

Economics Theories

demand theory

(19th century-)

First raised as a fundamental principle of microeconomics by French economist [Leon Walras](#) (1834-1910), demand theory is the analysis of the relationship between the demand for goods or services and prices or incomes.

Demand theory examines purchasing decisions of consumers and the subsequent impact on prices.

The theory was subsequently developed by English economist [Alfred Marshall](#) (1842-1924), Italian [Vilfredo Pareto](#) (1848-1923), Soviet [Eugen Slutsky](#) (1880-1948), American [Kenneth Arrow](#) (1921-) and the French-born [Gerard Debreu](#) (1921-).

Also see: [aggregate demand theory](#), [consumer demand theory](#), [Slutsky's theorem](#)

theory of consumer demand

(20th century)

Theory of consumer demand is the analysis of demand with regard to consumer behavior and rationale when changes occur in variable factors such as price, income, substitute goods.

Choice and revealed preference are two important factors affecting consumer demand.

Also see: [axiomatic theories](#)

h century-)

First examined by French engineer and economist [Jules Dupuit](#) (1804-1866) and later developed by 20th century economists, cost benefit analysis is the determination of the total value of a proposed investment's inputs and outputs.

Cost benefit analysis examines opportunity costs, [externalities](#), shadow prices and estimates of future interest rates.

The technique was first used in the assessment of projects under the US Flood Control Act, 1936, and received a firmer theoretical underpinning by English economist [John Hicks](#) (1904-1989) in a 1943 paper on consumer surpluses.

Also see: [consumer surplus](#), [compensation principle](#), [social welfare function](#)

marginal utility theory

(1870s)

Proposed in the late 19th century by the Marginalist group of economists, who used differential calculus to study the impact of small changes in economic quantities, marginal utility refers to the additional satisfaction a consumer derives from the consumption of one extra unit of a product.

Thus, an individual's demand for a product is determined not by the total utility of it but by its marginal utility. Therefore, the greater the supply of a product, the smaller its marginal utility.

The Marginalists rejected the **labor theory of value** which had previously been central to classical economics.

Source:

R D Black, A W Coats and C D W Goodwin, *The Marginal Revolution in Economics* (Durham, NC, 1973)

(19th century-)

The early classical economists believed that profits would eventually decline.

The Scottish economist **Adam Smith** (1723-1790) viewed the growth rate of capital accumulation (which took place at a rate higher than total output) as the cause.

The English economist **David Ricardo** (1772-1823) argued that a decline in the general rate of profit was caused by the diminishing marginal productivity of land.

The German political economist **Karl Marx** (1818-1883) believed that the rate of profit was influenced by the growth of competition between capitalists.

Source:

A Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations* (London, 1776);
D Ricardo, *On the Principles of Political Economy and Taxation* (London, 1817);
K Marx, *Capital*, i-ni (Harmondsworth, ,1976-81)

marginal productivity of distribution

(1899)

First formulated by American economist **John Bates Clark** (1847-1938), marginal

productivity theory of distribution shows how capital or labor will be sought until the marginal revenue from employing either is equal to its marginal cost.

Marginal productivity theory of distribution deals principally with demand for factors of production and disregards the supply side.

Also see: [Euler's theory](#), [returns to scale](#)

Source:

J B Clark, *The Distribution of Wealth: A Theory of Wages, Interest and Profits* (New York, 1899)

theories of profits

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18th century)

A doctrine proposed by the Physiocrats in France, whose principle of 'Laissez-faire, laissez-passer' (literally, allow to act, allow to pass) was later adopted by such classical economists as the Scottish [Adam Smith](#) (1723-1790).

Laissez-faire advocates nonintervention or minimum intervention by government in the economic affairs of a country.

Also see: [physiocracy](#), [mercantilism](#), [economic liberalism](#), [new classical macroeconomics](#)

Source:

J Viner, 'The Intellectual History of Laissez-faire', Journal of Law and Economics, vol. III (1960), 45-69

Keynesian economics

Named after the English economist **John Maynard Keynes** (1883-1946), Keynesian economics has influenced post-1945 economic management, particularly in its advocacy of government management of the economy.

Adherents believe that the macro-economy tends towards extended business cycles, with high levels of unemployed factors.

They assert that government management or stimulation of the economy to influence demand (through monetary or fiscal policy) can alleviate this problem of high unemployment. Monetary and fiscal policies thus stimulate the economy in times of slump by generating employment, and slow the economy down in times of inflation.

Also see: [business cycle](#), [equilibrium theory](#), [general equilibrium theory](#), [classical macroeconomic model](#)