SAY'S LAW: CRITICISMS, RESPONSES, AND A RESTATEMENT

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It is generally recognized that modern macroeconomic thought began in 1936 with the publishing of John Maynard Keynes' *The General Theory of Employment, Interest and Money*. The only 20th century economist that even comes close to the impact of Lord Keynes was Milton Friedman, and even he declared that "we're all Keynesians now" in that we still work from the same framework.[1] Keynes styled himself a proponent of *modern* macroeconomics because he rejected what he held as the three postulates of "classical" economics: (1) that the real wage is equal to the marginal disutility of the existing employment, (2) that there is no such thing as involuntary unemployment in the strict sense, and (3) that supply creates its own demand in the sense that the aggregate demand price is equal to the aggregate supply price for all levels of output and employment. This third postulate is known as "Say's Law of Markets," being named after the 19th century French economist Jean-Baptiste Say who most developed the idea.

Above all else, Keynes was praised for freeing economic thought from the chains of these principles. "Historians fifty years from now may record that Keynes' greatest achievement was the liberation of the Anglo-American economics from a tyrannical dogma, and they may even conclude that this was essentially a work of negation unmatched by comparable positive achievements… [Yet] the Keynesian attacks, though they may appear to be directed against a variety of specific theories, all fall to the ground if the validity of Say's Law is assumed."[2]

Abandoning this law is no simple matter either. Keynes was right in holding it up as a significant premise among all serious academic economists before him. According to John

[1] "In one sense, we are all Keynesians now; in another, no one is a Keynesian any longer. We all use the Keynesian language and apparatus; none of us any longer accepts the initial Keynesian conclusions." - Milton Friedman, "Why Economists Disagree," *Dollars and Deficits* (New York: Prentice-Hall, 1968), p. 15.

[2] Paul M. Sweezy in The New Economics, ed. by Seymour E. Harris, (New York: Alfred Knopf, 1947), p. 105.; Quoted in *Failures of the New Economics*

Kenneth Galbraith, before Keynes belief in Say's Law "was the test by which reputable economists were distinguished from crackpots."[3] This was an idea not only argued by Say, but by men like David Ricardo and John Stuart Mill, economists comparable to Adam Smith in their degree of influence. Say's Law cannot be easily dismissed as being wrong on its face, but requires a fully serious academic response.

Strangely, the typical attitude of economists today *is* to just ignore Say's Law, treat the matter as a settled issue. To hear the Nobel Laureate Paul Krugman discuss it, the principle that the classical economists was held is trivial, being of so little relevancy that he can safely neglect them in his modern refutations. "I understand that you can argue about whether that's what Say himself really meant; you can also argue about whether the 'classical' economists Keynes takes on, men who believe in this version of Say's Law [that shortfalls in demand aren't possible], really existed. But you know what? I don't much care. The fact is that the fallacy Keynes called Say's Law was and is a powerful force in economic discourse, seriously hampering our ability to respond rationally to economic troubles."[4] Say's Law is not only met with dismissal, but derision, which only the uneducated can ever really hold, when previously the reverse had been true.

We are in a strange position regarding Say's Law then. It's refutation is marked as Keynes' "greatest achievement" to break away economic thought from its grasp, but it's also

[3] "Until Keynes, Say's Law has ruled in economics for more than a century. And the rule was no casual thing; to a remarkable degree acceptance of Say's Law was the test by which reputable economists were distinguished from crackpots. Until late in the '30s no candidate for a Ph.D. at a major American university who spoke seriously about a shortage of purchasing power as a cause of recession could be passed. He saw only the surface of things, was unworthy of the company of scholars. Say's Law stands as the most distinguished example of the stability of economic ideas, including when they are wrong." – John Kenneth Galbraith, *Money: Whence it Came, Where it Went*, pages 218-219; quoted here https://iea.org.uk/blog/debts-deficits-and-slow-growth

[4] Krugman, *HearSay Economics*

something trivial that doesn't really matter, and Keynes also might have been entirely misrepresenting his opponents but that doesn't matter. This is nowhere near a proper academic or historical treatment of the principle.

How did the discussion of Say's Law become so confused? What is the true version that is being ignored? Can a better version of Say's Law be presented? To answer this, we must look at Say's Law from a historical perspective to see what Say said, then discover its true implications, and finally see how well the criticisms it faced in the 20th century stand. Hopefully a more serious treatment here can lead to a greater understanding, as well as reveal an insight to economic thought that seems to have been lost.

