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Retrospectives
Say's Law

William J. Baumol

This feature addresses the history of economic words and ideas. The hope is to deepen the workaday dialogue of economists, while perhaps also casting new light on ongoing questions. If you have suggestions for future topics or authors, please write to Joseph Persky, c/o *Journal of Economic Perspectives,* Department of Economics (M/C 144), University of Illinois at Chicago, 601 South Morgan Street, Room 2103, Chicago, Illinois 60607-7121.

Introduction

What is perhaps most curious about "Say's Law" is the continuing disagreement on its substance, and to whom it should be credited. John Maynard Keynes summarized the law as "supply creates its own demand," but it is now generally agreed that Keynes, at best, did not get it quite right. I have been unable to ascertain who coined the term "Say's Law," but it appears to be a 20th century appellation, preceding Keynes's use, but perhaps not by much. Jean-Baptiste Say was certainly among the earlier writers to discuss the topic at length, but so far as I can determine, none of Say's contemporaries—including Say himself—credits him with having been first to enunciate its principles.

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Biographical Note

J.B. Say was born in Lyons in 1767, the son of a tradesman. After moving to Paris, Say worked in a bank and then was sent by his father to England to complete his commercial education—the first of a number of visits. In 1799 Say was appointed to Napoleon's *Tribunat*, which oversaw the constitutionality of legislation and other government acts. By 1803, when he published his magnum opus, *Traité d'Économie Politique*—titled in translation *A Treatise on Political Economy* [1821]—he had broken with Napoleon and was dismissed from the *Tribunat*. For eleven years he was prevented from publishing a second edition of his *Treatise*. During this period he opened and operated a cotton mill outside Paris.

In 1814, Say was sent by the French government to report on England's dynamic economy. During this visit he met James Mill and David Ricardo at the latter's Gatcomb Park. However, that and a subsequent meeting in Paris were disappointing to Ricardo because of Say's expressed reluctance to discuss technical subjects orally. In 1821 the restored Bourbon government established the first French chair in economics, which Say accepted. He continued as an academic until his death in 1832.

What Is Say's Law, and Why Is It Ambiguous?

The disagreements about the contents of Say's Law are partly attributable to Say himself. Commentators from Ricardo to Schumpeter have remarked on his unclear discussion. But there is a more important reason. Writers on the subject at his time unquestionably had in mind much more than a single proposition expressible as an epigram. Rather, they were concerned with a set of interrelated positions that they considered widespread and dangerous errors likely to lead to unfortunate policy. No unique "law" was singled out by Say or the other authors.

These writers were reacting to the intellectual currents of mercantilism. First, in contrast to the mercantilist focus on accumulation of gold, Say and other writers emphasized the primary importance of the real sector of the economy for national welfare, with money simply serving as an instrument to facilitate production and exchange. Second, they rejected claims that excessive saving (or an unfavorable trade balance) would reduce demand for home products. Third, Say, James Mill and Ricardo, following Adam Smith, opposed the view that general lack of demand was the prime threat to prosperity, arguing that the main obstacle is inability or unwillingness to produce. Fourth, they argued that saving, seeking earnings, goes quickly into investment in production. Fifth, they emphasized that investment does far more for growth than demand for wasteful expenditure of resources, such as military activity and consumption of luxuries. Sixth, they disagreed with those who feared technical change. Though Say and Ricardo both admitted that innovation can destroy jobs in the short run, Say emphasized historical evidence that it created

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jobs in the long run. With such a multitude of conclusions, it should not be surprising that Say's Law—the "Law of Markets"—is really a complex of ideas.

