Arrange within each category each successive increment of DQ (each dq)

in descending scale of utility

$dq_{11}, dq_{12}, dq_{13}, dq_{14} \dots$

$dq_{21}, dq_{22}, dq_{23}, dq_{24} \dots$

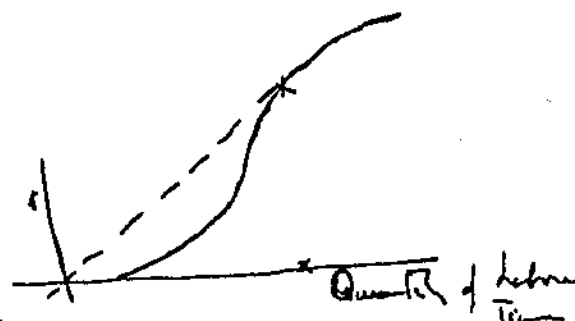
etc.

4 In case of joint utility, joint demand, in which component factors are not fixed parts of same thing then (7) variable ratios in use possible

eg. more or less labour on same quantity of land

greater or less intensity in use of piano

General	Physical
Utility	Output



Diminishing returns

eg quantity of land fixed

before x , concave upwards, increasing returns

after x , concave downwards decreasing returns

with increasing returns of labour it would be better to use less land if labour cannot be increased - because output per unit labour greater - if labour can be increased, demand strong & prices of labour rising

with decreasing returns for labour, more & more land will be called into use (less productive land at least in long run) & so in long run rents average on better land.

Theory holds for any variable combination of two factors

viz

1) product per unit of both agencies (factors) increases

2) product per unit of relatively increased agent decreases & of relatively decreased agent increases

3 stages

3) product per unit of both either agent decreases

as V_1 & V_2

[unless alternative uses, no competitive system possible]

increased from $0 \rightarrow \infty$

Fields in which market equilibrium operates

- 1) Services, fungible goods, durable goods - Market price
- 2) Use of durable goods -rent
- 3) Correlation - Discounted capitalization of rents = Market price of durable goods
- 4) Capacity to supply goods & services at future date

Present supply of factors - demand for consumption goods

vs

Estimate of future annual rates of profit [- interest on monetary capital]

Diff [future prices - present costs] = profits (theoretical)

Enterprise flows to fields of max. annual rate of profit, diminishes prices & profits in that field & so serves internal equilibrium of investment opportunity - i.e. brings profits down to zero.

Fields in which market equilibrium operates

1 demand = past, present, future supply

Demand A = present supply of consumer services, fungible goods, durable goods - Market Price A

Demand B = use not ownership of durable goods - rent Market Price B

Demand C = productive services - wages Marker Price C

Demand D - maintained or increased capacity to supply goods & services at future date

i.e. Estimate of future annual rate of profit $1/t [p v r f + /y -1]$

= Present supply of factors - demand for factors for consumption goods

Correlations (1) Market price of durable goods (A) - capitalized value of rents
[discounted at least if perpetual]

(2) Rent & wages are complementary

Rent is the saving in labour on more advantageous non-human factors

Wages are the additional product resulting from added unit of labour

If rent is defined as saving
in labour, then $R + W$
must equal selling price

~~Unless theoretical conditions selling price = $W + R$ when "W" and "R"~~
~~—vary according as undertaking has better or worse land~~

(3) Demand for factors for consumption goods restrained by increasing rate of
interest = increase in factors free ~~from~~ for producer goods
Estimate of factor annual rate of profit cut down by high rate of interest paid on loan
capital
Interest on loan capital a particular case of capitalized value vs rent income

Correlations (1) A & B
(2) A & (B & C)
(3) A vs. D & (B & C)
↑
D is future A

Schumpeter, Theory of Economic Development, Harvard, 1934
Eng Trans.

p166 "Within the normal course of the circular flow there is no reason at all to be aware of the value of land as such....Land ...is not sold in the normal circular flow, but only its uses. Therefore only their values and not the value of land as such are elements in economic planning. And the process of normal circular flow can teach us nothing about the determination of the value of land. Only development creates the value of land; it "capitalises" rent, "mobilises" land. In an economic system without development the value of land would not exist at all as an economic phenomena." ¹¹

Cf my Distinction between "Redistributional & Operative Exchange"

p176 "In a communist or non-exchange society in general there would be no interest in an independent value phenomena."

B.L. only the initial massacre and subsequent purges -political phenomena

p177 "If entrepreneurs were in a position to commandeer the producers' goods which they need to carry their plans into effect, there would still be entrepreneurs' profit, but no part of it would have to be paid out by them as interest....the whole of what they make over and above costs would be "profits" to them and nothing else."

"Hence nothing essential is obscured in the picture of circular flow, if it is assumed that the means with which production is carried on consists of the products of preceding periods; but in the case of new combinations[,] entrepreneurs have no such products with which to procure means of production. herel,] then [,] the function of capital comes in, and it becomes evident that nothing corresponding to it can exist in a communist or even in a non-communist but "stationary" society."

¹¹The original text in *The Theory of Economic Development* reads: "In an economic system without development the value of land would not exist at all as a general economic phenomena."

Schumpeter, Theory of Economic Development

66 Development is defined by the carrying out of new combinations

- 1) a new good, object of supply - a new quality in object
new, i.e. relative to consumers in given field; one with which they are not familiar
- 2) a new method of production or of commercial distribution - one not tested by experience - not necessarily a new scientific discovery.
- 3) opening of a new market - one that did not previously exist for country in question
- 4) new source of supply (raw materials, half-manufactured goods) new to country in question
- 5) new organization (creation or destruction of monopoly position)

New combinations emerge

- | | | |
|----|----|---|
| 66 | 1/ | α from new men who compete against and eliminate the old |
| 67 | | β in socialist or trustified capitalism, from some economic unit |
| 67 | 2/ | α side by side with all other production forces & leads [?] to increase of raw materials & employment |
| | | β in competition with existing production for same materials & labour |
| 69 | 3/ | α existing firms purchase labour and materials out of receipts of circular flow |
| | | β new firms need credit at start, for no receipts as yet.
to supply such credit is function of <u>capitalists</u> . |
| 71 | 4/ | α traditional analysis: capitalist those who accumulate the production means needed for new enterprises |
| 71 | | β Schumpeter considers this a false problem: not accumulation but command enabling one to divert old uses to new combinations is the essence of the thing |
| 72 | 5/ | α traditional analysis: this purchasing power comes from "savings" 1/5 of annual income in Europe or N. America |
| 73 | | β Schumpeter: it comes from creation of purchasing power by banks
it does so often and de facto
it would always do so if no previous development |
| 74 | | <u>Banker is not the middle man of "purchasing power" but the producer of that commodity:
he is the capitalist par excellence</u> |

Schumpeter & Lonergan

My real and my circulation phases involve no distinction between growth (mere increase in size) and development (new production combinations)

For Sch. those two are specifically distinct - the new production function creates new situations that increase enormously the average of error and bring about the cycles.

However, the ideas of capital, credit, interest, etc. that Schum. advances appear more clearly & more generally & in more detailed a fashion - The relevance of Sch. insistence on development as opposed to growth is in the concatenation of the phases - e.g. Sch development can take place in my static phase if $DQ''_n > 0$ and if the new combinations are continuously offset by equal liquidations of former enterprises.

Schumpeter - Entrepreneur - Theory of Econ. Dev.

Entrepreneur - the man who carries out new production combinations, introduces new production functions - in so far as he does so

Routine work would require the intellect of a giant if not for habit and custom, for the fact that time hammers logic into men.

no difference between lending machine, managing, banking etc. [84]

85 But a new programme has to be based on intuition - "thorough preparatory work, [and] special knowledge, breadth of intellectual understanding, talent for logical analysis, may under certain circumstances be sources of failure" - the only proof of practicality is that it works - data, effects, counter-effects are infinite - but the new is untried.

p. 85,6 "The more accurately, however, we learn to know the natural and social world, the more perfect our control of facts becomes: and the greater the extent with time and progressive rationalisation, within which things can be simply calculated, and indeed quickly and reliably calculated, the more the significance of this function decreases. Therefore, the importance of the entrepreneur type must diminish just as the importance of the military commander has already diminished."

B.L. example from military commander reveals weakness of position - justification supposes Kondratieff downgrade - reliable calculation supposes absence of radical change i.e. Kon downgrade.

p. 86 Besides difficulty of untried from view-point of knowledge, also "difficulty from viewpoint of will" In the breast of one who wishes to do something new, the forces of habit rise up and bear witness against the embryonic project. A new and another kind of [effort of] will is therefore necessary in order to wrest, amidst the work and care of the daily round, scope and time for conceiving and working out the new combination and to bring oneself to look upon it as a real possibility and not merely as a day-dream. This mental freedom presupposes a great [mental] surplus force over the everyday demand and is something peculiar and by nature rare."

Entrepreneur

1. Intuition

2. Will

3. Opposition

1) existence of legal and political impediments
2) astonishment, condemnation, ostracism, physical prevention, direct attack simply because new.

especially α in threatened groups
 β in finding cooperation ↗ -finance
↘ -trained workers
 γ in winning over consumers

hence entrepreneur a leader¹²

not a capitalist who takes a risk
not a manager who come in when is established
not necessarily an independent agent - may be subordinate in ↗ - big corporation
↘ -socialist state

not an inventor or a discoverer who adds to knowledge
Leader acts principally by will [,] authority [,] personal weight

entrepreneur a peculiar leader¹³

those who follow are competitors who will annihilate his profit
→ leads not by argument, creating confidence, (exception banker), but by purchasing material & hiring labour
leads for formal profit.

Motives¹⁴ α dream or will to found a private kingdom, a dynasty - not mere hedonism desirability of efforts simply not counted
 β will to conquer, to succeed - like sport
 γ joy of creating, getting things done

$\beta \gamma$ possible in socialist state (α directed to palace intrigue B.L.)

p. 90 [But] We neither style every entrepreneur a genius or a benefactor [to] {of} humanity, nor do we wish to express any opinion about the comparative merits of the social organisation in which he plays his role, or about the question whether what he does could not be affected more cheaply or efficiently in other ways."

¹²See *The Theory of Economic Development*, p. 89.

¹³See *The Theory of Economic Development*, pp. 89-90.

¹⁴See *The Theory of Economic Development*, p. 90.

Equilibrium Rates of Interest

1. Notion of Equilibrium

Rate of surplus income = rate of automatic savings plus rate of interest & savings

surplus income = $DS = DE''_n - DE''_n - D \text{ ForTr. } D \text{ Budg.}$

automatic savings = large concentration of (wealth &) income

interest savings = DI'' that would be DI' if interest lowers.

2. Action of equilibrium - scissors

high rate cuts down DS & raises (perhaps slightly) interest savings

low rate stimulates DS & lowers (perhaps slightly) interest savings

3. Necessity of equilibrium

α otherwise P' basic price level has more than prosperity rise in boom and more than recession fall in basic expansion

i.e. | pure inflation when interest rate too low
| pure deflation when interest rate too high

hence since enterprise is based on calculation of prices & interest rates - excessive capitalist phase when P' too high & interest rate too low - & recession becomes sharp when P' too low & interest too high

we do not say that lack of equilibrium is the cause - it may be that entrepreneurs & managers do not sufficiently discount prosperity rise in P' and cannot ~~[?] banks do not permit them to discount recession fall in P' .~~

~~[4. Possibility of Equilibrium - doubtful because interest has upper and lower limits]~~

4. Limits of Variation in Interest Rate

Lower | 1. must meet banking cost (working capital)
| 2. must attract funds to carry on redistributive activity
| 3. must attract savings funds to purchase of new cap. equip.