Historical

Finding the "proper" version of Say's Law is rather difficult as different economists will give you different answers. The principle itself has been in debate for centuries, but it was never quite formulated as a "law" after the fact by those who dismissed it. Strangely then, the beginning of our investigation is not with Say, but with Keynes and his followers. Working backwards from there, we can see how accurately the law formulations reflect what the classical economists actually argued.

Keynes gave us the most popular formulation of Say's Law as stating that "supply creates its own demand."[5] By this, Keynes meant in some loose sense that, "the whole of the costs of productions must necessarily be spent in the aggregate, directly or indirectly, on purchasing the product." If this were true, it would paint a very happy picture of the economy. Money would

[5] General Theory, Chapter 2, part vi

never be hoarded, and everything produced will find a buyer that will ultimately cover the costs of production.

A corollary of this doctrine is that any act of abstaining from consumption, i.e. saving, would release resources and workers from being tied up in the production of consumption goods so that they could refocus on the production of capital. As money would never be hoarded, the market faces no problems from deficient spending, guaranteeing full profitable employment. Saving is not only an act that benefits the individual, but the rest of society as well. There is no "paradox of saving."

Keynes offers two examples of economists arguing for this interpretation, John Stuart Mill supporting the doctrine itself and Alfred Marshall for its corollary. This will give us an easy starting point later on when we begin "looking back" to determine the accuracy of these formulation. I take Keynes' presentation of Say's Law to be the one that Krugman was concerned with, as it fits quite closely to his own formulation that "shortfalls in overall demand aren't possible, because money has to be spent on something." His preemptive dismissal of the historical accuracy of this interpretation does not give us a very promising start.

The next major 20th century statement would come from Oskar Lange's 1942 paper "Say's Law: a Restatement and Criticism."[6] According to Lange, "Say's law is the proposition that there can be no excess of total supply of commodities (general oversupply) because the total supply of all commodities is *identically* equal to the total demand for all commodities." This interpretation is similar in that it seems to indicate that everything that will be produced will be sold, making any kind of recession or involuntary unemployment impossible. Lange's

[6] *On the True Meaning of Say's Law*, Steven Kates

interpretation expands beyond Keynes as it relates to monetary theory, claiming that people will always necessarily be satisfied with the existing supply of money, essentially treating a monetary economy the same as a barter economy, merely hidden behind the "veil" of currency. People must never want to increase or decrease total cash balances because money would only ever serve the role as a medium of exchange, being never desired for itself, and if total supply equals total demand for all commodities, then money is already perfectly capable of filling this role. Thus Lange concludes that "Say's Law precludes any monetary theory. The theory of money must, therefore, start with a rejection of Say's Law."

The next major statement comes in 1952 from Gary Becker and William Baumol's paper "The Classical Economic Theory: The Outcome and the Discussion," which is when more significant departures from Keynes begins. No longer are the classical economists deniers of unemployment or recessions, but Say's Law is instead nuanced and approached from several angles. Most importantly, Say's Law was divided into three separate claims: (1) Say's Identity, (2) Say's Equality, and (3) Walras' Law.

Say's Identity states that "at any set of prices the total money demanded for *commodities* will be equal to the total money value of the quantity supplied of all *commodities*." This they ascribe as Lange's version of Say's Law,[7] essentially equivalent to "the quantity of money demanded, considered either as a stock or a flow, is independent of the price structure and is always equal to the quantity of money supplied." So once again, there is a disconnect between the price structure and aggregate supply and demand, with all money necessarily being spent.

[7] Becker and Baumol, *The Classical Monetary Theory*, p. 356-357

Say's Equality admits that demand for goods and the supply of goods may be brought out of sync, but this is rapidly fixed by the market mechanism, dropping the unrealistic assumption that the quantity of cash demanded is independent of the price structure. If the price level changes, people may seek to give up or increase their cash balance, rapidly bringing the price level to equilibrium. At that point, total demand for and supply of goods is brought back into balance, generating full employment.

Walras' Law holds that anyone who supplies a commodity receives an equivalent value of money, meaning the total value of all goods demanded (including money) is identically equal to the total value of goods supplied (including money). This is taken as a mere truism, with no significant economic implications, since it will be true for any given price configuration and says nothing about economic equilibrium.

