PART IV

EXCHANGE OF WEALTH

CHAPTER XXVI

VALUE AND PRICE

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Leaving now the subject of the production of wealth, we pass on to a brief consideration of some of the more important problems connected with its exchange. Wealth would be of little value, if, after it had been produced, it were not transferred from one individual to another. It will readily be seen that the complex conditions of modern industrial life, due to separation of employments and division of labor, make it impossible for one man to produce all the economic goods that he requires for his own consumption. The process by which he secures goods from others in return for his own goods is known, in economics, as the exchange of wealth.

Value. — Goods would not be desired and exchanged for one another, unless they possessed value. In a popular sense, the term "value" is given a wide application. We speak of the value of an individual to a community or of the value of an educational or of a religious system to society. In this sense, the term refers to the desirable qualities in the person or institution. In this manner we think of "personal values," "educational values," and "religious values" — each one of these phrases illustrating the general meaning of the term "value" as used in everyday life.

Its nature: *General meaning.*

In economics, however, the term "value" has a special significance and arises primarily from the utility of economic goods. It will be remembered that "wants" are the desires which individuals have for economic goods. Utility is the want-satisfying quality of a good. Therefore any economic good possessing utility has, in consequence, economic value.

Economic meaning.

But not all goods are economic; some are free. Occasionally things are so plentiful that, although they have utility, they do not possess value in the economic sense. For example, water, a free gift of nature, may or may not have economic value. Frequently it has not because it is not an economic good, — no one would give something upon which he had spent time and effort in exchange for it. But, to a man adrift on the South Pacific, the value of drinking water would be inestimable, — he would give anything in exchange for it. Thus in addition to utility, scarcity is necessary to economic value.

It has already been pointed out that utility is not synonymous with usefulness. Utility is simply the quality in an economic good which satisfies a want. Now, if an individual wants something that is not useful, this useless thing will possess utility. A diamond necklace or a quart of whisky may therefore posssess as much utility, and consequently value, as a well-furnished house or a nourishing diet. We may, therefore, conclude that economic value is the worth, without any necessary regard to the usefulness, that is attached to economic goods.

Forms of value.

If now we stop to consider for a moment, we shall see that this worth may be estimated either by the individual for his own special use, or by the whole group for purposes of exchange. This difference in the methods of estimating the worth of economic goods gives rise to two forms of economic value: value in use and value in exchange.

Value in use.

Value in use is purely subjective; that is, it is simply an individual estimate of the worth of a given commodity. One individual may value the utility of a certain economic good far more highly than would another individual. In this determination of value, personal peculiarities play a large part. For example, a silver spoon that has become an heirloom may satisfy such an intense want in an individual that he will value it far beyond its intrinsic worth. This individual valuation of the spoon is clearly not a measure of its general or social value. While this is an exaggerated case, nevertheless, it is perfectly true that individual valuations cannot be just estimates of values put upon goods by society as a whole. Therefore, economics is concerned primarily with the second kind of value, — value in exchange.

Value in exchange is a social valuation placed upon an economic good by a number of persons. Of course, a good must have value in use before it can have value in exchange. But, in determining value in exchange, the good is looked upon, not from the standpoint of its utility to a single individual, but from the point of view of its worth to a whole group of people. Thus, value in exchange is the social estimate of the general worth of an economic good and represents the "power of a good to command other goods in exchange for itself."

Value in exchange: *Meaning.*

In determining this exchange value of a commodity, its utility naturally plays an important part. But utility, itself, is variable. In discussing this subject under the head of consumption, we saw that to the tired traveler the utility of the first apple is much greater than the utility of the third apple; and that, in consuming apples, he soon reaches a stage where the utility is so low that he desires no more. This lowest utility of the apple is called its marginal utility, and it is upon this marginal utility that value in exchange depends, because no one will give more for apples than an amount representing the satisfaction which he expects to derive from the last apple which he consumes. Furthermore, it is not the marginal utility of a commodity to a single individual that determines its exchange value; but it is its marginal utility to a whole community that is the measure of this value. Thus, ex-

How determined.

change value depends upon the estimate that society places on marginal utilities.