Upper Must leave a margin of profit to the entrepreneur

5. Possibility of Equilibrium - Doubtful

in recession surplus income decreasing rapidly, automatic savings tricky [?]
interest cannot be lowered below banking costs, & this is not enough

in prosp. expansion surplus income increasing (automatic savings less rapid increase, interest possible but savings a new habit not required - i.e. income goes to new classes) bankers doubtfully actual unwilling to raise rate & spoil their business (Hayek)

If there is to be an equilibrium rate of interest [?] [?] must keep distinct

- A Bankers' costs 1. redistributional activity (liquidity of)
 2. supply of working capital

B Equilibrium: Rate of surplus income = Automatic savings plus interest savings

Roughly distinction between long-term & short-term interest rates

But (Schumpeter) has maintained that long-term financing is done in short term market

in A Banker is a prime cause

B Banker is a middle man

A must continue at all times, especially A_2

B has function of limiting surplus production to rate to which consumers consent

Working capital increases

- 1) cost of materials
- 2) cost of labour
- 3) number of new production units
- 4) turn from more labour-saving machines to more labour

~~Factor 4 needs an equilibrium~~

Factor 4 results from drop in real wages

Involves increase in rate of profit

Ricardo effect

Hayek 1939 essay

F. Hayek, Monetary Theory of the Trade Cycle, Jonathan Cape, 1933

p. 42.(n) "By 'equilibrium theory' we here primarily understand the modern theory of the general interdependence of all economic quantities, which has been most perfectly expressed by the Lausanne School of theoretical economics. " Fundamental Idea G.B. Say Théorie des Débouchés

p56 "The prevailing disproportionality theories are in agreement in one respect. They all see the cause of the slump in the fact that, during the boom, for various reasons, the productive apparatus is expanded more than is warranted by the corresponding flow of consumption; there finally appears a scarcity of [finished] consumption goods, thus causing a rise in the price of such goods relatively to the price of production goods (which amounts to the same thing as a rise in the rate of interest) so that it becomes unprofitable to employ the enlarged productive apparatus or [in many cases] even to complete it."

p60 "It is not, therefore, the simple fact of fluctuation in the production of capital goods (which is certainly inevitable in the course of economic growth) which has to be explained.¹⁶ The real problem is the growth of excessive fluctuations in the capital goods industries out of the inevitable & irregular fluctuations of the rest of the economic system, and the disproportional development[,] arising from these[,] of the two main branches of production."

p65 "Why do the forces tending to restore equilibrium becomes temporarily ineffective and why do they only come into action again when it is too late?"

p.68 "But the entrepreneur in a capitalist economy is not - as many economists seem to assume - in the same situation as the dictator of a Socialist economy.... In the modern exchange economy, the entrepreneur does not produce with a view to satisfying a certain demand (quantity of demand) ...but on the basis of a calculation of profitability; and it is just that calculation which will equilibrate supply and demand.

¹⁶In italics in Hayek text.

Hayek, Monetary Theory of the Trade Cycle

p.70 The other factor, no less important but all too often overlooked, is the price the producer has to pay for raw materials, labour-power, tools and ~~raw materials~~ borrowed capital - i.e. his costs. These prices, taken together, determine the extent of production for all producers operating under conditions of competition; and the producer's decisions as to his production must be guided not only by changes in expectations as to the {(selling)} price of his product [,] but also by changes in his costs. To show how the interplay of these prices keeps supply and demand [, production and consumption,] in equilibrium, is the main object of pure economics, and the analysis cannot be repeated [here] in detail. It is, however, the task of Trade Cycle theory to show under what conditions a break may occur in that tendency towards equilibrium which is described in pure analysis - i.e. why prices, in contradiction to the conclusions of static theory, do not bring about such changes in the quantities produced as would correspond to an equilibrium situation."

p75 "...the fact that every attempt to extend the productive apparatus must necessarily bring about, besides a rise in factor-prices, a further checking force - viz. a rise in the rate of interest."

B.L. interest rises only with increase in rate of producing [?] production goods apart from banking rules of thumb

p.75 "...all contemporary theories agree in regarding the function of interest as one of equalizing the supply of capital and the demand arising in various branches of production.

Hayek, Monetary Theory of the Trade Cycle

- p. 87 "Once we assume that, even at a single point, the pricing process fails to equilibrate supply and demand, so that over a more or less long period demand may be satisfied at prices at which the available supply is inadequate to meet total demand, then the march of economic events loses its determinateness and a range of indeterminateness appears, within which movements can originate leading away from equilibrium."¹⁶
- p. 114 "The rate of interest at which, in an expanding economy, the amount of new money entering circulation is just sufficient to keep the price-level stable, is always lower than the rate which would keep the [amount of] available loan-capital equal to the amount simultaneously saved by the public."

First cause of cycle. credit creation chap IV 169

- p. 179 "The determining cause of the cyclical fluctuation is, therefore, the fact that on account of the elasticity of the volume of currency media, the rate of interest demanded by the banks is not necessarily always equal to the equilibrium rate, but is, in the short run, determined by conditions of banking liquidity."¹⁷

cf.. Prof. F. A. Fetter, Interest Theories and Price Movements, American Economic Review¹⁸

"Throughout this process the much [-] esteemed elasticity of bank funds {(credit creation)} is the very condition causing, or making possible, the rising prices which stimulate the so called "needs of business". Truly a vicious circle, to be broken only by crisis and collapse when bank loans reach a limit and prices fall." cited in Hayek note p. 181 (Hayek italicizes).

cf. R.C. Hawtrey Monetary Reconstruction London 1926 2nd edit. ¹⁹

"so long as credit is regulated with reference to reserve proportions, the trade cycle is bound to recur."

Problem What are "business needs" What is equilibrium rate?

¹⁶Italics in Hayek text.

¹⁷In Italics in Hayek text.

¹⁸Vol. xvii, supplement, March 1927. Hayek notes see especially pp. 95ff.

¹⁹Hayek cites p. 135.

Hayek, Monetary Theory of the Trade Cycle

Credit creation does not merely affect basic price level

p. 128 "A rate of interest lowered by monetary influences, which must necessarily lead to the excessive production of capital goods."

B.L. production of capital goods is excessive when pure inflation - P' has more than prosperity rise but rate of interest can be lowered by monetary influences without this effect.

p128 "Wicksell and Mises both rightly emphasize the decisive importance of this factor in the explanation of cyclical phenomena, as its effect will occur when the increase in circulation is only just sufficient to prevent a fall in the price level."

p129 There also follows from credit creation

"changes in the relation of costs and selling prices and the consequent fluctuations in profits, which Professors Mitchell and Lescure in particular have made the starting point of their exposition; and the shifts in the distribution of incomes which Professor Lederer²⁰ investigates ...
"neither of these can be immediately connected with changes in the [general] value of money."

p.131 "The problem of cyclical fluctuations can only be solved satisfactorily when a theory of the money economy itself - still almost entirely lacking at present - has been evolved, comprising a detailed discussion of all those points in which it differs from the equilibrium analysis worked out on the assumption of a pure barter economy."

p.139 "...we constantly find those deviations of the money rate of interest from the equilibrium rate which, as we have seen, must be regarded as the cause of the periodically recurring disproportionalities in the structure of production."

²⁰Hayek cites Professor Lederer in *Grundriss der Sozialökonomik*, vol. iv, part 1, pp. 390-91.

Monetary Theory of the Trade Cycle Hayek

p.140 " the primary cause of the cyclical fluctuations must be sought in changes in the volume of money, which undoubtedly are always recurring and which, by their occurrence, always bring about a falsification of the pricing process, and thus a misdirection of production."

B.L. it is not change in volume of money but change in DE'/DE that changes structure of prices

p. 147 "The situation in which the money rate of interest is below the natural rate need not, by any means, originate in a deliberate lowering²¹ of the rate of interest by the banks. The same effect can be obviously produced by an improvement in the expectations of profit or by a diminution in the rate of saving, which may drive the 'natural rate' (at which the demand for and the supply of savings are equal) above its previous level; while the banks refrain from raising their rate of interest to a proportionate extent, but continue to lend at the previous rate, and thus enable a greater demand for loans to be satisfied than would be possible by the exclusive use of the available supply of savings. [Emphasis B.Ls].

B.L "exclusive use of available supply of savings" lets out expansion & ties one down to static phase or expansion = liquidation phase.

²¹"deliberate lowering" is in italics in Hayek.

- p.149 "- in principle an increase in the volume of cash, occasioned by an increase in the volume of trade, also implies a lowering of the money rate of interest... 77 (bl).
- p.152 "because the banks have no particular interest in keeping the supply of bank credit in equilibrium with the supply of savings."
- p.168 "...the natural rate of interest has risenThe reasons for this can be of very different kinds. ²² New inventions or discoveries, the opening up of new markets, or even bad harvests ²³, the appearance of entrepreneurs of genius who originate 'new combinations' (Schumpeter), a fall in wage rates due to heavy immigration; and the destruction of great blocks of capital by a natural catastrophe, or many others."
- p. 171-3" Which bank raises the rate? The one that wishes to lose business
- p.175 cites 10th yearly report of Federal Reserve Board, for 1923 (Washington 1924)
- "This is the usual sequence - an increase in deposits followed by an increase in currency. Ordinarily the first effect of an increase in business activity on the banking position is a growth in loans and deposits...Then comes a time when the increase in business activity and the fuller employment of labour and increased pay-roll call for an increase in actual pocket money to support the increased wage disbursements and the increased volume of purchases in detail."
- p176 Only so long as the volume of circulating media is increasing can the money rate of interest be kept below the equilibrium rate; once it has ceased to increase, the money rate must, despite the increased total volume in circulation, rise again to its natural level and thus render unprofitable (temporarily at least) those investments which were created with the aid of additional credit."

²²Hayek cites R.G. Hawtrey, *Trade and Credit*, London, 1928, p. 175.

²³Hayek cites V. P. Timoshenko, *The Role of Agricultural Fluctuations in the Business Cycle* (Michigan Business Studies, vol. ii, No. 9, 1930).

Hayek, Monetary Theory of the Trade Cycle

- 183 "For it is not the occurrence of a 'change in data' which is significant [,] but the fact that the economic system, instead of reacting to this change with an immediate 'adjustment' (Schumpeter) - i.e. the formation of a new equilibrium - begins a particular movement of ['boom'] which contains, within itself, the seeds of an inevitable reaction."
- 189 "So long as we make use of bank credit as a means of furthering economic development we shall have to put up with the resulting trade cycles. They are, in a sense, the price we pay for a speed of development exceeding that which people would voluntarily make possible through their savings[,] and which therefore has to be extorted from them."
- 199 "So long as the amount of credit obtainable at any given rate of interest is limited, competition will ensure that only the most profitable employments are financed out of a given amount of credit."
- 226 "...it is probably more proper to regard forced saving as the cause of economic crises than to expect it to restore a balanced structure of production." ²⁴ O.K. BL.
- 238 "...owing to the existence of banks, the equilibrating forces of the economic system bring about that automatic adjustment of all its branches to the actual situation."

²⁴Italicized in Hayek text.

Profits, Interest, Investment

Havek

1939 London

1 "Ricardo effect" - shift in profit schedules according to turnover period

2 Shift in multiplier & multiplicand quotient

Multiplicand - increment in demand for consumer goods dDE'

Multiplier - ratio between increment in demand for consumer goods dDE''/dDE' and increment in demand for producer goods

Quotient - inverse of multiplier i.e. dDE'/dDE''

3 Ricardo effect varies multiplier determinants [1 technological
[2 proportion of fixed to circulating capital

Increase in short-turnover profit schedules - decrease of multiplier

Increase in long-turnover profit schedules - increase of multiplier

Quotient [Profit increment in capital goods
↓ [Future & consequent increment (say after a year) of consumer goods
↓
↓ → → → → → → → → dDE'/dDE'' where numerator lags a year behind denominator[?]

Multiplier dDE''/dDE' simultaneous

Quotient inverted with effective zero rising to level of DE''

e.g. if $Q = 1/10$ then at constant rate of surplus expenditure

?
[bl] in ten years consumer goods are increasing 10/10
of increase in capital goods.

<u>Selling Price</u>	<u>Turnover Period</u>	<u>Profits</u>			
<u>Period years</u>	2	1	1/2	1/4	1/12
<u>Turnover volume</u>	24,000	12,000	6,000	3,000	1,000
<u>Annual rate of profit</u>	6%	6%	6%	6%	6%
<u>Profit on turnover</u>	12%	6%	3%	1 1/2%	1/2%

Suppose 1% rise or fall in selling price; therefore in rate of profit on turnover, provided wages and materials do not vary in price.

<u>Profit on turnover</u>	13%	7%	4%	2 1/2%	1 1/2%
	11%	5%	2%	1/2%	- 1/2%
<u>Annual rate of profit</u>	6 1/2%	7%	8%	10%	18%
	5 1/2%	5%	4%	2%	-6%

In general if Annual rate of profit is "A"
Increase in selling price is "dP" per cent
turnover period in years is "t"

then new annual rate of profit is $\frac{"A" + dP}{t}$

provided costs (wages & materials) do not vary

next page

Variations in the Annual Rate of Profits

$$\text{Annual Rate of Profits} = \frac{\text{Annual Profits}}{\text{Turnover Receipts}} = A$$

Turnover

Let V be annual volume of receipts - then outlay - receipts, so much every so often, say R every 1 years, so that $v_t = R$ and then "t" is turnover period. Defined as interval between outlay & receipts & new outlay: partly production period but prolonged when sales delayed, shortened when sales prompt.