Of these three interpretations, Say's Equality is taken as the "proper" view. Thus Becker and Baumol would reject the interpretations of Keynes and Lange, believing that Say's Law allowed the market to be brought out of equilibrium for short periods of time. However, since the market would always move to fix this problem, it was not very important to consider. While this makes the position of the classical economists less absurd, it is still hard to reconcile this position the existence of a prolonged recessions like the Great Depression. This is made more clear in a later paper by Baumol "Say's (at Least) Eight Laws, or What Say and James Mill May Really Have Meant." Here he states that Say's Law proper "[a]pparently takes the form of a type of Say's Equality, i.e., supply and demand are always equated by a rapid and powerful equilibration mechanism."[8]

[8] Baumol, *Say's (at Least) Eight Laws, or What Say and James Mill May Really Have Meant*, p. 159

While distinct, these different views all follow a similar pattern, keeping the focus and essential message of Say's Law one about how people will use or seemingly refrain from using their money. Criticisms have updated this interpretation away from some simple and naïve view presented by Keynes, but they ultimately follow the same line of thought. The main points I can glean from this "Spending Interpretation" in no particular order are:

(1) A denial of deficient aggregate demand.
(2) A denial that the introduction of money changes fundamental economic relationships, i.e. it holds money as neutral.
(3) Recessions are either impossible or at least are short lived.
(4) Savings are beneficial because it is never "hoarded," but always saved for some specific purpose or investment.

These are the views of the contemporary critics of Say's Law. What then of its defenders? The Austrian School of Economics seems to most directly integrate Say's Law into the rest of their work, so I turn primarily to their statements.

Most discussion of the Austrian School begins with Ludwig von Mises and F.A. Hayek, but surprisingly little attention is given to Say's Law in their body of work. Hayek never mentions the principle by name,[9] and Mises does not discuss it in his treatise *Human Action*. Mises did however wrote his thoughts of Keynes' critique in a 1950 paper titled "Lord Keynes and Say's Law," and would add similar points to later editions of his 1912 work *The Theory of Money and Credit* in his discussion of the "Full-Employment Doctrine." This absence is perhaps explained by the essentially "negative" role Mises believed Say's Law played. According to

[9] Horwitz, *Say's Law of Markets: An Austrian Appreciation*

Mises, Say's Law was not meant to be a fundamental postulate of economics as Keynes declared, but more simply the denial of an untenable view.

When the economy hit hard times, people would blame two things: (1) the scarcity of money, or (2) general overproduction. Merchants are worried that either their clients do not have enough money lining their pockets, or that their competitors have driven down their prices too far to stay profitable. The former was refuted by Adam Smith, and Say's Law addresses the latter.

So long as a good is not freely available to all, it is not absolutely abundant Therefore, any increase in its supply ceteris paribus would imply more ends would be satisfied. Considered absolutely, there can be no such thing as a glut of any good. At worst, it is redundant, at best it is useful. However, considered *relatively* there can be a glut if the increase in supply of one good implies the decreased supply of another good that satisfies a more highly valued end. King Midas was cursed not because he had too much gold, but because he lacked everything else. While the increase is essentially good, it may be accidentally detrimental.

Money plays an intermediary role as the general medium of exchange. The way we ultimately pay for commodities is with the commodities we produce ourselves, as this is what supplies money with its purchasing power. "Every commodity produced is therefore a price, as it were, for other commodities produced," says Mises. By the act of production itself, we supply the means through which we demand other goods and services. This is not to concede to Lange that money is *merely* a veil, but a recognition that money's role between selling a good to obtain it and spending it to obtain other goods. Supply perhaps does not create its *own* demand, but we demand *from* our supply. The power to derived from the goods we produce, and if the power it carries is insufficient it is because the good we produced was insufficient. Furthermore, because production is always only bad *relatively* speaking, Say's Law is not so much focused on spending, but on the *proportion*. It's conclusions on aggregate supply and demand are a consequence of this principle.

