

Supply and demand argumentative



The Theory of Economics does not furnish a body of settled conclusions immediately applicable to policy. It is a method rather than a doctrine, an apparatus of the mind, a technique of thinking, which helps its possessor to draw correct conclusions.

It is not difficult in the sense in which mathematical and scientific techniques are difficult; but the fact that its modes of expression are much less precise than these, renders decidedly difficult the task of conveying it correctly to the minds of learners. Before Adam Smith this apparatus of thought scarcely existed. Between his time and this it has been steadily enlarged and improved. Nor is there any branch of knowledge in the formation of which Englishmen can claim a more predominant part. It is not complete yet, but important improvements in its elements are becoming rare.

The main task of the professional economist now consists, either in obtaining a wide knowledge of relevant facts and exercising skill in the application of economic principles to them, or in expounding the elements of his method in a lucid, accurate and illuminating way, so that, through his instruction, the number of those who can think for themselves may be increased. The recognition of order in any branch of natural phenomena is but the prelude to the formulation of a set of laws, the simpler as the order is more universal, which describe, and as we say, explain it. Thus the perception of the even, elliptical courses of the heavenly bodies led to the statement of the law of gravitation and the laws of motion. In economics, similar laws have long since been enunciated, and have proved themselves such valuable instruments for the understanding of the daily problems of the workaday world, that they have been woven into the texture of our ordinary speech

and thought. 1. When, at the price ruling demand exceeds supply, the price tends to rise.

Conversely when supply exceeds demand the price tends to fall. 2. A rise in price tends, sooner or later, to decrease demand and to increase supply. Conversely a fall in price tends, sooner or later, to increase demand and to decrease supply. 3. Price tends to the level at which demand is equal to supply.

These three laws are the cornerstone of economic theory. They are the framework into which all analysis of special, detailed problems must be fitted. Their scope is very wide. I have purposely refrained from introducing into my statement of them any reference to commodities; for they extend far beyond commodities.

Subject to an important qualification, they apply to capital, the price paid for the use of capital being what we call the rate of interest. They apply hardly less to “ services,” to the remuneration of labor of every kind and grade. People sometimes protest warmly against the idea of treating labor “ like a commodity.” If this indignation expresses no more than a belief that in matters concerning conditions of work, and relations between employees and the management, the sensibilities of human nature should be taken into due account, it is based on elementary decency and commonsense. But if, as sometimes appears, it is directed against the fact that the remuneration of labor is controlled by the laws of supply and demand, it is a mere baying at the moon, with singularly little provocation.

For these laws are in no way peculiar to commodities, and it is no one's fault that they include commodities too within their scope. But let us go back to the laws themselves, and probe them and dissect them, and turn them this way and that, so that we may perceive their full content, and grasp it firmly in our minds. The third law implies a prevailing tendency for demand to be equal to supply. This tendency can be verified by anyone from his experience and observation (provided he is a reasonable person and not the tiresome kind who would dispute the law of gravitation because he sees that a feather falls to the ground more slowly than a stone). But it can also be deduced as a corollary from the two preceding laws; and to regard it in this way will help us to appreciate its significance. Start, for instance, by supposing that demand is in excess of supply.

Then the price will tend to rise. After the price has risen, the supply will become larger, while the demand will fall away. The excess of demand with which we started will thus clearly be diminished. But if there remains any portion of this excess, the same reactions will continue; the price will rise further, and for the same reason; demand will be further checked and supply further stimulated. In other words, these forces must persist until the entire excess of demand over supply is eliminated.

If we start by supposing supply to exceed demand, the converse chain of sequences will operate. Now these very simple steps of reasoning illuminate the nature of the normal equilibrium of demand and supply.