<u>Other terms</u>	Quantity	Receipts	Variable Costs	Fixed Costs	Profits
per unit		p	v	ft/q	a
per turnover	q	pq	vq	ft	aq
per year	q/t	pq/t	vq/t	f	aq/t

$$\text{where } p = v + ft/q + a \quad a = p - v - ft/q$$

$$A = \frac{aq/t}{pq/t} = \frac{a}{p} = \frac{p - v - ft/q}{p} = \frac{1}{t} \cdot \frac{p - v}{p} - \frac{f}{pq}$$

$$= \frac{1}{t} \cdot \frac{p - v}{p} - \frac{f}{pq}$$

More accurately

$$\text{Annual rate of profits} = \frac{\text{Annual Profits}}{\text{Turnover outlay}} = A$$

$$A = \frac{aq/t}{vq + ft} = \frac{1}{t} \cdot \frac{aq}{vq + ft}$$

$$= \frac{1}{t} \left[\frac{p}{v + ft/q} - 1 \right]$$

$$= \frac{1}{t} \left[\frac{p}{v + ft/q} - 1 \right]$$

Implications of Variations in Annual Rate of Profit

1 There is no equilibrium rate of interest

Since $A_1 = \frac{1}{t} \left[\frac{p}{v + ft/q} - 1 \right]$ annual rate of profit is function

of turnover period in most fundamental way - to offset alterations of new profit schedule resulting from change in price & cost patterns, interest would have to be changed per turnover.

2 There is a "secondary wave"

Primary wave given by $C' p'' dq'' = (P' - C'kp') dq'$
where dq'' increases, forced savings $(P' - p'')$ increase, and then dq' increases as result of increased dq'' - Prosperity - recession

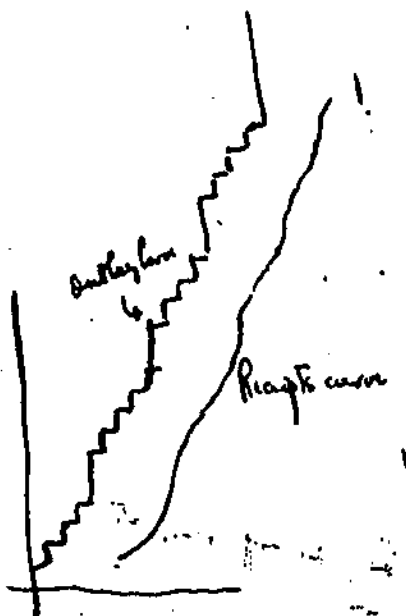
Secondary wave

- A Forced savings $(P' - p')$ increase; revise basic profit & schedules; new production (increment in dq') plus price lag (action of K) further increase of forced savings
- B Forced savings $(P' - p')$ can rise p' , p'' - further forced savings - which covers contraction expressed by increasing dq'
- C Rise in p' , dq' , p'' , dq'' , P' causes rise in P'' - surplus profit schedules revised in favour of short-turnover firms - rise in dq'' - further forced savings
- D Hence general up - saving till rise in full employment threatens pure inflation -- the banks tighten - prices begin to drop - revision of profit schedules in favour of long-turnover firms - elimination of short-turnover expansion

p. 147 "It is clear that it is entirely sound and, under certain restrictions, socially desirable economics to permit the practice of using loss leaders, provided the ratio of the sensitiveness of demand (for the economy) of the loss leader and its companion commodity is neither too small nor too large. The net effect of this is to increase the consumption of the loss leader and of the companion commodity and at the same time give merchants greater profits... Hence it is not at all necessary to require that all goods be sold above cost, nor is it desirable. Such a situation leads only to decreased consumption. In other words[,] the whole notion of selling every good on a cost plus basis is faulty: it is based on inadequate knowledge of joint demand.

p. 172 *Thus, in the problem as formulated here, operations of entrepreneurs are largely dependent upon whether they chose optimistic or pessimistic values of Y_p . Therefore employment depends to considerable extent upon entrepreneurial guesses of expected price and, of course, as already pointed out, of consumer income.* (italics in Roos)

→ BL. But consumer income itself depends upon entrepreneurial decisions in the aggregate.



Velocity of Money

1 Redistributional Price - neglect

2 Process

α Suppose series of productive factors
eg. series T_1 , series T_2 , series T_3 , etc

β [Receipts = Value of Production Graph corrected by increases or
[decreases in inventories
[Outlay = Step graph
[so much added every week
[so much added per month
[so much added per 6 mos

Smooth out step graph

Diff between ordinates
= $\sum P_i DQ_i + \sum dl_i$
= Consumer balances
= Trader Outlay

net outlay value of production in productive period
 \pm increases or decreases in inventories
= $P_i DQ_i + \sum dl_i$

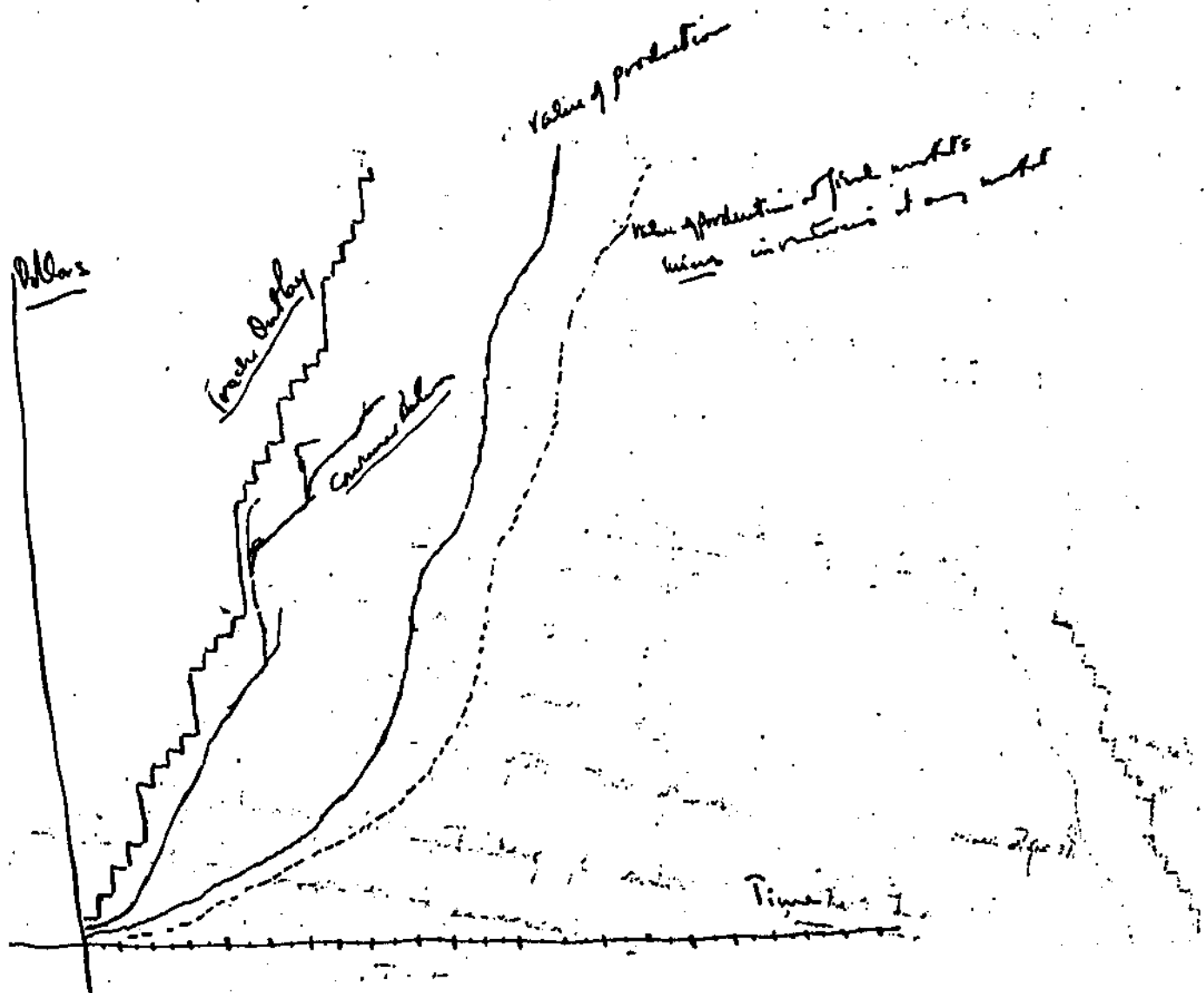
From Traders to Consumers $\sum_{i=1}^{i=n} P_i DQ_i$ & dl_i

γ Income step graph identical with outlay graph
Expenditure identical with receipts graph

Minimum difference = Basis for permanent loans to Redistribution Area

Max dif - Min dif = Basis for Call Loans, demand deposits

P.T.O.



Trader Outlay : a step function, so much per wk, per month, per quarter, per half year, etc.

Value of Production: at Final Market [Curve heightens α with shortening of every production period
 [β with rise in prices
 [Curve flattens α with lengthening of productive period
 [β with drop in prices

Inventories : anywhere along the line

x Value of production minus Inventories

x Trader Outlay minus [Value of production x minus inventories] plus x other sources
 = Consumer Balances

x Measure along ordinate

Banking is using consumer balances to create trader balances

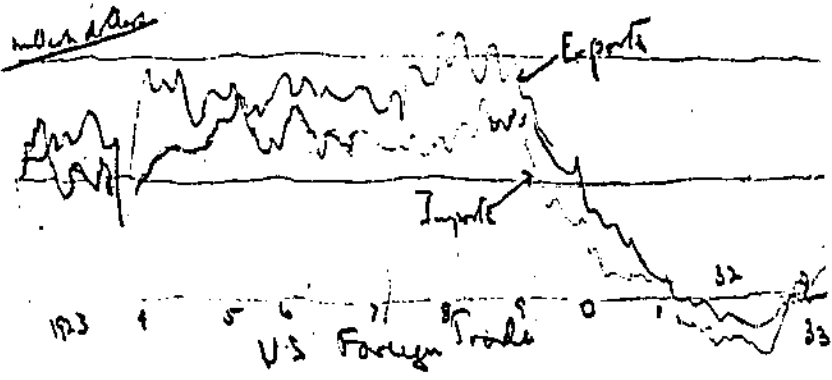
Ross Dynamic economics, p. 239

"The excess of exports over imports may be regarded as internal inflation of purchasing power"

Ross, p 222

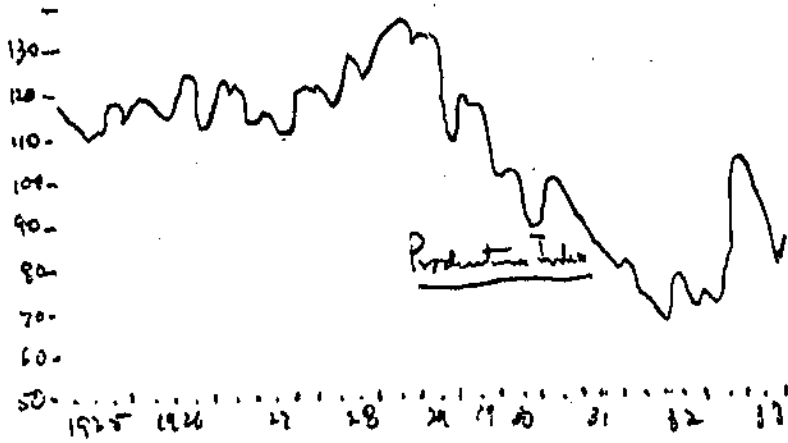
Ross p 222

Poss p. 223



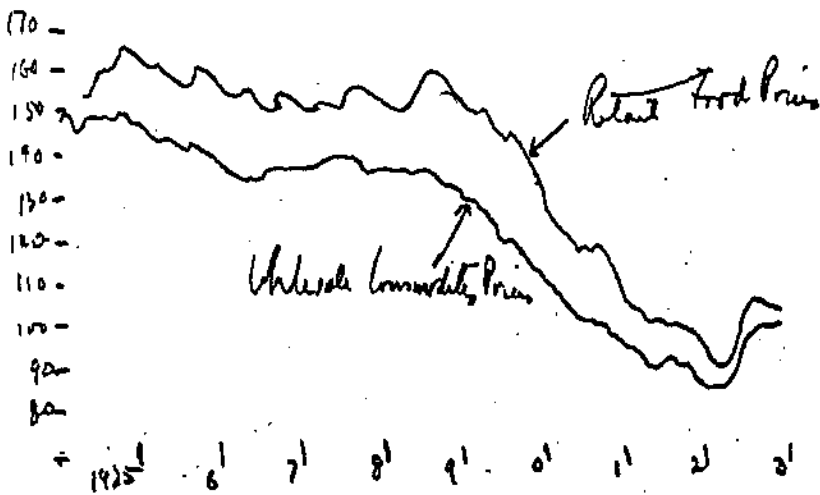
Ross dynamic economy p 229

"Excess exports over imports may be regarded as internal inflation & purchasing power"