Benjamin Anderson has provided a very similar view. In Chapter 60 of *Economics and the Public Welfare* Anderson presents Say's Law as a refutation against those who hold that "purchasing power must be kept above production if production is to expand." This is unnecessary because "purchasing power grows out of production," meaning the essential problem lies on the other side, increasing production so that we can gain purchasing power. Humanity is only able to demand a large supply of goods and services because it has produced a large supply of goods and services. Thus "Supply and demand in the aggregate are thus not merely equal, but they are identical, since every commodity may be looked upon either as supply of its own kind or as demand for other things. But this doctrine is subject to the great qualification that the proportions must be right; that there must be equilibrium." This qualification is what distinguishes Anderson's view from Walras' Law, which did not look towards proportion at all.

Henry Hazlitt confirms his own agreement with Mises and Anderson in Chapter 3 of his "Failures of the New Economics." Hazlitt analyzes other statements around Say's Law a bit more closely though to further unpack the implications of the principle. In particular, he looks at the four essential meanings of Say's Law given by Bernice Shoul:[10]

(1) Supply creates its own demand; hence, aggregate over-production or a "general glut" is impossible.

[10] Bernice Shoul, "Karl Marx and Say's Law," The Quarterly Journal of Economics, Nov., 1957, p. 615.

(2) Since goods exchange against goods, money is but a “veil” and plays no independent role.

(3) In the case of partial overproduction, which necessarily implies a balancing underproduction somewhere else, equilibrium is restored by competition, that is, by the price mechanism and the mobility of capital.

(4) Because aggregate demand and supply are necessarily equal, and because of the equilibrating mechanism, output can be increased indefinitely and the accumulation of capital proceed without limit.

Hazlitt takes this list to be most accurate, with only (2) being false as stated, but with the potential to be made correct as well. Like Mises and Anderson, Hazlitt believes there is no inconsistency in thinking that commodities ultimately exchange against commodities, while still believing money has an independent role of its own. Proper statements of Say’s Law must recognize that the proportions between goods and money-prices must be accurate to reach equilibrium, but proportionality is something that Say’s Law has always championed to begin with, so it is a simple matter.

In more recent years, Steven Kates has been publishing several interesting papers on Say’s Law of markets, which gives a bit more color to Say’s Law, while still being in essential agreement with Hazlitt, Anderson, and Mises. For Kates, Say’s Law denies the possibility of demand failure, attributing recessions to co-ordination failure, because demand is constituted by supply. Gluts are partial, never general, so the solution to recessions is a structural one, where resources are reallocated towards profitable ventures, not by increasing the “flow” of money through the same structure. “Where the concept of Say’s Law and the theory of recession were brought together was through the recognition that demand was constituted by supply ('effective demand depends upon production'). The point was that one made purchases with the money received from the sale of one's own productions. If saleable goods were produced, then an income with which to buy goods was earned. Such a situation could continue indefinitely."[11]

Looking at this, I will once again attempt to glean the general principles of Say's Law given by this diverse collection of views, which I will collectively refer to as the "Proportionality Interpretation":

(1) Our supply of goods and services is ultimately what constitutes our demand.

(2) Gluts of one good are necessarily accompanied by a shortage of another good.

(3) For all scarce goods, unemployment is a sign of disproportionality.

(4) Saving is a redirection, not the negation, of demand.

(5) In general equilibrium, all goods will be sold at cost-covering prices.

This emphasis on proportionality is being more readily recognized among non-supporters of Say's Law as well. Thomas Sowell heavily emphasizes its import in his book *Say's Law: An Historical Analysis*. "It is clear that Say's Law… did not preclude disequilibrium, and that the 'balance' referred to was not an accounting identity persisting through all conditions of the market, but an equilibrium condition that could be reached in a 'properly' functioning economy."[12] While Sowell's view on Say's Law is somewhat mixed, it is clear that he does not think that Say's Law is something truistically true or easily disproven by the Great Depression. Sowell's worries are more focused on bringing reconciliation between the two camps, thinking

[11] http://college.holycross.edu/eej/Volume23/V23N2P191_202.pdf
[12] Say's Law, p. 22

that the supporters of Say's Law might be blinding themselves from real short term spending problems by their focus on the long run "ultimate" balancing of the economy.

