

## Handout B: Theories of Value

**Directions:** Read the excerpts below and answer the questions on **Handout C: Theories of Value Questions**. (Note: Clarifying information on each excerpt can be found in the margins.)

**Background:** *Scottish Enlightenment philosopher Adam Smith, the father of modern economics, wrote An Inquiry into the Nature and Causes of the Wealth of Nations in 1776. The book is widely regarded as the most influential work on economics in history. David Ricardo was an early nineteenth century English investor who developed one of the most important theories in economics, the theory of comparative advantage. William Stanley Jevons, an English economist in the third quarter of the nineteenth century, was one of the developers of the utility theory of value and of “marginalism”. Alfred Marshall, another English economist, wrote the most influential economics textbook of the late nineteenth and early twentieth centuries, Principles of Economics. In that book, among other things, Marshall developed the current mathematical models of supply and demand. Through these excerpts, we understand that subjective value is the most widely-held understanding of value.*

### **Excerpts from *An Inquiry Into the Nature and Causes of the Wealth of Nations* by Adam Smith (1776)**

Book I, Chapter 4: The Diamond-Water Paradox

The word VALUE, it is to be observed, has two different meanings, and sometimes expresses the utility of some particular object, and sometimes the power of purchasing other goods [that] the possession of that object conveys. The one may be called ‘value in use;’ the other, ‘value in exchange.’ The things [that] have the greatest value in use have frequently little or no value in exchange; and on the contrary, those [that] have the greatest value in exchange have frequently little or no value in use. Nothing is more useful than water: but it will purchase scarce any thing; scarce any thing can be had in exchange for it. A diamond on the contrary, has scarce any value in use; but a very great quantity of other goods may frequently be had in exchange for it.

**Smith distinguishes “value in use” (like the value we place on water) from “value in exchange” (like the value we assign to diamonds). We find value in both, but the nature of that value is different.**

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### Excerpts from *On the Principles of Political Economy and Taxation* by David Ricardo (1821)

Chapter 1, Section I: On Value (Italics are the author's own.)

*The value of a commodity, or the quantity of any other commodity for which it will exchange, depends on the relative quantity of labor that is necessary for its production, and not on the greater or less compensation that is paid for that labor.*

...If the quantity of labor realized in commodities, regulate their exchangeable value, every increase of the quantity of labor must augment the value of that commodity on which it is exercised, as every diminution must lower it.

### Excerpt from *The Theory of Political Economy* by William Stanley Jevons (1888)

Chapter 1, Introduction: On the Utility Theory of Value

Repeated reflection and inquiry have led me to the somewhat novel opinion, that value *depends entirely upon utility*. Prevailing opinions make labor rather than utility the origin of value; and there are even those who distinctly assert that labor is the cause of value. I show, on the contrary, that we have only to trace out carefully the natural laws of the variation of utility, as depending upon the quantity of commodity in our possession, in order to arrive at a satisfactory theory of exchange, of which the ordinary laws of supply and demand are a necessary consequence. This theory is in harmony with facts; and, whenever there is any apparent reason for the belief that labor is the cause of value, we obtain an explanation of the reason. Labor is found often to determine value but only in an indirect manner, by varying the degree of utility of the commodity through an increase or limitation of the supply.

### Excerpts from *Principles of Economics* by Alfred Marshall (1920)

Book 5, Chapter 3: On the Interaction of Supply and Demand

When therefore the amount produced (in a unit of time) is such that the demand price is greater than the supply price, then sellers receive more than is sufficient to make it

**The value of a manufactured good is dependent on the amount of labor that went into producing the good and not on how much the workers were paid.**

**Utility, or the happiness or satisfaction we get from a commodity, is the only source of value. The amount of utility a commodity provides changes with the amount of that commodity that we already have.**

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worth their while to bring goods to market to that amount; and there is at work an active force tending to increase the amount brought forward for sale. On the other hand, when the amount produced is such that the demand price is less than the supply price, sellers receive less than is sufficient to make it worth their while to bring goods to market on that scale; so that those who were just on the margin of doubt as to whether to go on producing are decided not to do so, and there is an active force at work tending to diminish the amount brought forward for sale. When the demand price is equal to the supply price, the amount produced has no tendency either to be increased or to be diminished; it is in equilibrium.