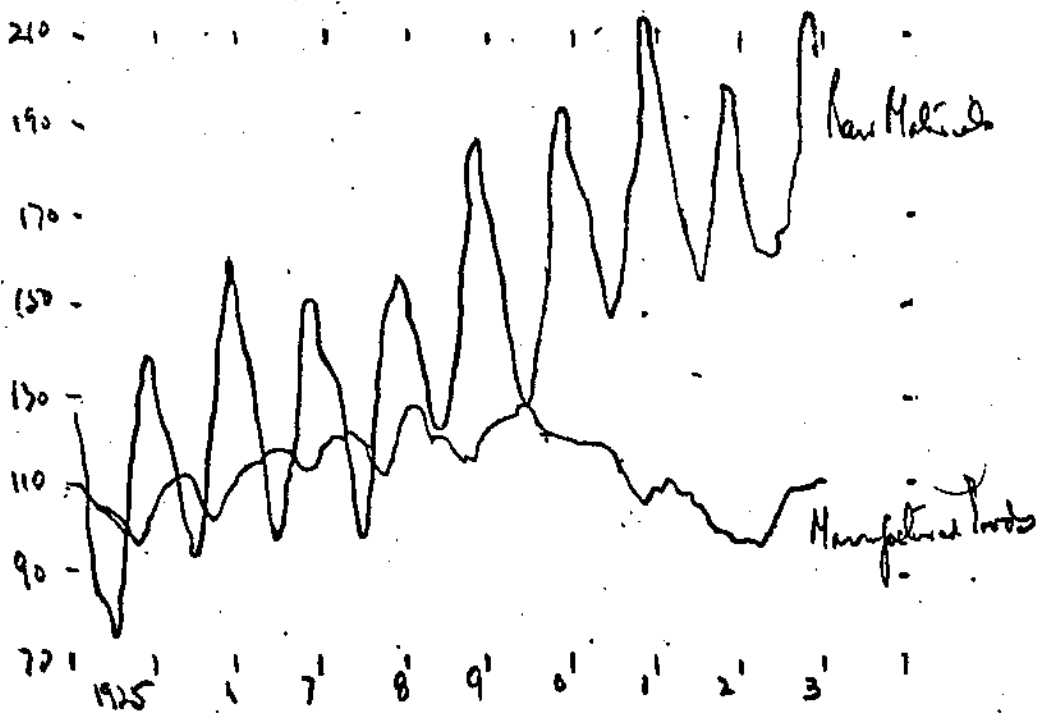


Ross p 222

Boyle Gys



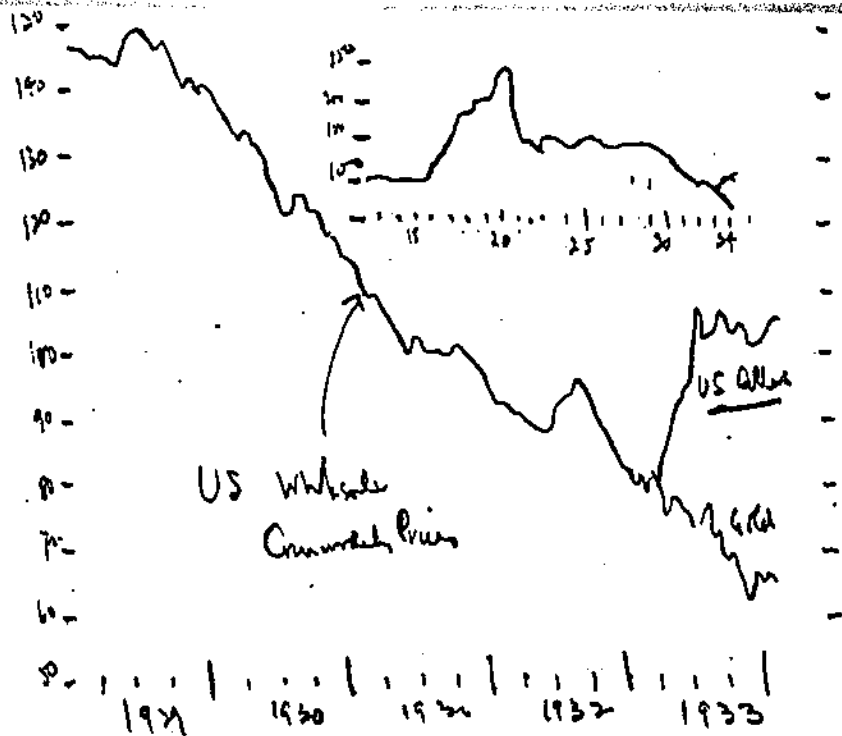
Ross p 222



Ross p 223

Inventories

Form.
234



Bernard Lonergan

**Economic Fragments
Archive Files A330-A334**

**Transcribed by Michael Shute
Memorial University of Newfoundland
St. John's NF A1C 5S7**

A330

$$\Gamma_{i1} \quad \Gamma_{i2} \quad \Gamma_{i3} \quad \Gamma_{i4} \quad \dots \quad \Gamma_{i(n-1)} \quad \Gamma_{in}$$
$$\begin{array}{ccccccc} \text{dr}_{i2} & \text{dr}_{i3} & \text{dr}_{i4} & & \dots\dots\dots & \text{dr}_{in} & \text{carry costs} \\ \text{s}_{i1} & \text{s}_{i2} & \text{s}_{i3} & \text{s}_{i4} & & \dots\dots\dots & \text{s}_{i(n-1)} & \text{S}_{in} \\ \text{ds}_{i2} & \text{ds}_{i3} & \text{ds}_{i4} & & & \dots\dots\dots & \text{ds}_{in} & \end{array}$$

$$\text{Cir. cap.} = r_{ij} + S_{ij} + \sum_{j=2}^{j=n} (dr_{ij} + ds_{ij})$$

dr. varies with increases in initial payments per turnover

varies with turnover frequency re? fixed costs
that are not "price -costs" wages per day

\underline{ds}_{ij} varies in increases in

s_{ij}	s_{2j}	s_{3j}	s_{4j}		transitional prices
					transitional quantities (depends upon <u>frequency</u> size)

 number of instances varies with frequencies

DM¹ Γ_{i1} Γ_{i2} Γ_{i3} re some from [?] contribution

Quantity is a function of frequency
Quantity + frequency = rate of payment per interval.

One may reflect that all this has been said before. But over one hundred years, practice followed in the wake by theory, has, moved away from the view that fluid prices and competition are the panacea for all economic ills and the guarantee of ever greater benefits. No doubt that view provided an effective means for enforcing the consistency of prices: it worked the whole world into a single market place. Again it gave a free hand to the entrepreneurs...

But it eliminated itself. ~~Competition is no more than an embargo upon a very valuable type of view Too harsh~~

Competition an embargo
Too harsh
An Age of corporations

Neither fluid prices nor competition

But not praise of fluid prices & competition
Not a norm but a mechanism, Definition

Review statements ===

Result __ But the ideal of mechanism: handle
the merely empirical. Postulate & effect enlightenment.

But ? prices

Prices & Acceleration

Prices: Mechanism [→for handling the merely empirical]
or Norm

Competition of Fluid Prices

- actual & potential consistency
- monopoly vs. potential competition
-

1) The rigidity inertia of real prices

$$q_i = q_i \cdot p_i$$

$$q_i = q_i \cdot p_i$$

$$dq_i = q_i dp_i + p_i dq_i + dp_i dq_i$$

suppose $dq_i = 0$

then dp_i and dq_i have to be opposite in sign

more means a lower real price

less means a higher real price

and everything cannot accelerate at once.

2) The problem of "more money"

- 1) mercantilism
- 2) Bills of exchange, banking
- 3) Gold standard
- 4) No gold standard

3) Booms an artificial acceleration

Slumps cutting out the artifice - propensity to consume max
for zero acceleration

A331

71 & 72

$$DM - DA = D^2R + D^2T$$

1 D^2R and D^2T same sign

2 if quantity added is greater than positive rate of absorption
then D^2R increasing interval after interval

if quantity removed is greater than negative rate of
absorption then D^2R decreasing interval after interval

3 true whether addition be DS DD \pm DG

4 D^2S depends on changes in DS in successive
intervals may be 0 with $DS + 0$ —

hence

$$D^2S + D^2R + D^2T = D^2t + D^2O$$

$$T = D^2t + D^2O$$

$$D^2S = 0$$

$$D^2R = D^2O + T \text{ interval after interval}$$

apart from adjustments

5 Hence - provided added money is not concentrated
by absorption [draining income velocities?] -
borrowed money is not replaced virtually by absorption
(increasing income velocities) - both limited - then

D^2R D^2T D^2O move up or down according to DS

with-str
intensification or change of trend D^2S || DD DG
stimulation

6. DO follows D²O

DR follows D²R

7. frequency acceleration

{ positive with expansion
negative with contraction

$$\begin{array}{rcl} 5 + 2^2 & & 7 \\ 7 + 2^0 & & 9 \\ 9 - 2^{-4} & & 7 \\ 7 - 2^0 & & 5 \\ & & -2 \end{array}$$

8 prices indices DP' DP''

positive with expansion -- decrease with frequency acceleration

negative with contraction -- opposed ? by frequency deceleration

9 DQ' DQ''
follow DR' DR''
apart from DP' DP''

A333

FC. notes "5th page from the end of A Method..." I made a careless mark on margin of no significance at all"

in pencil first page, top right hand corner.

	Totals
1. pp 11	11
2. pp. 10	21
3. pp. 9	30

Outlay DO'

$$DO' = \sum_i [(d_{i0} + j-1 + d_{ij})r_{i0} + \sum_{u=1}^{u=w} (j-n + d_{ij}) dr_{in}]$$

where d_{i0} d_{ij} are constants for each "i"

d_{i0} the fraction of the zero turnover leftover from last turnover

d_{ij} the fraction of last turnover, found in this one

$j + 1$ is number of turnovers collecting[?] both fractional turnovers.

dr_{in} is the difference in outlay between the nth and the (n-1) th counting the first complete turnover as the first

Negative accelerations

$DM' = -K$

General squeeze - falling prices

if at once & universal, solution
de facto, falling prices & reducing production
which augments - DM' - makes
it systematic - & does not provide
solution

Return from positive acceleration to zero acceleration on[?] acquired
higher level

I Acceleration - proportionate lag
- unless - DD' , then + DP'

End of acceleration - lag ends unless + DP' , then - DP'

can't take it because unorganized for
general price drop

and cause can't be avoided, because unorganized
for - DD'

II No - DS' - if expansion on increasing return of loans
then remaining at peak of expansion
means remaining at peak of volume of loans
to pay the loans off & not renew them - reduce volume-
gives - DS' , gives reduced turnover size.

Abortive Accelerations

1° Profit & Loss corrected 1 index of expansion or contraction

1° Varying inventories

 \
 uncorrected

2 acceleration starts & finishes
without going round[?]

2° Windfall profits & losses

X makes outlay & Y gets it in addition to his outlay

Y' gets it & makes a - DD"

X' spends + DD' - Y uses it to decrease c.cap on
short turn loans

Successful acceleration & success of process

~~Wrong to put DE' = DO'~~

~~DO' at beginning of expansion - a saving needed to meet? t' DR[?]~~

successful process says a good deal more

| DP' DD' at beginning & end

| DS' & no repayment of principal

Surplus Circuit

1) Repeat all said about basic

2) Case of DD'' different

- Investment
 - 1) Redistributive
 - 2) Services of financial houses
 - 3) New capital equipment DD''
 - 4) New monetary circulating capital, $DS' DS''$

3) Difference α Once expansion in process

same then $DI'' = DE''$

purchase of more capital equipment at $DD'' = 0$

β different DD'' can be positive over long periods

~~less danger of raising price levels~~

& this positive gives cross-over disequilibrium

a new complication of basic circuit

expansion. The more remote units of production would anticipate increased demand for thier products in the increased demand for final products.
[on bottom of previous page - upside down]

$$DO' - DR' = DS - D^2R - D^2T = DA - DD - DG$$

$$DO' - DS = DR - D^2R - D^2T$$

from Loneragan's Early Notes on Economics, p.131.

activity ^is apt to raise price levels and so multiply the need for more money throughout industry and commerce^ ~~does more to raise prices than anything else~~

Mutatis mutandis, the same arguments that hold at the beginning of an acceration hold throughout it [sic] duration. For any rate of acceleration of goods and services, DQ' ; ~~there is a lag bet [ween]~~ goods in production are in advance of goods in the final market, and ~~income~~ increasing income is in advance of the possible ^basic ^ expentiture at inital prices. This lag is a function of DQ' , increasing with its increase, & decreasing with its decrease; and corresponding to the size of this lag there is some single advance in prices, DP' , that clears the basic market with DD' at zero. When the lag changes DP' another change in prices is necessary if DD' is still zero. ~~But to~~ Hence when the acceleration DQ' eventually becomes zero, a positive DD' is for the first time desiraeable, namely, to prevent the negative DP' implied in the disappearing lag.