Having now considered all the views, we are left with the task of determining which view more accurately reflects what was argued by the classical economists of the 18th and 19th century. There might be some difficulty in doing this because the versions of Say's Law presented in the spending interpretation are inherently bound up in the critique of the law. Obviously we shouldn't expect the classical economists to present their view in a way that makes themselves seem wrong, but we can at least see if they are talking about the same thing. By the spending interpretation, Say's Law denies the existence of general gluts because money will always be spent. What has been produced is taken as irrelevant, because under any circumstances there will be no lack of buyers. By the proportionality interpretation, the focus of Say's Law is on asserting that there is an equilibrium condition, and that spending is a consequence and not the cause of growth.

We once again begin with Keynes' interpretation and the sources he cited in its support, the first of which being John Stuart Mill's *Principles of Political Economy*.

> What constitutes the means of payment for commodities is simply commodities. Each person's means of paying for the productions of other people consist of those which he himself possesses. All sellers are inevitably, and by the meaning of the word, buyers. Could we suddenly double the productive powers of the country, we should double the supply of commodities in every market; but we should, by the same stroke, double the purchasing power. Everybody would bring a double demand as well as supply; everybody would be able to buy twice as much, because every one would have twice as much to offer in exchange.

Keynes concludes from this that the classical economists would deny that there's ever a problem of bringing new goods to the market. No matter how many goods or what kind of goods are brought to the market, they will always find a ready buyer. The difficulties of unemployment are simply ignored by Say's Law. "Thus Say's law, that the aggregate demand price of output as a whole is equal to its aggregate supply price for all volumes of output, is equivalent to the proposition that there is no obstacle to full employment."[13]

This interpretation of Mill is so bad that we might even call into question Keynes' integrity, or at least question how seriously he took Say's Law himself. If we extend Mill's quote by just a few more sentences, we are immediately introduced to concepts of proportionality and an explanation of why some things might remain unsold, and both Anderson and Hazlitt tear into Keynes for this fact. Mill continues,

> It is probable, indeed, that there would now be a superfluity of certain things. Although the community would willingly double its aggregate consumption, it may already have as much as it desires of some commodities, and it may prefer to do more than double its consumption of others, or to exercise its increased purchasing power on some new thing. If so, the supply will adapt itself accordingly, and the values of things will continue to conform to their cost of production. At any rate, it is a sheer absurdity that all things should fall in value, and that all producers should, in consequence, be insufficiently remunerated. If values remain the same, what becomes of prices is immaterial, since the remuneration of producers does not depend on how much money, but on how much of consumable articles, they obtain for their goods. Besides, money is a commodity; and if all commodities are supposed to be doubled in quantity, we must suppose money to be doubled too, and then prices would no more fall than values would. A general over-supply, or excess of all commodities above the demand, so far as demand consists in means of payment, is thus shown to be an impossibility.

In terms of historical accuracy, this is a huge blow against Keynes. The idea of proportion is immediately introduced, showing partial gluts of some goods accompanied by shortages of another. We also see that people are ultimately demanding from their supply of goods and services, since they bring "double demand" when they bring double their supply. We see that remuneration is not a problem at any level of output because sales are ultimately compensated by the amount of consumable commodities available. We even see money being included among the "doubled" commodities, showing that its need to be held in proportion as

[13] General theory, chapter 3

well was not being ignored, as suggested by Say's Identity. Keynes' refutation of Say's Law then, his greatest achievement, appears to be mostly based on ignoring this section of Mill.

It was not merely Mill who held this insight though, but all supporters of Say's Law. Ricardo is more at home with Hazlitt than Keynes when he states in his *Principles of Political Economy and Taxation* that: "Productions are always bought by productions, or by services; money is only the medium by which the exchange is affected. Too much of a particular commodity may be produced, of which there may be a glut in the market as not to repay the capital expended on it; but this cannot be the case with respect to all commodities."[14] And again, in his *Notes on Malthus*, Ricardo further emphasizes error and disproportionality as the root of economic woe. "Mistakes may be made, and commodities not suited to the demand may be produced – of these there may be a glut; they may not sell at their usual price; but then this is owing to the mistake, and not to the want of demand for productions."[15]

Between the Spending Interpretation and the Proportionality Interpretation, it seems clear that the latter fits the position of the classical economists better. Both interpretations agree that Say's Law denies the possibility of general overproduction, but for very different reasons. The the former holds that there is no problem with demand because "money must be spent on something," while the latter sees money as taking a more secondary role. There is no issue in demand for the classical economists because your supply *is* your demand. Say's Law proper is not Keynes' "supply creates its own demand," but Kates' "demand is constituted by supply."[16]

[14] David Ricardo, The Principles of Political Economy and Taxation, (Everyman ed., New York), pp. 193-194.
[15] Sraffa edition, Cambridge University Press, p. 305.
[16] Kates, *On the True Meaning of Say's Law*

Now that we have an accurate interpretation, we can move on to addressing the criticisms. Do they still valid objections, or simply misunderstandings? Some of the responses should be obvious by this point, since criticisms and interpretations have been so tightly bound together, but a formal address is still warranted.