...When demand and supply are in equilibrium, the amount of the commodity [that] is being produced in a unit of time may be called the *equilibrium amount*, and the price at which it is being sold may be called the *equilibrium price*.

...We might as reasonably dispute whether it is the upper or the under blade of a pair of scissors that cuts a piece of paper, as whether value is governed by utility or cost of production.

In the same way, when a thing already made has to be sold, the price which people will be willing to pay for it will be governed by their desire to have it, together with the amount they can afford to spend on it.

**Excerpts from *Capital: A Critique of Political Economy, Vol. I. The Process of Capitalist Production* by Karl Marx (1867)**

Part V, Chapter XVII: Changes of the Magnitude in the Price and Labor-Power and in Surplus-Value

V.XVII.1

The value of labor-power is determined by the value of the necessaries of life habitually required by the average laborer. The quantity of these necessaries is known at any given epoch of a given society, and can therefore be treated as a constant magnitude. What changes, is the value of this quantity. There are, besides, two other factors that enter into the determination of the value of labor-power. One,

**It takes both supply (based on the cost of production, including labor) and demand (based on utility) working together to determine value. That value is reflected by prices.**

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the expenses of developing that power, which expenses vary with the mode of production; the other, its natural diversity, the difference between the labor-power of men and women, of children and adults. The employment of these different sorts of labor-power, an employment which is, in its turn, made necessary by the mode of production, makes a great difference in the cost of maintaining the family of the laborer, and in the value of the labor-power of the adult male. Both these factors, however, are excluded in the following investigation.

I assume (1) that commodities are sold at their value; (2) that the price of labor-power rises occasionally above its value, but never sinks below it.

On this assumption we have seen that the relative magnitudes of surplus-value and of price of labor-power are determined by three circumstances; (1) the length of the working day, or the extensive magnitude of labor; (2) the normal intensity of labor, its intensive magnitude, whereby a given quantity of labor is expended in a given time; (3) the productiveness of labor, whereby the same quantum of labor yields, in a given time, a greater or less quantum of product, dependent on the degree of development in the conditions of production. Very different combinations are clearly possible, according as one of the three factors is constant and two variable, or two constant and one variable, or lastly, all three simultaneously variable. And the number of these combinations is augmented by the fact that, when these factors simultaneously vary, the amount and direction of their respective variations may differ. In what follows the chief combinations alone are considered.

On these assumptions the value of labor-power, and the magnitude of surplus-value, are determined by three laws.

(1.) A working day of given length always creates the same amount of value, no matter how the productiveness of labor, and, with it, the mass of the product, and the price of each single commodity produced, may vary.

If the value created by a working day of 12 hours be, say, six shillings, then, although the mass of the articles produced varies with the productiveness of labor, the only result is that the value represented by six shillings is spread over a

**The value of a product can be measured by the average number of labor hours required to produce it.**

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greater or less number of articles.

(2.) Surplus-value and the value of labor-power vary in opposite directions. A variation in the productiveness of labor, its increase or diminution, causes a variation in the opposite direction in the value of labor-power, and in the same direction in surplus-value...

(3.) Increase or diminution in surplus-value is always consequent on, and never the cause of, the corresponding diminution or increase in the value of labor-power.

Since the working-day is constant in magnitude, and is represented by a value of constant magnitude, since, to every variation in the magnitude of surplus-value, there corresponds an inverse variation in the value of labor-power, and since the value of labor-power cannot change, except in consequence of a change in the productiveness of labor, it clearly follows, under these conditions, that every change of magnitude in surplus-value arises from an inverse change of magnitude in the value of labor-power. If, then, as we have already seen, there can be no change of absolute magnitude in the value of labor-power, and in surplus-value, unaccompanied by a change in their relative magnitudes, so now it follows that no change in their relative magnitudes is possible, without a previous change in the absolute magnitude of the value of labor-power.