A number of recent writers, including Thweatt (1979), Kates (1997, 1998), and the present author (1977), have published lists of items that, they assert, together constitute the content of the Law of Markets. For simplicity, I report Thweatt's (p. 81) list, modifying only its order and numbering:

> 1) The production process (supply) generates the income necessary for the demand for these products. Money, therefore, is only an intermediary . . .
>
> 2) There is no need to worry about the possibility that some of the income generated in the production process will not be spent during exchange. . . . incomes are always completely spent on either commodities satisfying present wants (consumption), or on commodities satisfying future wants (. . . accumulation) . . . Further, since no one in his senses would accumulate "dead stock," there is no worry about hoarding.
>
> 2a) Saving, which is the surplus of income over consumption, is essential if the economy is to expand. [Hence, it is "productive consumption" in contrast with the "unproductive consumption" of luxuries.]
>
> 3) Of course, partial overproduction of specific commodities by individual producers is possible if and when "mistakes" are made . . . but this type of partial disequilibrium is quickly rectified in a competitive market economy, via the principle of competition equalizing profit rates between industries . . .
>
> 4) As a consequence, . . . an economy cannot save too much.

To this list I must add (at least) one proposition that Kates (1998, p. 216), with some justice, considers the central idea of those who contributed the Law of Markets: "In accepting the law of markets, they had not denied the occurrence of recession, or that recessions have endogenous causes, or that monetary instability can lead to recession . . . But what they had done was to deny flatly that failure of effective demand was a cause of recessions and unemployment."

These positions may, perhaps, not be consistent, but that possibility was not recognized by the early writers.

The Law of Markets and Unemployment

The main literature on the Law of Markets does, indeed, maintain that there cannot be a general failure of demand—that is, an absence of willingness and ability to purchase that is sufficient to acquire all of what is currently supplied, except perhaps in the very short run and except for individual products that had been mistakenly overproduced. But proponents of the Law of Markets also clearly believed that unemployment, notably from labor-saving technology, was nevertheless both possible and harmful.

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As Say (1821, pp. 86-87) wrote:

> Whenever a new machine, or a new and more expeditious process is substituted in the place of human labour previously in activity, part of the industrious human agents, whose service is thus ingeniously dispensed with, must needs be thrown out of employ . . . . This, however advantageous to the community at large . . . is always attended with some painful circumstances. For the distress of a capitalist, when his funds are unprofitably engaged or in a state of inactivity, is nothing to that of an industrious population deprived of the means of subsistence.

David Ricardo (1814 [1951], Vol. I, pp. 389-390) makes a similar point in his chapter "On Machinery" (which was not a discussion of business cycles) that "the discovery and use of machinery may . . . be injurious to the labouring class, as some of their number will be thrown out of employment, and population will become redundant, compared with the funds which are to employ it."

In the second edition of the Treatise (1803 [1814], p. 88 fn., my translation), Say even advocated public works as an appropriate remedy for this sort of unemployment: "[A] benevolent administration can appropriately make provision for the employment of supplanted or inactive labor in the construction of works of public utility at public expense, as in construction of canals, roads, churches, or the like . . ."

Along with the possibility of technological unemployment, Say and other economists of this time recognized the possibility of broader business stagnation and joblessness and considered these issues to be matters of great importance. Say (1820 [1821], pp. 1–2) begins his *Letters to Mr. Malthus*—four letters occupying 57 printed pages, published as a pamphlet—in the following way:

> . . . what fixes my attention, because all the interest of the moment is attached to it, is, from whence comes that general overstock of all the markets of the universe, to which goods are incessantly carried which sell at a loss?—Whence comes . . .that universal difficulty that is experienced in obtaining lucrative employ? And when the cause of this chronic malady is discovered, what are the means of cure?

However, the remainder of the discussion in the pamphlet is devoted primarily to arguing that the problem cannot be attributed to a deficiency of demand, without offering answers to these questions.

An extensive search of Say's and Ricardo's writings on this subject turned up little. For example, Say (1803 [1821], p. 135) writes:

> . . . if this be so [if there can be no overall deficiency of demand], how does it happen, that there is at times so great a glut of commodities in the market, and so much difficulty in finding a vent for them? Why cannot one of these superabundant commodities be exchanged for another? I answer that the glut

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> of a particular commodity arises from its having outrun the total demand for it in one of two ways; either because it has been produced in excessive abundance, or because the production of other commodities has fallen short.
>
> It is because the production of some commodities has declined, that other commodities are superabundant. To use a more hackneyed phrase, people have bought less, because they have made less profit.