Notes on Economic Topics - 2

Bernard Lonergan

Archive File A335

Transcription by Michael Shute

Erik Lindahl Studies in the Theory of Money Capital

London 1939

George Allen & Unwin

p. 21 "The final aim of Economic Science is either to explain the economic phenomena of the past or to forecast the economic events that will, under given conditions, probably occur in the future. In the first case we are concerned with problems of Economic History, in the second with problems of our actual life, especially those referring to the domain of Economic Policy,"

Hence study of structures

Majors to connect data: all past,
part past, part future

Also method of procession from psycho, moral
social assumptions - prior conditions of
economic activity - imperatives

Economic Science - a machine of which man is apart
- a machine from which man is distinct which man can control.

Disequilibrium exists because

1. Innovation resisted

2. Once effected

- initiated in widening circles
induced in other fields

hence

big

- even though elements small
tends to a transformation

clustered

- resistance then initiative
in a rush

irregular

- some industries ahead
others lag
results that would not arise if
smooth and coordinated

Schumpeter's Assumptions

Innovation involves

New Plant [not negligible time & expense]
New Firms
New Men in Leadership

Hence

Resistance
clustered advance (initiative & induced change)
In some sections and not others
[with different affects from smooth evolution]

upgrade : radical innovation

downgrade : induced, completing innovat.

Innovation

p100

Cluster affect

benevolent neutrality to routine
resistance to innovation

- 1) disapproval - machine -made products
prevention - prohibition of machinery
aggressive - smashing of machinery
- 2) loans easy for routine, hard for innovation
labour of right type ready & available for routine
consumers buy what they understand
- 3) inhibitions to new (partly irrational)
e.g. aeroplane production if only
paid on assumption that everyone now using motor-cars would as readily
use aeroplane

Once set-up easy to copy and to improve
forced to do so by competition

hence innovations cluster

not spread evenly over time but in lumps
not spread at random over space but in areas

Transformation effect ⇒ Induced innovation

Railroad through new country upsets all conditions
of location, all cost calculations, all production functions
Hardly any "way of doing things" is optimal before [?]¹ & after.

Electrification ditto

¹Schumpeter, *Business Cycles*, volume 1, p. 101 has "hardly any ways of doing things" which have been optimal before remain so afterward"

Schumpeter BC II 768

quotes with approval Prof M W Watkins

Journal of Pol Econ Feb '31

pp. 67,8²

automobile industry	did not develop	aviation
bicycle carriage industry	did not develop	automobile
telegraph	" "	telephone
theatre industry	" "	motion pictures

'The explanation seems to be that the managers & directors of older industries once they have proceeded in establishing as an economic "going concern" the special branch of industry with which they are primarily identified, lose their adventurous inclinations. They tend to become sceptical of new processes & new products. They become absorbed in the complicated routine of their own affairs and the ever recurring problems of adjustment and adaptations of which no field of business enterprise is ever free. In these circumstances

²Professor M.W. Watkins, "The Aviation Industry" *Journal of Political Economy*, February, 1931.

it is only the far-sighted, uneasy, venturesome individuals here & there who are ready to "cut loose from" a secure position and in [sic] assured income, and who have the gift of imparting their enthusiasm to other restless individuals (technicians, salesmen, labourers) ad to still others with private capital, who are willing to take great risks for the chance of great gains - it is only in a word adventurers who found new industries. The aviation industry has been no exception." ³

³Schumpeter, *Business Cycles*, volume 2, p. 768

Equilibrium & Disequilibrium Analysis

Any product sells as a function of the outlay on all ~~other~~ products

$$DE_n = C_n \sum_{j=1}^{j=n} G_{jn} DO_j$$

Equilibrium of fact given by equation

Equilibrium of marginal utility

$$\Sigma D_n = \sum_{j=1}^{j=n} S_{jn}$$

ΣD_n = summation of marginal utilities of demand

ΣS_{jn} = summation of marginal utilities of supply

$$DE_n = P_n C_n \sum G_{nj} DQ_{nj}$$

where there are N equations of which this is the "n" th
where j has successively all integral values from 1 to N

1. Equation expresses fact

2. Equation expresses tendency to balancing
of marginal utility of product $DE = F(u)$
with marginal disutility of effort & abstinence
 $DQ_{uj} = F_n(e)$

Innovation

redistributes unties (?) channels

transforms methods commodities

begins in some sector spreads,
every emergence implying & facilitating
further emergence

offering opportunities for further improvement

until this line of attack has exhausted its possibilities

Innovation ↗ direct line: new products
 ↘ induced lines : farm machinery

Invention → Knowledge

Innovation → application in economic system

$$DQ_{ijk} = F(a, b, c, d, \dots)$$

Variations in a b c d
give variations in DQ

Innovation -- setting up a new production

function -

either a new method change in f_d
or new commodity, change in L or k

fact that innovation not possible before certain
quantity of DQ_{ijk} reached, does not
disprove innovating character of innovation

Innovation = a new cost curve
a shift of curve

Innovation

Schumpeter, p. 93

involves New Plant

non-negligible time and outlay

Not necessary - important to analysis

But new Plant not necessarily innovation
may be non-growth

financial consequences follow
evolutionary consequences do not follow

New Firms and New Men

- ↓ true in competitive capitalism
- ↓ less & less true in trustified capitalism

↓
New emerge - compete - old, react, adapt
survive (if double capital outlay can be met B.L.)

p97,98

- | Continuous & growth adaptation to innovation
- | Intermittent adaption (by bankruptcy)
resulting in disequilibrium

Assumption of ideally rational behaviour
by business works as long as routine
as long as "growth" - tried experience
& familiar motive "It breaks down as soon
as we leave those
precincts and
allow the business community under
study to be faced by - not simply
new situations, which also occur as soon
as external factors intrude but by - new
new possibilities of business action which
are as yet untried and about which the
most complete command of routine teaches
nothing

Hence departure from Walrasian-Marshallian
scheme - O.K. for static or monthly (?) expanding

Socialism - economically

The limiting case of growth
in size & extent of
production functions

The transference of saving from
the individual (family position)
to the state

The transference (& elimination)
of innovation from the
individual to the state
the breakdown in moral
self-control

Either minimum taxes, free capitalist machine
violent cycles from above connected by elimination

Or social welfare program, higher taxes,
breakdown of capitalist motivation, socialism

Or middle way - group economics

Kondratieff downturn

"exploitation to the utmost, partly under duress, of existing possibilities of technological and organizational innovations on lines & principles established before but steadily improved in the process; revision of the whole structure of industry in quest of increased efficiency; systematic struggle with each item in the list of costs."

Schump BC, p759

Socialism can achieve this imperfectly if it has a model before its eyes

Schumpeter p.660

"Crises would have occurred if no central or member bank had ever called a single loan, and must be understood in the light of the fact that in any economic or social system which is unable to prevent irresponsibility and misconduct correction by consequences is the only method to prevent indefinite aberration"

Case for morality of economics

Analogy with medicine

| cannot take organism apart to examine
| symptoms for diagnosis

economics - statistics = symptoms for diagnosis
theory = principle of | diagnosis
| prescription

Difference between large scale and small scale enterprise

↑

in recession profits are consumers basic income

↑

in prosperity they add surplus income

But a large scale undertaking is not
satisfied by basic income

Hence in recession large scale

undertaking is not motivated

DQ_{ijk}

- i level of acceleration
- j type of goods or service supplied at final market
- k production function

Sch Innovation Growth of Toynbee Genesis Growth

- ↓
- ↓ → new production functions - new K's
- expansion of production functions - bigger DQ's⁴

Cyclic Phenomena

- a) cycle of learning, trial & error
- b) cycle of execution, phenomena

capitalist phenomena

- | Kitchen's Juglars Kondratieffs
- | Primary wave - Prosperity Recession
- | Secondary wave - Unsound ventures,
depression, revival

Imperatives : function of bankers -responsibility to systems, to society
| note cheap but irresponsible financing is
| what matters

function of entrepreneurs
duties of labour, operation of fields

⁴arrow connecting "expansion of production functions - bigger DQ's"
/ Growth above

"There is nothing in theory or fact to justify belief in any tendency in the recurrent waves of profit (in our sense) either to increase or decrease systematically. It follows that interest fundamentally deriving from profit should also not display such a tendency" Sch BC. p 628

True "profit" = profit from innovation

interest proportionate to marginal
anticipated profit

| profit at origin of cycle
| interest rates in cycle
| recessive waves may well be equal

511 "Normal"

the unemployment that would at any time exist
if the system already reached the neighbourhood
of equilibrium toward which it is tending
includes "seasonal," "accidental" (= fire in factory),
unemployability, change of residence, of job
imperfection of competition or of equilibrium

513 "Vicarious"

due to wage rates above equilibrium value

514 "Disturbance"

liquidation of firms, change of frontiers

514 "Technological"

due to any innovation
Not only displacement of workmen by machinery
but any change of production functions

515 "Secondary" resulting from other unemployment

"Cyclical" = technological

Technological employment results from

cycle of innovations

results in reabsorption at higher real wage level

¶ Hence

"long-run interest of the working class is in the effects of innovations on the [total] real wage bill and not in the incidental variation of employment[,] which is but an element of the mechanism that produces the changes of the former and can be separately handled by public policy

Interest

p602 Schumpeter, B. Cycles

= premium on present over future
means of payment

= + coefficient of tension in the system
_____↑

Stationary equilibrium - only
persons driving present rather
than future means of payment
are entrepreneurs - hence
rate of interest proportionate
to marginal profit [marginal
increment of prospective profit
any?⁶
for all ^ entrepreneurs]

⁶BLs insertion.

Interest ^a $DE'' = DE_m + DE''_n$
m = maintenance
n = net

DE''_n

$\overline{DE'} + DE''$

Interest 1^o the reward of abstinence DE''_n does not go to primary consumption
(helped by magnitude of incomes)

2^o the price of present over future purchasing power
in developing economy entrepreneurs at zero interest tend to infinity

3^o the brake on expansion

in non-exchange economy - forced saving

effect of interest - time becomes a cost

^aSee J. A. Schumpeter, *Business Cycles*, volume 2, pp. 605-638.

"Only as twilight settles, does Minerva's owl take wing." This, then, is the propitious hour. Before the candle of thought is snuffed out in the Brave New World" of tomorrow, let us pause to enjoy a luxury that soon will end. When the modern world was emerging from the medieval guilds & manors. It first found shape in a galaxy of city states that extended from Florence & Genoa & Venice across the Alps, along the Rhine and about the harbours of the northern coast. The contrasts of this little world in miniature stimulated economic treatises particularly on the coming of foreign trade and, when the city states were overshadowed by the later, more bulky national states, the [?] ideas took on the form of mercantilism, a collection of recipes to guide an absolute monarch in the important task of keeping his own treasury ever filled, his country ever ready to replenish it, and his rival monarchs in a less comfortable situation. But the popularity of the monarchs varied ? & economies took on a non objective interest and a non scientific air. The physiocrats tried to formulate the nature of things; more happily Adam Smith found in unshackled self-interest a comrade-in-arms for the nascent industrial revolution; and a few decades later, James Mill, the father of a more illustrious son, boasted that soon political economy would be as accurate and as definitive as Newtonian Physics. Einstein suggested that Newton had not had the last word, and then the first great war of our century opened the way for the revolutionary violence & mass propaganda that compensated for the hitherto intellectual deficiencies of socialism. "In the beginning was the Devil" and in Faustian style the deeds of Lenin & Mussolini, of Stalin & Hitler, have made socialism a matter of serious consideration. They now are wrecking Europe, but perhaps as Europe's sun is setting into a night of physical exhaustion and mental eclipse, we may be able to discuss the essential lineaments of a problem that mercantilists & pysiocrats, classical economists & socialists, have approached but not reached, have sought but could not find till history provided the experimental incidence & so released Minerva's owl to flight over the ruins."

Like a syllogism our argument falls in to three parts. In a process of reasoning such as A is B because C is D, one has to distinguish the conclusion, that A is B, the supposed fact that C is D, and the implication that if C is D, then A is B. The first section of this work presents a set of implications, of major premises. They are not exclusively economic in character, but hold generally of sets of inter-connected & accelerating rhythms or rates of flow. Accordingly, for both clarity & simplicity, they are worked out without reference to economic phenomena: somewhat after the fashion of the textbook in mechanics which deals with particles, which do not exist, and perfectly symmetrical or perfectly rigid bodies, which cannot be found in nature, so we set up a working model, a set of spheres that emit hypothetical patterns to one another in a fairly preposterous fashion.

