History of Economic Thought

Ordinary Exam 17.12.2024

Outline of solution

1. The answer should contain and expand on the following points;

(a) The quantity theory of money had its early formulation in works of mercantilist authors such as Petty and Locke, who considered the connection between an increase of the amount of gold and silver in circulation on the one side and the general price level on the other. These considerations were successively refined by Hume, Cantillon and others, and the classical authors from Smith to Mill took over these formulations, and added only minor details.

(b) Among the neoclassicals contributions to the quantity theory were given by Irving Fisher, formulating the quantity theory in the way it is used today, and relating the theory of interest to markets for dated commodities, and Knut Wicksell who emphasized the role of financial intermediation in the cumulative process.

(c) Keynes introduced a reformulation by which the immediate functioning of the quantity theory is suspended due to the speculative demand for money, giving rise to the so-called liquidity preference function. Later Keynesian economists would allow for a short-term liquidity preference but retain the long-run functioning of the quantity theory.

2. The survey should start with mentioning that some notion of demand has been present in the work of several economic authors since the mercantilists. Also the notion of utility has been around, at least since Bentham, again only in general terms.

(a) The notion of demand as dependent on price and possibly income came later, namely with Dupuit and Cournot, both using demand functions explicitly in their analyses, and the connection to utility, although latent with Dupuit, was not established before the neoclassicals, although Gossen was reasonably close.

(b) The diagrams with supply and demand functions are usually ascribed to Marshall, who used in his discussion of short run market equilibria. But supply curves and the intersection of supply and demand curves had been used several decades earlier by Rau, von Mangoldt and Jenkin.

3. (a) Classical economists discussed the distribution of income into categories wages, rent and profit. For Adam Smith, the production technology with two productive factors labour and land would determine a division of the net product into payoff to the two factors, and then the wage fund theory will determine the final division between wages and profits. With Ricardo, the rent is determined by the least productive pieces of land, and adding from Malthus the assumption that wages will remain at subsistence minimum, then the net product will tend to take the form of rent to the owners of land.

(b) With the marginalists, notably J.B.Clark, the remuneration of productive factors would be established by market forces as their marginal products, no matter whether labour or capital or perhaps other factors. For this to be a satisfactory theory of income distribution, the factor remunerations must exhaust the product. Wicksteed showed that this would indeed be the case provided that there are constant returns to scale in production.