All that Ricardo provides on the subject appears in his *Notes on Malthus,* where he tells us (1820 [1951], Vol. II, p. 415):

> In all cases a good distribution of the produce, and an adaptation of it to the wants and tastes of society are of the utmost importance to the briskness of trade and the accumulation of capital. The want of this is in my opinion the only cause of the stagnation which commerce at different times experiences. It may all be traced to miscalculation, and to the production of a commodity which is not wanted instead of one which is wanted.

That is the complete passage. Ricardo seems to offer no more on the subject. I have not been able to find any more systematic description of recessions and their mechanism in the earlier writings of Say or Ricardo.

In short, there does not seem to be any coherent and explicit model of economic depression in the writings of the proponents of the Law of Markets. Jonsson (1997) attributes to them a model in which errors in production planning in a few industries lead to coordination failure throughout the economy,[1] a view that seems consistent with the preceding quotations, as well as with Kates's (1997, 1998) analysis and Blaug's (1997) illuminating observations,[2] but while Jonsson's modeling may be in the right spirit, it goes far beyond anything I can find a classical economist

[1] Jonsson (1997, p. 215) writes: "This paper suggests that [Say and the Ricardians] were thinking along lines related to those now considered by modern temporary-equilibrium business cycle theorists . . . as well as the so-called New Keynesians. . . . That is, Say and the Ricardians explained gluts in terms of how miscalculation leads to coordination failures which in turn may limit the effective demand for goods. In contrast, Malthus and Sismondi argued that gluts were caused by the effect of uneven income distribution etc. On the absolute willingness to spend. . . . In short . . . the Say vs. Malthus debate mirrored some of the elements of the debate between (1) those who see coordination failures and sectoral shifts as the cause of business cycles and (2) simple underconsumptionists."

[2] Blaug (1997, pp. 234–5) writes: "Marxian unemployment is the result of both excessive population growth and price levels too low to produce an adequate flow of savings, combined with a primitive, rigid technology. Too little thrift, not insufficient aggregate demand, impedes the expansion of output. Marxian unemployment is a structural, not cyclical, problem and for that reason an easy monetary policy and an expansionary fiscal policy, effective in curing Keynesian [demand deficiency] unemployment, is much more likely to produce inflation without leading to full employment . . . I contend . . . that the classical economists grasped the fact that they were confronted with Marxian, not Keynesian unemployment, and that their misgivings about Sismondi and Malthus calling for more unproductive consumption by landlords were well-taken. But we in the western world are faced with Keynesian unemployment, which is indeed due to insufficient effective demand and which is indeed curable by standard demand management, albeit assisted by supply-side policies."

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to have written or said. In my view, all these interpretations are consistent with the earlier texts, but each describes only one of the several "Say's laws."

More Recent Interpretations and Critiques

John Maynard Keynes is often taken as the most substantial 20th century critic of Say's Law. Near the beginning of his *General Theory of Employment, Interest and Money*, Keynes (1936, pp. 18-19, 26) wrote:

> From the time of Say and Ricardo the classical economists have taught that supply creates its own demand;—meaning by this in some significant, but not clearly defined, sense that the whole of the costs of production must necessarily be spent in the aggregate, directly or indirectly, on purchasing the product . . . As a corollary of the same doctrine, it has been supposed that any individual act of abstaining from consumption necessarily leads to, and amounts to the same thing as, causing the labour and commodities thus released from supplying consumption to be invested in the production of capital wealth. . . .
>
> Evidently this amounts to the same thing as full employment . . . 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.

It can be argued that the first statement is a fair representation of the classical view. For example, Adam Smith (1776 [1904], Vol. I, pp. 320–321) wrote:

> What is annually saved is as regularly consumed as what is annually spent, and nearly in the same time too . . . By saving a part of [the rich man's revenue], as that part is for the sake of profit immediately employed as a capital either by himself or some other person, the food, clothing, and lodging, which may be purchased with it, are necessarily reserved for the latter. The consumption is the same, but the consumers are different.

Interestingly enough, Say himself did not always agree. In the *Letters to Mr. Malthus*, Say (1820 [1821], p. 36n) calls attention to the failure of demand during " . . . what happened to us in 1813 . . . . when interest of money fell so low, for want of good opportunities of employing it and by what is happening to us at this moment in which the capitals sleep at the bottom of the coffers of the capitalists."