Sincere men, welfare of state & of farmer at heart
natural reaction to mercantilism which was projection
of medieval paternalism into rational state of modern
times

Led to a great development of accuracy of economic
definitions: capital, land-rent, costs of production,
division of product, income etc.

It eliminated the Realpolitik of mercantilism which
saw one state's progress to involve ruin of others.
But it fell to opposite extreme, exaggerating farmers
as mercantilists exaggerated trade - [its idea of
natural law was full of Hobbes Locke Rousseau
Montesquieu Helvetius p. 96 note 3]

99 in some individuals it led to advising the
drawing up of a blue-print for all countries
to be enforced immediately & in detail
Failure to grasp that economics is a function
of physical geography, national characteristics
customs, etc.

1. Many interesting remarks in Plato Aristotle Xenophon[ck] Cicero etc. on economic events & conditions.

Medieval writers engaged in evaluating moral aspects of economic activity

But economic doctrine properly began only in modern period with the question:

What makes a people rich? Mercantilism Physiocracy, Smith.

2 Was mercantilism a system?

It developed as a practical system of trade policy (Handelspolitik#); & even as a theory, it is not the work of any single writer or even school; it represents the dominant views of a few centuries of economic practice & reflection

3. Adam Smith's idea of mercantilism

Smith supposed mercantilism to consist in the belief that wealth is gold & that if a country does not possess gold mines, then it can become rich only by a favourable balance of trade [balance of trade: notion? appears first in Bacon of Vera 1615]

But a favourable balance is had by increasing exports & decreasing imports & so this becomes the policy of every state.

4 Mercantilist Practice

α Tariffs & embargos to prevent import of foreign manufacture, export of domestic raw materials [import forbidden α to force foreigner to buy manufacture β to make raw materials cheap at home]

β Bounties and kickbacks for export of manufacture, import of raw materials

γ Embargo on export of gold or silver

δ Loans & other devices to encourage development of new branches of industry

ϵ Trade treaties with foreign states

ζ Privileged companies for difficult fields of foreign trade

η Search for colonies in foreign lands [colonies treated as mere means to (?) of home-land]

5. Did mercantilists really think gold wealth? Did Smith really believe they did?

Smith speaks of popular notions & implicit assumptions - the mercantilists may not have failed to distinguish between money & wealth & yet failed to make that distinction effective in their thought

A. Oncken⁷ Geschichte der Nationalökonomik I (1902) 225 states that he sought & failed to find in the whole of merchantalist literature the explicit statement "Wealth is Money" - only a single instance in an unimportant work

Pesch: even if mercantilists did not openly confuse gold & wealth, even if Smith was unshaken in considering it the implicit assumption of all their thought, there can be no doubt that they exaggerated the importance of gold.

Friedrich Kleinwächter (1906) De facto theory & practice in Mercantilism period was directed to increasing & protecting domestic gold supply - this direction was not an illusion - the period after the discovery of America was the birth of capitalism & capitalism had to have gold - Mercantilism is the scientific system of budding capitalism.

⁷This is Auguste Oncken, See Joseph A. Schumpeter, *History of Economic Analysis* [hereafter HEA] (New York: Oxford University Press, 1954), pp. 225, 228, 244..

Schmoller, Gustav: in *Jahrbuch für Gesetzgebung Verwaltung und Volkswirtschaft*, VIII (1884) 15ff, reprint in *"Umriss und Untersuchungen"* (1898) 1ff.

Schmoller advanced that Smith failed entirely to understand mercantilist movement; that he had no grasp of the forces of political history between 1450-1700 in which grew up the modern centralized states; that his discussion of competition, compensation, interdependence is on the small scale of a neighbourhood

Schmoller considered that the essence of mercantilism was not a matter incoming gold stocks, of the F.B.T., in tariffs, bounties, Navigation Acts - that essentially mercantilism was the instrument of a social revolution, the replacement of local agricultural economy by national & state economy - the F.B.T. was merely an item in the movement.

Schmoller is thinking principally of German & especially of Prussian development {note in margin Pesch G. Lonergan} The towns of late medieval times counted a greater or less important body of merchants & craftsmen. To these burghers, the limitations of the feudal organization were so many hinderances to progress. It was to their interest to enlarge the field of exchange, to breakdown barriers not only within their own country but also between countries. The compass led the sailor to the open sea and the world market was the goal of the merchant. The discovery of America & of the East enlarged indefinitely the scale of this tendency. Now the commercial revolution created an ever increasing need for more money. Merchants & producers could carry on & extend their enterprise only if they had money - Again money was the object of their striving.

Connected with the commercial revolution and its implicit Geldwirtschaft was the political tendency: from the feudal & corporative organization of society to that of the absolute prince ruling over individuals - the interests of the prince & the bourgeoisie coincided - the prince wanted power & wealth, and the means were the break-up of the old social structure & the enrichment that resulted from trade - but these precisely were the aims of the bourgeoisie - and the prince to ensure his own position could play off the nobility & the bourgeoisie against one another - Now in this change the power of gold again appears: it is no longer a matter of feudal pledged service but the living of mercenaries, no longer a matter of payment in kind, from feudal subordinates but payment in cash - The discovery of powder & shot finished off the knights - hence the pressure on the royal borrowing: money was needed to run the emerging state; it could not subsist on rents of royal domains and occasional donations or taxes; it had to have money & to have it abundantly, it had to favour manufacture, trade & the F.B.T. [∴ manufacture & trade the expansion of the moment F.B.T. increase in gold supply necessary for commercial & political expansion.

Mercantilism. Theories of its Nature Pecsh II 19-22

August Oncken Geschichte der Nationalökonomie I (1902)

Mercantilism was system of policies for the well-being of princes

"System der landesfürstlichen Wohlstandspolizei" "Système réglementaire"

Fundamentally the mercantilist care of manufacture & trade was a political opportunity. the favourable balance of trade was the single dogma that mercantilism put forward. it was but part of a larger doctrine: "the end of the state is the wealth & power of the prince : from this follows the subordination of the welfare of the people, the system of state regimentation of economics, the rivalry & enmity with foreign nations."

Hence another consequence, the economic progress & effort of the people was not directed to their well-being but to the territorial & political aggrandizement of the national state - & in harmony with the absolutism of the times this was conceived as the increasing power of the sovereign. Again the capitalist profit motive not merely was the economic instrument of the state; it coloured political thinking - to Voltaire one state's loss is another's gain - Hence ruthless national egoism - (later this view gave way to the equally inadequate view that trade was equally to the advantage of all (Free trade)) Trade or manufacturing developments in one state were considered to be simultaneously the weakening of others. (Rightly but conditionally in monetary order)

Wars of the period were thoroughly at the service of trade, the extension & consolidation of trade & colonial domination ?- they were but an element in the chain of regulations for the achievement of wealth & power at the expense of others.

Hence according to differences of territory, situation, economic & political development & circumstances generally; the practical measures of mercantilist policy varied in different countries & towns.

Wilhelm Frhr. von Schröder

"Fürstliche Schatz -und Rentkammer" 1686

"The prince is to prefer the maintenance of his own person to the well-being of his subjects"

He considers it absurd to recommend thrift to the prince

The indispensable basis of absolutism is a powerful standing army and a large ton of gold in the treasury.

In order that taxes may bring in a lot of gold, attention must be paid to the well being of the people.

As a householder must fertilize and plough his land, so the prince must attend to the well-being of the people- to raise taxes to a point that undermines the people's welfare is like letting a hog into the kitchen garden

Johann Joachim Becher

"Politischer Diskurs von den eigentlichen Ursachen des Auf- und Abnehmens der Städte, Länder und Republiken;
in specie, wie ein Land Volkreich und Nahrhaft zu machen und in eine rechte Societatem civilem zu bringen"

ed 1 1668 ed 2 1673 (dedicated to Kaiser Leopold II)

1. Totally in favour of state control of trade
2. Insists that the ruler is for the community, not the community for ~~the authority~~ the ruler
- 3 Demands diligence & hard work from prince: "he is well paid"
- 4 Nothing does more harm and brings a people and country more quickly to ruin than a large and idle court"
- 5 Republics and "Reichs-Stätt" are better off than monarchies because in the former there is no conflict between the interests of the country and the interests of the court
- 6 If a monarchy, put the interests of the country first
- 7 In a later work, composed or influenced by him

F.W. v. Hörnigk

"Wohlmeynenden Fürschlag" 1684

Kameralökonomie is a subdivision of Partikularökonomie
which is a ~~part~~ subordinate part of "allgemeinen Landesökonomie"

Mercantilists Theory Factors in Economics Pesch II 44-45

Leibnitz : "regionis potentia consistit in terra, rebus, hominibus"
esp. land, capital, labour

mercantilist commonplace - a large population is a main factor in the power of the state
but not merely a large also a well-to-do population

Vauban & French King

Christian Wolff

Vernunftige Gedanken von gesellschaftlichen Leben der Menschen 1721
Oeconomica methodo scientifica pertractata 1754

The two main factors of a state's power are numerous subjects & rich subjects

Becher ["Politischer Diskurs"]

A large population postulates the means of subsistence - Abundant food increases the population at home and attracts immigrants from abroad - The increase in the population makes it all the easier to obtain food, for it is easier to keep going in a city than on a deserted island - Hence material causality

William Petty 1623-1687

Founder of "Political Arithmetic"
hand & labour are the basic factors of wealth: labour is the father, the active principle; lands are the mother

Similarly Cantillon in 18th Effertz in the 19th century
land & labour are the irreducible principles of wealth

Mercantilists Theory Factors in Economics Pesch II 45,46

Among mercantilist theorists, greater or less esteem was accorded by different writers to special types of labour, in particular some thought more rather than less of the merchant

J.J. Becher The merchant stands next to nature - trade brings the poorest countries to life, to health, to great prosperity

he considers peasants (all producers of raw materials) & craftsmen, as productive & not merely the merchant - he thinks consumption is the key that binds the three factors together. - but the merchant stands above all as a factor in increasing the food & wealth of a community

he points to Mercury's four wings: Intelligence, Determination, Money, and Freedom - the merchant must have all four.

he asks every help for merchants - e.g. a canal system linking Germany's main rivers

he insists that merchants can do harm as well as good - & demands that they do not chose their freedom to the determinant of population, the food supply, or the Gemeinschaft

v. Hörnigk nine rules of Landesökonomie

- 1 Exact inquiry & full use of all resources of a country - notably of mines
- 2 All processing & manufacturing of raw materials in country itself
- 3 Greatest possible increase & useful employment of inhabitants
- 4 No exportation of or tampering with the currency
- 6 Necessary imports, bought at first hand, spend for in kind
- 5 Greatest possible restriction to home products
- 7 Necessary imports, in so far as possible, brought as raw materials
- 8 Greatest possible exportation of manufactured goods, sold for gold & not by barter
- 9 No imports of what the country itself can provide
the use of bounties (tariffs)

Mercantilists Theory Factors in Economics Pesch II 46,47

W. Schröder If a country wants gold, then push foreign trade - Domestic trade is commutation

favours prosperous peasantry → abundance of food → lowered costs of production

Manufacturing countries with a poor soil are a way ahead of non-manufacturing countries with rich soil.

The state must discover what manufacturers are lacking within its borders & fill up the gaps - Machine-industry finds no favour with him since it robs people of their living - On the other hand, he is enthusiastic about banks which make a great deal of trade with very little gold

Leibnitz to produce raw materials for export and then buy back the (1715) finished product, is comparable to buying back your horse from the thief that stole it

denies any opposition between interest of farmer, manufacturer and merchant: farming like roots of a tree, manufacture & commerce the branches which draw in gold from foreign countries and enrich the home-land; the farmer gets a good price when manufacture & trade flourish; trade & manufacture flourish when food-supply & raw materials are abundant and excellent

Christian Wolff Trade flourishes but when it is not restricted

Like Joshua Gee he gives a list of motives in which it is profitable to export raw materials and import manufactured goods
Wolff deserves mention because in an age that looked mostly to the prince's treasure and the prosperity of the middle class, he drew attention to the fact that wages have to provide a healthy and contented labouring class

Mercantilists Theory Finance

Pesch II 47,48

J.C. v. Justi | Ausführliche Abhandlung von den Steuern und Abgaben 1762
| System des Finanzwesens 1766

Joseph v. Sonnenfels Grundsätze der Polizei, Handlung und Finanz 1765
Both grasp the volkswirtschaftliche Bedingtheit der Finanzwirtschaft
Both oppose the Plusmacherei (gold gaining) of the old treasury economists

Mercantalist Theory French

Pesch II 48

Bodin, Jean 1520-1597

Réponse aux paradoxes de M. Malestroict 1568
Discours sur le rehaussement et la diminution des monnages 1578
De la république (six livres) 1576

~~thought that to double the gold supply meant a doubling of prices~~
Explained the price level changes of XVI century by inflow of precious metals
Favoured tariffs & bounties - freedom of trade-

Antoine de Montchrétien, Sieur de Vateville

Traité de l'économie politique 1615 [first appearance of term
"économie politique"]

[N.B. First appearance of "political economy"
James Stewart: An Inquiry into the Principles of Political Economy 1767]

Montchrétien insists on the mercantalist thesis : trade, industry, merchant marine, colonies.
finance - one man's gain is another's loss - internal trade is no gain to the nation - the foreign
merchants are pumps sucking out the life blood of the nation.