Criticisms and Responses

Say's Law has been subject to many different criticisms, but I will try to categorize them together as best I can.

(1) Say's Law denies a problem of unemployment, as in recessions. But recessions do occur.
(2) Say's Law holds that aggregate supply and demand are equal. But if people collectively decide to increase their cash balances, thereby reducing demand and not supply.
(3) Say's Law holds money as a veil, making the economy essentially equivalent to a barter economy, making monetary theory impossible. But monetary theory is possible.

This first major criticism of the modern era is brought by Keynes, and as we have seen is easily dismissed. Say's Law will only denies the possibility of unemployment in a state of general equilibrium, when the production of all goods and services are in proper proportion with prices adjusted accordingly. So long as the economy *is* out of proportion, which in our ever changing world of uncertainties it usually is, involuntary unemployment is easily accounted for. Say's Law denies the possibility of a recession caused by demand failure, *not*

The second charge claims that Say’s Law assumes the economy is merely a barter economy in disguise. "Say's law implies a peculiar nature of the demand for money, namely, that the individuals in our system, taken together, are always satisfied with the existing amount of money and never wish to hold either more or less. There is never a desire to change the total cash balances otherwise than to adapt them to changes in the amount of money available. Under these circumstances, purchases of commodities are never financed for cash balances nor do sales of commodities serve to increase cash balances."[17]

Say’s Law implies no such thing. Money is brought into its analysis as a good acting as a medium of exchange, but with the “medium” part emphasized. Say’s Law looks to the proportion between goods, and to the extent that money is itself a good it can be brought out of proportion with the rest of the economy, leading to people wanting to change their cash balances.

Others charge that Say’s Law will only be applicable in a barter economy. The introduction of money provides a new method of trade fundamentally distinct from a barter economy, creating problems of saving, hoarding, and a whole host of other economic issues. Money is not merely a “veil” but something that can have real influence over the economy, otherwise all monetary policy would be pointless, for good or for ill. If money is not irrelevant then, we must think that it has an independent effect of its own, therefore making a disconnect between what we demand with and the “real” supply of commodities.

However, Say’s Law does not see the role of money as trivial, but sees its power as being essentially derivative. It holds that proportion between goods must be maintained, and it establishes this proportion through a free market with prices freely adjusting to guide production.

[17] Lange

It is only natural that money can have a profound effect on the economy because it is through the price system that different goods are properly proportioned to one another, and in a monetary economy that almost always means a money-price. There is no incompatibility with recognizing that money's power to demand is derived from something else while also recognizing that money behaves in a particular way.

No supporter of Say's Law ignore monetary theory or dismiss it as non-existent, but instead integrates money into its analysis of goods that must be balanced. Mill already made clear above, and we can see that view expressed again here: "It must, undoubtedly, be admitted that there cannot be an excess of all other commodities, and an excess of money at the same time."[18] Ludwig von Mises developed an extremely detailed monetary theory in his *Theory of Money and Credit* in which he very strongly argues against the neutrality of money while still maintaining Say's Law. We cannot say that it will preclude monetary theory then, but perhaps only monetary theories mistaken enough to forget its intermediary role.

It might be objected that this defense is essentially a ground shift for Say's Law, moving it towards Walras' Law as a tautological defense. There might be some truth to this, as Say's Law is making a very similar point. Walras' Law however misses the subtlety of Say's Law in its discussion of proportion, going beyond the simple identity. Additionally, it has already been clear that the supporters of Say's Law use the principle essentially as a *refutation* of a position, not the groundwork that a significant amount of theory is built upon. Tautologies are only useless until someone is foolish enough to forget them.

The Future of Say's Law

[18] JS Mill, Essays on Some Unsettled Questions of Political Economy, p. 71

It seems then that the primary contemporary charges set against Say's Law have all been misguided, fighting a demon that does not exist. Can this doctrine be saved then? Can it be properly integrated into modern macroeconomic theory once more?