Today's criticisms of Keynes's position on Say's Law emphasize two points. First, Keynes took into account only one of the complex of ideas that preoccupied the writers on the Law of Markets, and represented it as the whole. Second, Keynes offered an egregious mischaracterization of the views of Say and others

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by claiming that they denied the possibility of depression and unemployment and believed that all forms of intervention in the market to prevent or alleviate such conditions were, at best, redundant and, at worst, harmful. A charitable interpretation of the Keynesian critique might take him to be asserting that the classical *premises* implied that there could be ''no obstacle to full employment'' (at least during periods of intermediate length)—even though the classical economists were mistaken in failing to recognize this. But a more plausible conclusion, it seems to me, is that Keynes simply never really studied what Say (and James Mill) had written. It is perhaps significant that despite some interest in the history of economic thought, as illustrated in his *Essays in Biography* (1933 [1963]), in Chapter 23 of *General Theory* and elsewhere, Keynes (1936) mentions Say only three times in the *General Theory*, and mentions Say's Law only once. Only two of these four references are relevant to our discussion. Those are the passages quoted above.

More recent characterizations of Say's Law that have been adopted widely—and widely criticized in turn—are attributable to Oskar Lange (1942) and to Gary Becker and myself (1952). Lange proposed a formalization of the notion that supply creates its own demand in terms of the following identity in real output alone:

$$\Sigma_j p_j x_j = 0, \text{ for } (j = 1, \ldots, n),$$

where p_j is the price of good j and x_j is the excess demand for that item. The identity states that the sum of the money value of quantities of goods and services demanded at any time must be identically equal to the money value of the quantities offered for sale.

It can be maintained with some justice that the early advocates of the Say's Law positions did sometimes make assertions akin to this identity. There is an abundance of passages in the writings of Say and others advancing the claim, as in the above quotation from Adam Smith, that income not devoted to consumption will always be spent on investment, and without delay, because delay would forgo earnings on the capital. Lange's (1942) error, it seems to me, is parallel to that of Keynes. Even if this identity is related to the early Say's Law doctrine, it fails to recognize the many other fundamental strands of the discussion—including concern over unemployment and depression.

Becker and Baumol (1952) argued, citing some evidence, that Say and other writers recognized that the zero value of the sum of excess demands, or supply creates its own demand (''Say's identity''), may not hold in the short run. Say's passage in his *Letters to Malthus*, quoted above, even suggests an explanation—a desire to hoard or, as we would now put it, a temporary excess demand for money. But they thought the market would fairly quickly and automatically restore equilibrium (''Say's equality''). I can easily provide passages suggesting that the classical economists at least sometimes held a view closer to that than to the identity, but this is clearly not the place to pursue

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the issue. My themes here are that the supposed identity between supply and demand is hardly all there was to the "Law," that the relationship between supply and demand that did exist did not preclude depression or unemployment in the minds of its advocates, and that the term "Say's Law" itself may be a misnomer.

Once More Unto the Breach—Who Did Discover Say's Law?

Let me end with what is probably the least important but most intriguing issue, and the one most often discussed—who really originated Say's Law? The answer must be (as in Agatha Christie's thriller, *Murder on the Orient Express*) that they probably *all* did. There are many substantial strands to Say's Law, as I have emphasized, and different writers contributed or clarified different parts of the story. Jacob Viner taught me long ago the dangers of asserting that a doctrine was *first* enunciated by any particular writer. Such claims only encourage scholars to turn up earlier writers who asserted something related to the proposition in question. On these issues, as on so many others, Adam Smith had his predecessors and precursors,[3] but it was Smith who deserves credit for spelling out the proposition that all income is spent, or is desired to be spent, either on consumption or investment.