Mercantilists Theory Italians Pesch II 48,49

The Italians the great pioneers in political economy

Düring, Kritische Geschichte der Nationalökonomie * 38f
treated especially of the evils of debased currency & of trade

According to Ganilh⁹ the Italians had the worst economies
but the best treatises on the subject

Giovanni Botero [resembles Bodin]

Delle cause della grandezza delle città 1588

Della ragione di stato 1589

Gasparo Scaruffi

Discorso sopra le monete et della vera proporzione

fra l'oro et l'argento 1579

advocated a single currency for all Europe

Antonio Serra

Breve trattato....¹⁰ (1613)

Examines the general causes of the wealth of states, of Genoa, Florence, Venice - affirms
mines to be the sole immediate causes of an abundance of gold & silver.

Affirms mediate & proper causes to be the fertility of the land, provided the products are
exchanged abroad for silver & gold, and the suitability of its situation for foreign trade; affirms
general mediate causes to be the industry & ability of the people; trade especially sea-borne
trade; manufacture in which products are more durable & less subject to uncontrollable factors
than agriculture + with its natural limits; finally the type of government, the laws, order.

⁹Düring, Kritische Geschichte der Nationalökonomie und des Socialismus 1871 See HEA, p. 381.

⁹Charles Ganilh (1758-1836) See HEA, 498-99

¹⁰Breve trattato delle cause che possono far abbondare li regni d'oro e argento dove non sono
miniere (1613) HEA, 194.

Mercantilists Theory Italians

Pesch II 49,50

Antonio Genovesi

Lezioni di Commercio ossia di Economia Civile 1765¹¹

Nearest approach to systematic presentation of mercantilism

1 Wealth & fortune of a nation does not consist in abundance of gold & silver - it is only the lubricant on the axle of trade - more axles, more oil; more trade needs more gold - otherwise the double gold supply is to double prices

2 Rising price levels kill export trade & encourage imports

Gian Rinaldo Carli (mid XVIII cent)

Ragionamento sopra i bilanci economici della nazioni

Solidary, interdependence of different classes in nation; hence real politician will not be a class-man

Spaniards

Moncada

begin XVII century- critique of previous economy

Navarette ¹²

Bernardo de Ulloa

mid XVIII century - Colbertism¹³

Serovimo de Ustáriz

aim of trade policy - balance that eliminates gold payments

Mariana

Portuguese - on Money

¹¹See HEA, p. 177.

¹²Pedro Fernandez Navarrete *Discursos* (1621) See HEA, 168.

¹³On Colbertism See HEA, 147fn

Mercantilists Theory

Dutch

Pesch II, 51

Pieter Van der Hove (de la Court)

Het interest van Holland 1662

Increase in national wealth through foreign trade: internal trade is unprofitable (one man's loss another's gain)

Hence favour for manufacture that develops foreign raw stuffs & reexports

Friend of economic power: labour troubles to be solved in

favour of the master - republic favours survival of fittest & so to be

preferred to monarchy - the estate owner is more inclined to

protect the weak, which is good for the family but bad for the

state, in which the strong should become stronger & the weak sacrificed.

Pieter de Groot son of Hugo Grotius

Advanced to Louis XIV the following argument against tariffs

Every nation has more of some things & less of others; it is to the interest of all that there be exchange; tariffs mean that people have too much of one thing & not enough of another

This idea of "Weltarbeitsteilung" according to Oncken first expressed by Pieter - Pesch finds same idea in Richard of Middleton (+ 1300) Quodl II q. 23 a1

According to Pesch, Bodin drew the proper conclusion from de Groot's premise: no embargoes but not no tariffs

Mercantilists Theory English

Pesch II 52, 53

Prosperity a function of foreign trade

Thomas Mun England's treasure by foreign trade, or the balance of our trade is the rule of our treasure 1664

foreign trade not the sole but the principle means of increasing a nation's wealth

! Mun was a director of East India Company

!

→ hence all - ship building, trade, tariffs, exports, currency must be subordinate to foreign trade

Trade is conditioned by existence of sound currency - Mun, North, Locke accordingly demanded a face-value currency - point had already been made by anonymous W.S. in Compendious or brief Examination of certayn ordinary Complaints etc. 1581
Isaac Newton (in charge of treasury 1700-1727) had a currency less than nominal value for internal use, to prevent its flowing off to foreigners.

Josiah Child New Discourse of Trade 1668

Treatise concerning the East India Trade 1681

Low interest rates the causa causans of the wealth of the Netherlands

Interest rates depend upon supply & demand of capital - no use making laws.

Same idea in Dudley North Discourse on Trade 1691

Free trade as oppose to monopoly-privilege was argued for by Misselden & Malynes (both 1622) - Child praises Navigation Acts because for good of country not of group (Magna Carta Maritima) - favours however the special case of the East India Company.

Joshua Gee The Trade & Navigation of Gt Britain 1727

favours free-port-system but asks for only two such ports Gibraltar
Port Mahon

Matthew Decker An essay on the causes of the decline of the foreign trade etc" 1744

favours all English ports free for both exports & imports

Josiah Tucker Elements of Commerce 1755 - Down with foreigners - Do better work & sell cheaper

Locke (1714) you bring both sides to a balance quicker by taking from the heavier & putting in the lighter - hence favourable balance better than gold mine

History of Economics

Pietro Custodi : Scrittori classici italiani di economia politica

Parte antica (1803, 4) 7 vols. - Parte moderna (1803-16) 50 vols.

Pesch II 55- Mercantilism

A state policy in which trade, possession of gold, the favourable foreign balance & indigenous manufacture played compensating roles

Both theory & practice from the late middle ages till the eighteenth century were dominated by the mercantilist state policy
it cannot have been purely & simply an error

Roscher Geschichte der Nationalökonomik, 232f

Pesch II 55

Errors of Mercantilism

importance

1. exaggerated idea of value of gold II 56

Not in sense that gold was confused with national wealth

Need of gold a) expanding trade b) taxation machine

Dühring Kritische Geschichte der Nationalökonomie 34ff

"Der Besitz des edeln Metalle als Wirkung und als Ursache, als Erfolg und als Anregung der wirtschaftlichen Tätigkeit unter der Leitung des Handels - dies ist, soweit überhaupt ein paar Worte zur Kennzeichnung genügen können, die leitende Idee des Mercantilismus gewesen"

cited Pesch II 56

Error lay in putting importance of gold too much in the foreground - it is a means to trade, trade a means to economic well-being

Pesch II 56-59

Errors of Mercantilism

2. Exaggerated importance of foreign trade & industry

Agricultural surplus makes possible distinction of trade, manufacture and agriculture - this distinction certainly results in vast increase of productivity.

Mercantilism insists on industry & foreign trade almost to neglect of other factors - this was meeting the challenge of his time & even more developed theory would not point out a different way [Ingram, Geschichte der Volkswirtschaftslehre p. 51. Still (Pesch II 5)] a more balanced view would have promoted greater intelligence in facing the problems of the emergent worker class, greater care of agricultural interests

On the last point (agriculture) criticism valid in varying degrees - but the general exaggeration of the importance of trade cannot be denied II 58

3. The Absolutism and the close-fisted profit-seeking of mercantilist policy

Both the growth of internal trade and the problems of external pressure & expansion imposed a strong central government with a positive economic policy - But the error of the times was that the goal of this effort was not the national well-being but the power of the sovereign and the advantage of the treasury
Peak of absolutism in German Kleinstaaten which sold mercenaries abroad

Pesch II 62

Errors of Mercantilism

4. Exploitation of colonies & international trade rivalry

~~Love of the home country implies~~

"To wish the greatness of the home country is to wish the ruin of its neighbours" Voltaire II 62

Colonies totally subordinated to well-being of home-land.
Peace was merely an armistice between 1600-1800

"Wenn [so] die ganze Zeit von 1600 bis 1800 von jahre- und jahrzehntelangen Kriegen erfüllt ist, deren wesentlicher Zweck ein wirtschaftlicher war, ... so zeigt das den Geist der Zeit in seinen wahren Lichte: die nationale Leidenschaft der wirtschaftlichen Rivalität war allerwärts in einem Grade erwacht, Daß sie nur in diesen Kämpfen ihren vollen Ausdruck und ihre Befriedigung finden konnte."

Schmoller, Umriss und Untersuchungen, 50f
cited Pesch, II 63

Der Merkantilismus hat in der Richtung, in welcher er tätig war, zum Teil Grossartiges geleistet. Handel und Gewerbe sind durch ihn mächtig gefördert worden. Das hat [auch] Adam Smith, obwohl Gegner des Merkantilismus, anerkannt. Wird aber die Frage gestellt, ob der Merkantilismus unter allgemeinem [volks]wirtschaftlichen Gesichtspunkte Lob verdient, so dürfte heute kaum jemand diese Frage unbedingt bejahen wollen... daß Merkantilssystem nicht bloß durch seine Erfolge, sondern auch durch seine [Einseitigkeiten und Übertreibungen,] Fehler und Mängel lehrreich geworden ist.

Pesch II 63

Physiocratic System Pesch II 64-67

New Ideas & aims

64 Reaction against mercantilist state control in name of "natural liberty"

65 Medieval craftsmen protected - in same fashion & by same means (Privilege, Monopoly, Statutes, Regulations, Elimination of competition, subsidy in international competition) the modern state favoured manufacture. But what began as an aid ended as a hinderance. In time of Colbert after his successful Dutch War (1672-78) the merchant Legendre at a council of producers & traders had said "Laissez-nous-faire." After Colbert under Louvois bureaucracy spawned endless officials.

At same time agriculture found itself in least favoured position - feudal obligations to church & to the lord, military service, internal tariffs, the destruction of war, the rank behind manufacture & trade.

At death of Louis XIV state debt was 2 milliards
interest 89 millions, income 69 millions - oppressive taxation.

66 | John Law advised foundation of a bank issue & a trade company
| for the exploitation of the Mississippi - shares owned $\frac{2}{3}$ by state, + state's
| profits to maintain value of its fiduciary issue- profits not
| realized, bank insolvent 21 march 1722 - 2 milliards
| of money became worthless, universal loss
| Monopoly of company remained overall overseas
| trade- cotton, coffee, tobacco - merely to advantage of King &
| countess who owned the 56, 000 shares on which there was a
| guaranteed income of 150 livres per share no matter what the
| conditions of trade

67 Situation cried aloud: Freedom, Agriculture. Financial Reform.

Pesch II 67-

Writers of Transition Period to Physiocracy

Though Colbert had aimed not at "abondance de l'argent" but at "abondance des denrées" still these writers found it necessary to insist

1 On the rejection of the exaggerated regard for gold & money

P. de Boisguillebert (1646-1714) wealth is not gold (paper would do for money) but solely in food, clothing, & necessities

Vauban, friend of Colbert's and a mercantilist, "gold & silver are not wealth but only the abundance of goods needed for human life

Mélon gold is not merely not the sole riches; it is only the sign of the rest of riches

Montesquieu gold & silver poetic wealth, merely a sign of real wealth; the Portuguese Spaniards mistook the sign for reality & so sought only sign - their success undermined its value

Richard Cantillon The earth is the source or matter of wealth; work is the form that produces it; and wealth itself is merely food, clothing, conveniences, agréments de la vie.

2. The Role of the Land

II 68 Swing away from mercantilist view that favourable balance & its conditions (domestic manufacture, tariff barriers) the causes of wealth Colbert has done the peasantry as much harm as Sully under Henry IV had done it good: Sully considered agriculture & cattle raising "die beiden Nährbrüste des Staates" but he was not precursor of the Physiocrats believing thoroughly in state intervention.