In determining exchange value there is still another point that must not be overlooked. The value of an economic good varies with the relation of supply to demand. This, however, is only another way of saying that it depends upon marginal utility, because an increase in the supply of a commodity means a decrease in its marginal utility; and this, in turn, means a fall in value. On the other hand, a decrease in the supply of a good means an increase in its marginal utility, and a corresponding rise in value. From this standpoint, therefore, the amount of economic goods (supply) contrasted with the intensity and prevalence of wants (demand) determines value in exchange.

For example, if the demand remains the same and there is an increase in the supply of turkeys, their marginal utility will decline and their exchange value fall. But if, with the approach of Christmas, the demand for turkeys increases and the supply remains stationary, the marginal utility of turkey will become greater and the exchange value higher. This relation between supply or goods, on the one hand, and demand or wants, on the other, must always be reckoned with.

Price. — Price is exchange value expressed in terms of money. When, for example, we wish to express the exchange value of some commodity, such as a pear, we do so in terms of some other commodity which is used as a standard of measuring all values. We do not say that the pear is worth two apples, but that the pear is worth two cents; because money, not apples, is the standard by which all economic values are measured. Money thus becomes a common denominator of value, and prices are expressed in terms of this commodity.

What price is.

It will be observed that we have said that money is a commodity, exactly like pears or apples. This is true, because money is merely some form of metal which is as much an economic good as oil or coal. In the United States, it represents gold. Now since gold is a commodity, it is subject to the same law of value as any other commodity. That is, if its supply increases in a greater proportion than the demand, its value will decrease correspondingly. Under these circumstances, therefore, instead of pears being worth two cents, they may now be worth three cents; and the prices of all other goods will rise similarly, because the value of gold (or money) has fallen. Conversely, if the supply of gold diminishes as compared with other goods, the prices of commodities will fall because the value of gold has risen. Consequently, a general rise or a general fall of prices is possible. On the other hand, there can be no general rise or general fall of values, because exchange value represents the purchasing power of a commodity; that is, a relation between two commodities. If, therefore, the value of one of these goods rises, the value of the other must fall. If a pear formerly exchanged for two apples, and now exchanges for three, the value of the one has increased at the expense of the other. Therefore, there can be no general rise or fall in values.

Difference between prices and values.

Under conditions of free competition, buyers and sellers meet on a common ground — the market place — and there determine price by deciding as to the value of commodities. The value agreed upon is the price, and it is expressed in terms of money. The price will depend upon the law of supply and demand governing value. The seller will look at the problem largely from the standpoint of production, and the buyer

How determined: *When competition is free.*

from the standpoint of consumption. This method of determining price is still in vogue, to-day, in backward and rural communities. In fact, even in some civilized European countries, such as Greece and Italy, "bargaining" is still resorted to as a method of determining prices. Usually, however, in large modern societies, the one price system has been adopted. That is, the seller estimates the value of the good to the community in terms of price. If his estimate is correct or nearly so, he sells the commodity; if not, he changes the price to conform to the social estimate. Thus, price represents the point at which the seller and the buyer meet in their estimate of value.

When competition is not free.

From this discussion we have seen how price would be determined normally. On the one hand, among producers there would be free competition, and, on the other, among consumers there would be wants of varying degrees of intensity; while the law of supply and demand would form the backbone of the whole process. But conditions are not always as here depicted. In fact, in modern industrial society, conditions of production are continually changing. Competition gives way to monopoly, and cost of production plays a diminishing part in determining prices. Consequently, in this absence of competition the monopolist fixes the price at a point which affords him the greatest monopoly profit.

TOPICS FOR CLASS DISCUSSION

1. Does every good possess utility? Is everything which possesses utility a good?

2. Have the following utility: whisky, a gambler's pack of cards, clothes of antiquated fashion, opium, grand opera, air?