Example of essay on diamond-water paradox [2 pages]

Business, Marketing

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Essay 1

The Diamond-Water Paradox first appeared in Adam Smith's An Inquiry into the Nature and Causes of the Wealth of Nations (30) to illustrate the irony of value as seen by consumers and traders. It since became a classic analogical centerpiece among subsequent economists to explain their respective theories of value. This essay gives a snapshot of Smith's original description of the paradox, followed by David Ricardo and Eugen von Bohm-Bawerk.

Adam Smith's ' Paradox of Value

So goes the ' Diamond-Water Paradox': " Nothing is more useful than water; but will purchase scarce anything; scarce anything can be had for it. A diamond, on the contrary, has scarce any value in use; but very great quantity of other goods may frequently be had in exchange for it" (Smith 30). In the mind of Smith, an enormous irony exists between water and diamond. Water is of great value in use; but, unlike, a diamond, it has little value in exchange. He then described the Paradox Value: " The things which have the greatest value in use have frequently little or no value in exchange; and , on the contrary, those which have the greatest value in exchange have frequently little or no value in use" (Smith 30). The paradoxicality appears to come from the perspective of the consumers who wondered on the apparent irony: why would a useless material (diamond) be so valuable in exchange (or command an exchange for a greater quantity of other goods) when it is far less valuable to use than water? The natural paradigm seems to be that things of greatest value in use must be as greatly valued in exchange.

Ricardo’s Response to ‘ Paradox’

David Ricardo responded with a labor theory of value when explaining the Diamond-Water Paradox. He proposed that diamonds are expensive because it requires a lot of labor to find and mine whereas obtaining water requires much less labor to accomplish. Eventually, in the long run, prices will reflect costs per unit produced.

Bohm-Bawerk’s ‘ Paradox’

Eugen von Bohm-Bawerk explained the Diamond-Water Paradox using the story of a colonial farmer having five sacks of grain wherein the value of each sack was lowest in the fifth sack and as valuable as his life in the first sack. He proposed, like other Marginalists, that the marginal utility of a good rests upon its most important use to a person. Thus, the value of water or diamond resides not in their total usefulness but in the usefulness of each water or diamond. While the total usefulness of water is tremendous as it is needed to survive, its large supply enables it to satisfy its most urgent uses. Consequently, the marginal utility of water also drops, making each unit of water worth less to people. Conversely, diamonds are of limited supply. The supply of diamonds is so low the usefulness a unit of diamond values more than a unit of water. Those who want diamonds (perceived high utility) must be willing to pay a higher price.

My Response to ‘ Paradox’

The central tenet in the economic theory of value is that of supply and demand. My theory is that even perceptions of abundance and rarity with respectively diminish and increase the value of a unit of goods, be it water or diamond. If people can be made to perceive water as rare, despite abundance, the value of water will be increased.

Essay 2

Anwar Shaik’s The Power of Profit [3 Pages]

For Robert Hellbroner, the lifeblood of capitalism is profit, which is “ the functional equivalent of the acquisition of territory of plunder for military regimes, or an increase in the number of believers for religious ones, or the legitimization of recognized authority for states in which a change of rulership has taken place” (n. p.). He concurred with Karl Marx that the profit motive dominates and organizes the Capital Mode of Production. This provides an overview of the conception of profits in the eyes of Classicists, Neoclassicists, and Robert Heilbroner, through whose eyes Anwar Shaik made the greatest impressions on the concept of profit. .

Dynamics of Capitalist Market

In this statement in Capital, Karl Marx (218) voiced his misgivings on the perceived exploitation of capitalism on labor: “ But in its blind unrestrained passion, its werewolf hunger for surplus-labor, capital oversteps not only the moral, but even the merely physical maximum bounds of the working day.” He proposed the rate of surplus-value as proof for capital’s exploitation of the labor power and, in effect, of the capitalist’s exploitation of the laborer.

While the attribution of profit as a form of exploitation is contentious, the concept did emphasize the economic power of profit in driving the dynamics of the capitalist market.

Unlike Marx, Adam Smith (45-46) viewed profits as a necessity for the undertaker of the work (entrepreneur) “ above and over” the cost of the materials and the wages of the workmen because the undertaker risked (hazards) “ his stock in this adventure” (this enterprise). He made it clear that the product does not belong to labor, contrary to what Marx would have wanted to be considered non-exploitative. Conversely, he insisted that the profit has no proportional relationship with “ the quantity, the hardship, or the ingenuity” of labor used in the production of goods. Essentially, profit and price are market determined.

Moreover, profits are capable of driving the market through their reemployment of profit or capital in increasing the annual “ quantity of labor” to produce “ vastly greater value” (Smith 50). In effect, profit can drive expansion in the capitalist market from the sheer capital it infused into the economy increasing production capacity each time new capital or profit is added into the economic equation. Heilbroner (55) described self-interest (profit) not just a driver of the market but of man’s action. However, he contended that increasing profits will allow competitors to step in with lower prices. Subsequently, a man refusal to pay his worker with wages like other workers will also result to losing his employees. Thus, human greed in increasing profits will eventually result to social harmony (56).

Profit in Neoclassical Economics

The Neoclassical Economics proposed a model of a perpetual motion machine wherein households sell or rent land, natural resources, labor, and capital as production factors to firms in exchange for rent, wages, and profit as payment factors (Hall et al. 664). Unlike the Marxian accusations on profits as outcomes of exploitation, Neoclassicists tend to view less differently with the Classicalists in considering profits as necessary factors in price determination in selling goods in the market. Initially though this school of thought focused on wealth distribution and the " efficiency of markets" instead of generation of wealth.

Conversely, Ricardo proposed that the rate of profit and the accumulation of capital derived from the marginal cost of production. He insisted that profits are inversely related to wages (Nabers 98). He also proposed that redistribution of profits (as part of income) improves highly the economic progress.

In the Neoclassicist equilibrium, profit maximization requires equalizing the contribution of both the production and the price factors (Hall et al. 666). Moreover, Veblen viewed profit as a pecuniary interest derived from " an alert redistribution of investments from less to more gainful ventures (Nabers 86)." In effect, profits derive not just from any marginal cost of production, but more importantly in investments where this margin are much higher compared to similar investments.

My Reaction to the Marginalist Treatment of Profit

Any suspicion to the Marginalist thought on profit must be predicated with whose perspective a critique will consider these theories. From the workers' perspective, especially with a Marxian or a Helbronerian bent, profits, particularly an increase thereof, will be interpreted as a value ' exploited' from the workers. That understanding of profit, however, will erroneously miss the fact that much of profit depends upon the market, or how consumers are will to pay for the goods. And the exchange value of goods is never equal to the effort that labor placed into its production. Much of profit is perceptional in character that may be incorporated in the pricing decision. This perceptional factor arises from the marketer's understanding of the market, not from the efforts contributed by labor in generating the goods. However, if seen from the perspective of the traders, which most Marginalist tend to increasingly favor, profits, or higher profits as the case may be, resulted from the risk of stock that the trader took in order to produce the goods and ensure that they reach the market and sell the goods there, which is not far from Smith's concept of " hazards of adventure." Marginalists like Ricardo and Veblen simply enhanced on the Classicist thought by adding, such concepts as " rate of profit," profit maximization," and " redistribution" of profits or capital.

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