2. Role of land, con't

Boisguillebert A state obtains well-being & power through its peasant population
medium prices for corn the optimum: too high & too low a bad sign

Mélon placed national wealth in its soils [Grund u. Boden]
affirmed peasants to be the largest proportion of population &
their income a better index of national wealth than the F.B.T.
Cantillon, Quesnay, A Smith -similar views

Véron de Forbonnais agriculture the basis of wealth, not
like physiocrat assertion of agriculture as sole source of wealth
Wealth is not large scale commerce but "in einem guten
allgemeinen Ackerbau, in den Gewerben derjenigen Einwohner,
welche jenem nicht obliegen können, und einem gesunden inneren
Handel"

Marquis d'Argenson all grand scale commerce reduces to usury-
the ideal line in the "golden mean" exemplified by Switzerland

Cantillon does not make the soil the unique factor- work & soil
combine to give wealth - despite his grand sympathy for
the agricultural interests, Cantillon was a mercantilist & not
the father of physiocracy as Jevons & Higgs tried to make out

Vincent de Gournay merchants - real source of wealth, parallel
to agriculture & not a mere offshoot.

Marquis Victor de Mirabeau (the older Mirabeau) wealth & Power lies
in large population, not city but country population,
that is diligent, high moral character
Later he conceded to Quesnay that wealth a cause & not an effect
of population

Transition to Physiocracy Pesch II 69-

3. Elimination of State Interference

Boisguillebert removal of all local & district customs - Let state be content to keep down injustice - Nature under divine providence will attend to rest

Mélon trade is the exchange of superfluous for necessary - freedom must prevail at least to extent of enabling everyone to pass on his surplus. eliminate freedom that does not militate against the common good - in doubtful cases decide in favour of freedom

Montesquieu did not demand absolute freedom - limitations on merchants is not restraint of trade - Trade with colonies must be monopoly of mother-country, an advantage owed the mother-country for the military protection she provides- neither Quesnay nor Smith favoured such monopoly of mother-country in long run not to her advantage.

René d'Argenson first to demand absolute international freedom from all tariffs - goods must exchange as freely as air & water circulation - the whole of Europe must be a single market in which the best producers & best nations come to top Better favour the foreign producer for the local has already the advantage of low transportation- Not only free trade in international sphere but generally " Pour gouverner milieux, il faudrait gouverner moins" - "Laissez faire, tel devrait être la devise de toute puissance publique, depuis que le monde est civilisé"

See Oncken Geschichte der Nationalökonomik I 274

Transition to Physiocracy Pesch II 70-

3. Elimination of Interference

René d'Argenson con't

New function of the state is solely to provide good judges, the suppression of monopolies, equal protection for all, constant currency, roads & canals
But d'Argenson did not speak as the Manchester School in the interest of great estates & big business; his favourite was the country populace

Victor Mirabeau also wanted the removal of all tolls & customs

Universal peace Mirabeau, d'Argenson connected it with economic organization as did the later Manchester School

J. C. Vincent, de Gournay until Oncken's Geschichte der Nationalökonomie
de Gournay passed as the author of the phrase laissez faire
It was used by Legendre to Colbert; it is found in d'Argenson

In de Gournay laissez faire laissez passer refers to
removal of tolls & customs - it does not imply the rejection
of the mother-country's monopoly with colonies, of privileges
& prohibitions - De Gournay is according to Oncken, simply
the representative of a liberal tendency within the mercantilist
frame-work [Gesch. Nat.ök. I, 291]

Transition to Physiocracy Pesch II 72-

4. Reform of Taxation

Maréchal Vauban outlined a primitive system of income tax - conceived as the principle but not the sole tax - It implied the destruction of the feudal system & so was taken amiss by Louis XIV

Abbé de Saint-Pierre favoured a tax based on productivity of the soil instead of the varying "taille arbitraire" - from this Quesnay developed his "impôt unique", but Saint-Pierre did not conceive a single tax.

de Gournays school wanted taxes on consumption objects, especially luxuries. production was not to be taxed.

François Quesnay 1694-1774

Pesch 73-74

Influences: α the age, the miserable conditions of France, the sanction agst Mercantilism
 β son of a peasant, & a doctor who followed the school of Hippocrates
& believed that politics as well as medicine should let
nature take her course, a doctor at the court from 1749

74 where he could contemplate at first hand the deficiencies of
the administration
worked scattered, published anonymously

Oeuvres économiques et philosophiques de F. Quesnay Aug [August] Oncken, 1888

Physiocracy: the rule of the "national order" - name goes back to Quesnay
physiokratisches System: name used in Germany sooner than
agricultural system: name spread in England by A Smith

Quesnay Pesch II 75-

Quesnay proceeded philosophically, objecting against current political theory that it took a one-sided view of historical development. Truth in its fullness cannot be known from given relations & positive law but only from antecedent nature. History sees everywhere beginning, growth, decline, decay - but this is meaningless without an a priori measure of natural order.

Quesnay distinguished a natural order and a positive order. The natural order, self-evident as natural or ideal for the whole of social living, presents the universal, unchangeable eternal principles. It is decreed from God as First Cause. The positive order consists in practical applications & proportionate executions of the eternal principles - Such applications & execution has to be adapted to the changing circumstances & times. Lasting welfare is had only when the positive order realizes properly the natural order

76 The natural order implies [Ingram, Geschichte der Volkswirtschaftslehre¹⁴, 5]

1 droit naturel à la subsistance

Society did not destroy the Hobbesian primitive "everyone's right to everything" which in the primitive state was as meaningless as the swallow's right to every fly in the air - Hence the natural right remains - Society must take [care] of its poor - yet each individual is free to seek more than subsistence by his own efforts.

Inequality is not an evil but a manifold stimulus to progress

¹⁴History of Political Economy

The natural order implies

2 the "sacred freedom" of imposing one's lot as much as one can without harming others - hence full freedom in the use of property, freedom of vocation, of trade crafts

3 the unitary not the federative state, legal not arbitrary despotism enlightened Absolutism was Quesnay's choice - He has little taste for Montesquieu's Constitutionalism, considering that like republicanism it degenerated into a class-state with one-sided representation of dominant interests - no division of powers but pouvoir absolu réglé par les lois - the monarch in this state was also le seul pontife and full-fledged theocracy the best form.

4 Economically the national political form is "royaume agricole"

Economic need is for subsistence & reproduction: gold is needed for currency [or exchange: to seek more than this need requires is absurd. Wealth is what nourishes man & reproduces itself; its sole source is the land; the land gives it, increases & multiplies it; land, forests, mines, fisheries are alone productive; alone they yield a produit net; and their source is the natural fruitfulness of the land & improvements on the land

the natural order implies
5 con't

y) Trade & industry gives the third class - la classe stérile
the name implies no reproach but simply states the fact
that [the earth is creative of wealth
[the peasants labour multiplies it
[the manufacturer & trader add to it

This class tries to take to itself the natural profit that has its
source elsewhere - an attempt in which it succeeds to the
general detriment

The wealth of the land is richesses véritables richesses réelles
but the traders' profit is richesses fictives richesses pecuniaires
richesses stériles

Foreign trade is a good thing for no country produces all kinds
of goods - but the theory of the favourable balance of trade is
une chimère des spéculateurs politiques; for the gold
one gets, one gives goods in equal value (Mercier de la
Rivière); profits of trade are the fruits of privilege; and the
merchants gain is the country's loss

81 Criterion of economic good - the lot of the farmer; "Pauvre
paysan, pauvre royaume; pauvre royaume, pauvre roi"
"hat der Bauer Geld, hat's die ganze Welt"

Hence not mercantilist subordination of farmer
to foreign trade but visa versa

not shifting
not excessive

Vital $\Rightarrow \Rightarrow \Rightarrow$ High prices for farm produce $\Rightarrow \Rightarrow$ bigger capital for farm investment $\Rightarrow \Rightarrow$
bigger produit net The A + SL of Quesnay.

Quesnay

Pesch II 81

The natural order implies 5y con't

82 Quesnay distinguishes between | prix naturel - what ought to be
| prix courant - what is

The "pris naturel" of manufactured goods etc. = sustenance of factors
The "pris naturel" of farm produce

α basic price - costs of production

β farmer's selling price - adds the "produit net" of nature

γ consumer's cost price - adds dealer's livelihood

Optimum $\beta - \alpha$ large $\gamma - \beta$ small

83 Interest rate - based on produit net of land

5 Fourth class - wage-earners

"dernières classes des citoyens" "bas peuple" "petit peuple"

No opposition between this class & farmers

H.C.L. results from goods farm prices

But wages gravitate about subsistence level, so no
difference to worker whether cost-of-living high or low

Malthusian law makes number of poor inevitable - hence state-aid

Pesch II 84

The natural order implies 6

Taxes - essentially an input unique

direct land tax on rent of large land owner

Voltaire missed point of physiocratic doctrine in his [7]

"L'Homme aux quarante écus"

indirect taxes rejected - in long run it falls in produit net

but is more expensive to collect. & yields less; also distorts

The Positive Order is the realization of the natural order

It has to take changing circs [circumstances] into consideration; it changes with them

Politically - army needed for protection even after physiocracy has put

an end to commercial wars - professional army - obligatory education -

rentiers freely fill administrative judiciary posts

Economically- an arrangement to favour agriculture - the

positive order introduced a large amount of regulation

despite the "liberté entière et absolue" of the natural order

Population - to be increased by increasing the food supply

Pesch II 85

Turgot as Physiocrat (1727-81) studied theology but never ordained

86 All Quesnay's fundamental ideas

Riches is not gold - the earth the sole source

87 More insistent on freedom & less given to limit it
in realizing the natural order by the positive order.

He has here termed the real pioneer of practical
individualism

Given to dogmatism, to putting ideas rashly into practice

But one of the great figures

88 In other countries a few important followers but
despite one or two experiments no results - No
following in England where the protection of the landed
interest by the corn laws made the agrarian
exaggeration of physiocracy manifest.

In France the "table economique" appeared to
many as a discovery equal to Newton's

Pesch II Judgment on Physiocracy - Criticism II 91-94

Is agriculture alone productive?

1) It is the source of raw materials - But man cannot live on raw materials work & its organized direction also necessary

2) It supports itself & as well it supports industry & commerce
Moreover the value of industry & commerce equates with the materials used to support producers during time of production.
Hence it alone yields a surplus.

Rejoinders B.L. one might as well say that industry & commerce support agriculture & alone yield a surplus - A surplus of raw materials results from agriculture - a surplus of finished goods results from industry & commerce
Pesch answers that yielding a surplus is not the end of economies[?]

3) But in point of fact it is not solely agriculture that yields a surplus --an economic system's capacity to yield a surplus is a function of its productivity & its thrift & its enterprise - - Productivity is supplying quantitatively & qualitatively what people wish with the minimum expenditure of labour & materials - Thrift is non-directive of productivity to consumption - Enterprise is direction of productivity to new fields that may increase productivity.

Pesch Judgment on Physiocracy Continues II 95-99

2) Individualistic Natural Law

α to set up an ideal besides the positive order is not utopian - the utopian thinker leaps out of the real world, into one of dreams - but any thinker that passes judgment, offers criticisms, rationally approves or disapproves must examine standards which are not mere matters of fact but ideal.

β There is a tendency to refuse the name "law" to whatever lacks coercive power - but there is the coercive power of conscience - without it no state can stand - Again if the only law is positive law, then no despotism nor tyranny can be unjust [right = legal, no matter how iniquitous the laws, how arbitrary, how cruel, how backward, how stupid] Again if there is any natural law, then it regards not only the individual & the state but also the family & intermediate associations [which are necessary if the state is not to become a monster that engulfs the individual]

γ the tendency to deny the natural law arises from any of a number of confusions - natural law is not the law of the old political economists - it is not the law of Rousseau's state of nature nor of his Social Contract - it does not involve a set of pundits & judges with parallel power to that of the official legal apparatus - It is the first principles on which any social positive order must be built.

δ The later physiocrats with their unqualified assertion of freedom of trade [la liberté générale et indéfinie du commerce - no state intervention - elimination of guild associations] did a great deal of harm Their theory suffers from a lack of distinction between moral & physical natural laws

The natural order implies

4. con't

Trade & manufacture do not give a produit net - increase in value of flax woven into lace may be 1000 fold - but this increase simply represents the cost of living of the needle - artist during the period of production - hence trade & manufacture are not additional sources of wealth but mere appendages to agriculture; their role is like that of domestic servants - as long as trade & manufacture remain in this role they play a notable part in national economy & are fully justified.

5. Hence the division of the population

a) la classe des propriétaires the highest class politically & socially a classe mixte; politically they are unproductive; in the field of economic administration (improvements, roads, canals, irrigation, forest preserves, & originally the clearing of the land) they are productive and entitled to rent as their share of the produit net

β) la classe productive of peasant farmers - no produit net from la petite culture which barely provides sustenance for the métayers - Q. wished la grande culture using horses to be extended - this gives a produit net - he sets down a proportion that must be attained of fixed to circulating capital [avances primitives at least five times as great as avances annuelles]