Twenty-seven years later, Say (1803) published the first edition of his *Traité*, in which he pointed out the subordinate role of money, which, in his view, was merely

[3] Priority has been ascribed to Smith's noted teacher, Frances Hutcheson, who formulated hints of the law of markets in his reply to that notorious doggerel poem, *The Fable of the Bees*, or more accurately, *The Grumbling Hive: or Knaves Turn'd Honest* (1705 [1924]) by Bernard de Mandeville, a Dutch-born physician living in England. Mandeville's defense of vice as a source of effective demand and prosperity gained him many readers and widespread denunciation. The following excerpt gives the flavor and may amuse the reader:

> All Trades and Places knew some Cheat,
> No Calling was without Deceit.
> The Lawyers of whose Art the Basis
> Was raising Feuds and splitting Cases . . .
> They kept off Hearings wilfully,
> To finger the refreshing Fee . . .
> Physicians valu'd Fame and Wealth
> Above the drooping Patient's Health . . .
> Thus every Part was full of Vice,
> Yet the whole Mass a paradise
> . . . Luxury
> Employed a Million of the Poor
> And odious Pride a Million more . . .
> Their darling Folly, Fickleness,
> In Diet, Furniture and Dress,
> That strange ridic'lous Vice was made
> The very Wheel that turn'd the Trade . . .

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a facilitator of commerce, and the superior contribution to national prosperity of "productive consumption" (investment) over unproductive. This was followed four years later by James Mill's (1807) pamphlet, *Commerce Defended*, whose immediate purpose, as the subtitle indicates, was to rebut the claim, ". . . that Commerce is not a source of National Wealth." More immediately important for our purposes, this tract explained more fully than Say's first formulation the grounds for their rejection of inadequacy of aggregate demand as an explanation for business depression. The second edition of Say's *Traité*, published in 1814, expanded its discussion of this point as well. Thus, if we take this to be the main message of Say's Law, I am inclined to accept Thweatt's (1979, pp. 92–93) judgment that: " . . . an examination of James Mill's writings [including book reviews, etc.] between 1804 and 1808 shows conclusively that Mill had indeed preceded Say, and that all things considered [including] Mill's original views, 'Adam Smith really is the father of the Say's Law discussion.'"

Finally, we may note that Say's contemporaries differed in their assessment of the originality of Say's contribution to the discussion. James Mill takes Say to have derived his discussion of the Law of Markets, along with most of his other ideas, from Adam Smith. Reviewing the first edition of Say's book, Mill (1805) remarked " . . . not only are all the general principles copied from Smith, but . . . the author has copied too slavishly."[4]

In contrast, Ricardo (1817 [1951], Vol. I. pp. 6–7) implies that Say may have added something to Smith in this arena.

> M. Say, . . . was the first, or among the first, of continental writers, who justly appreciated and applied the principles of Smith . . . and has enriched [political economy] by several discussions, original, accurate, and profound. Chap. xv. part i. [of the second edition] "Des Débouchés," contains, in particular, some very important principles which I believe were first explained by this distinguished writer.[5]

In a third appraisal, McCulloch (1845, p. 21) says of Say's book: " . . . except in so far as respects the inquiry relating to gluts, Say has left the science in precisely the same state in which he received it from Adam Smith." But writing even about Say's exposition of the principle "that effective demand depends upon produc-

[4] In an article on Lauderdale (1804), Mill had in effect himself all but attributed the Law of Markets to Smith. However, later (1808), as an anonymous reviewer of his own *Commerce Defended* (!), Mill praised his discussion of the law as " . . . an excellent specimen of Mr. Mill's acuteness and powers of abstraction." I am deeply grateful to Professor Thweatt for drawing my attention to these reviews and articles by Mill.

[5] Yet Ricardo soon had reason for second thoughts on Say's perspective, after reading Say's *Letters to Mr. Malthus* quoted earlier in the text. In a letter of November 24, 1820, Ricardo wrote to Malthus: "I have also written some notes on M. Say's letters to you with which I am by no means pleased . . . . he yields points to you, which may almost be considered as giving up the question, and affording you a triumph" (appearing in 1951, vol. VIII, pp. 301–302).

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tion," McCulloch (p. 21) remarks: "This principle had been previously advanced by [others]."[6]

The bottom line is that to them, as to us, the Law may justly be deemed partly Say's. But it is emphatically not Say's alone.

[6] Curiously, though McCulloch (1845, p. 56) lists Mill's tract, he never mentions it in connection with the Law of Markets.

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