Thomas Sowell seems to believe that it can be done, with a few noted limitations. For Sowell, Ricardo was mistaken in his defense of Say's Law by looking at comparative statics, focusing on the long-run conclusions of Say's Law, but ignoring the practical questions of the short run. This is the main charge presented against Say's Law by Thomas Sowell, following an argument Malthus originally presented to Ricardo. Malthus and other general glut theorists did not aim to prove that there can be a *permanent* general glut, but are instead arguing for a theory of equilibrium income, where *ex ante* costs of production are too great to make current production sustainable. Say's Law has reached an economic half-truth, properly recognizing that markets might be able to clear, but denying that all markets could necessarily clear at prices which can be maintained. "Both Say's Law and the theory of equilibrium income – its intellectual complement and historical rival – can be traced back to a common origin in the Physiocrats and are reunited in post-Keynesian macroeconomics… The questions remain: Why this long period before these ideas could be reconciled? Why did two of the biggest controversies in the history of economics rage between those who supported one-half of this basic truth and those who supported the other half?"[19] Here I believe deeper Austrian theory of factor pricing can be of great assistance.

While the claims of Mises against the existence of absolute overproduction are strong, especially when all goods such as money and leisure are considered, there is no argument against

[19] Sowell, *Say's Law: An Historical Analysis*, p. 219

the general costs of production being so great as to preclude profitable venture. We can imagine a fantastical case where the world wakes up one morning to find its supply of money reduced in half, so that everyone who had $100 previously would now find himself with $50, every $20 bill turned to a $10, and so on. Surely the price at which goods may be sold would quickly fall, presumably reducing in half themselves, and this final sales price would likely not cover the *ex ante* costs incurred in all except the most profitable of ventures.

Of course it's also ridiculous to assume that *only* the final consumer price of goods would drop in this scenario. Factor prices would reduce in half as well. Since some prices are stickier than others and would not adjust to this change as quickly, there would undoubtedly be some degree of disturbance for this process, but ultimately the problem here reduces itself to one of proportionality, as Say's Law maintains. There is some general equilibrium that would restore balance to production, with perhaps some things being over-produced and others under-produced in the meantime. It is still true that there is no absolute overproduction of goods in this circumstance, but it is still true that at the current prices production cannot be profitably maintained or increased. The solution here is not

By Austrian theory,[20] factor prices are ultimately derived from the price of the consumer goods they produce. This follows the minds process of valuation. Consumer goods are valued for the ends they directly satisfy, factors of those consumer goods are valued because they produce that good, and so on all along the production structure. Capitalists and entrepreneurs bid for factors of production for the sake of making a profit, selling the final product for a higher price, so they will not intentionally bid higher than what they believe can be remunerated, tending

[20] Ludwig von Mises, *Human Action*, ch. 16.3; Murray Rothbard, *Man Economy and State*, ch. 7

toward their discounted marginal revenue product. Thus we are guaranteed that factor prices will adjust to a level that will once again make them profitable, and seeing as how there has been no loss in real goods or resources, this should be at a comparable level of production. Granted there must be some transition period between these statics, but we can maintain that even here there has still been no true case of a "general glut," even a temporary one, as the problem is caused by a relative shortage of money against all other goods and the solution is not to cut the production of all goods down to factor prices, but to restore the proportion between money and other goods by either increasing the supply of money back to before it was "halved" or lower prices. There was never a problem of deficient demand.

Conclusion

We have seen the case for Say's Law then from all sides, both historical and theoretical, from its supporters and critics. In the end, it seems that economic thought has done a great disservice in dropping Say's Law. Without it, macroeconomic theory is sure to form many misconceptions about the essential problem of recessions and the role that spending and savings have for the overall economy. It has mixed up priorities, blamed people for not demanding what the economy has produced when the economy is meant to be the servant of the people. Properly grasping Say's Law means a return a more laissez-faire system, where prices are allowed to accurate reflect the state of affairs, and the solution to economic woe is to allow as smooth a transition to a balanced economy as we can provide. Anyone can recognize that an increase in prosperity and wealth is an undeniable boon for mankind, and if our economic theory denies this, then we must change our theory to conform to fact.

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