

Economics in 30 Minutes

Part 2: Why Prices Are What They Are

Vincent Maistre

Around 1900, why was flour dear?

The wheat crop was poor.

The trusts are keeping prices up.

Speculators.

The railroad charges too much to haul it.

There's more gold around, so everything costs more.

These explanations describe different forces. We need a way to sort them.

First idea: things are worth the labor in them

Smith, Ricardo, Marx



\$4,000

*Forty hours of my labor.
One terrible chair.*

Marx's reply: only socially necessary labor counts.

Ricardo's own exception

Rare statues and pictures.

Scarce books and coins.

Wines from grapes grown on one particular soil.

No amount of labor makes more of them.

*Labor requirements alone don't tell us
today's market price.*

Second idea: price covers what it cost to make

*Costs explain why nobody sells below a floor forever.
They don't explain why anyone wants the thing.*

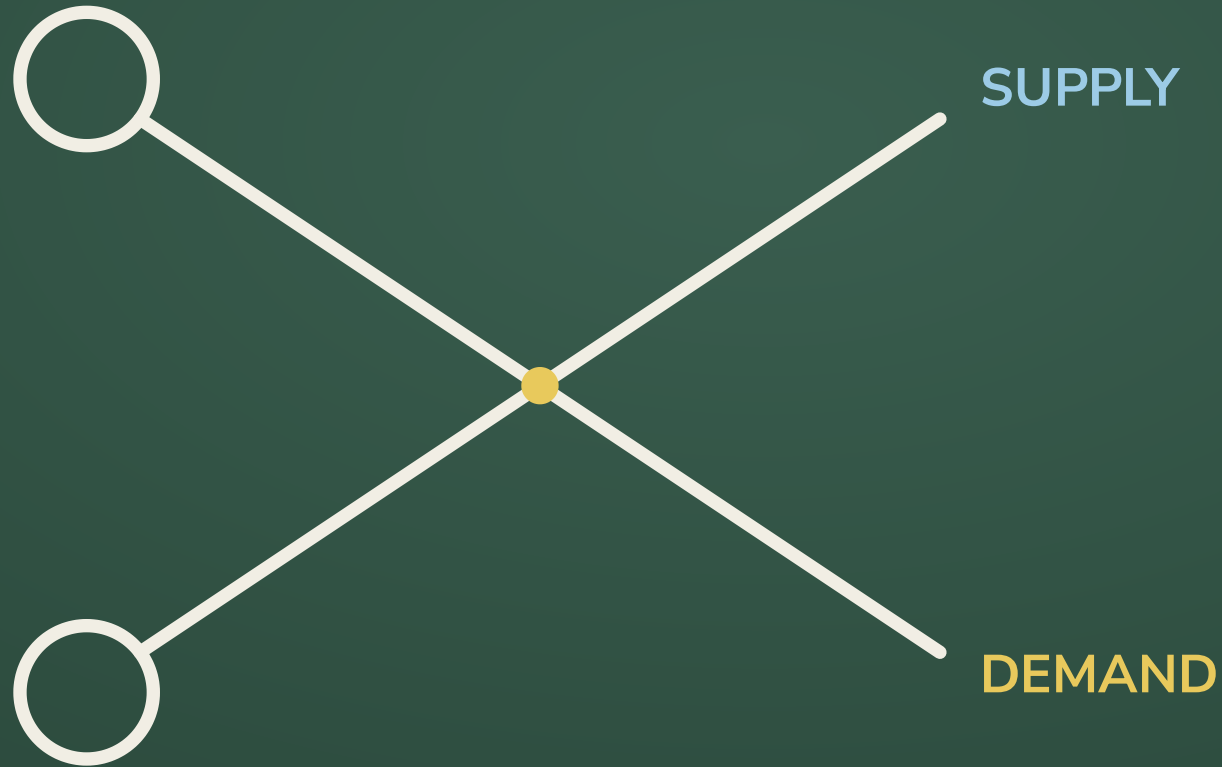
Rent, in one sentence

Ricardo: good land earns more than bad land.

von Thünen: land near the market earns more than land far away.

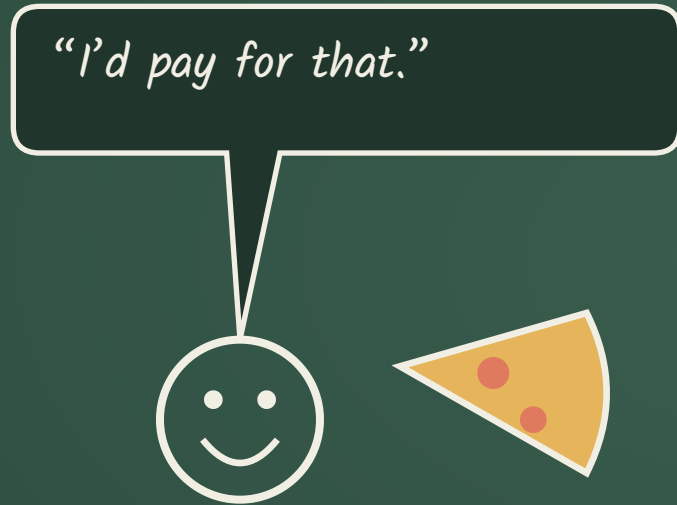
True. And still only part of a price.

Marshall, 1890



*Which blade of the scissors
cuts the paper?*

Slice one



Slice seven



Same slice every time. What changed is how much the next one is worth to you.

Pause

*What would you pay
for the next slice?*

*One number when you're hungry.
One number after you've had four.*

Thinking at the margin

*Economists don't ask "is this good?"
They ask "is one more worth it?"*

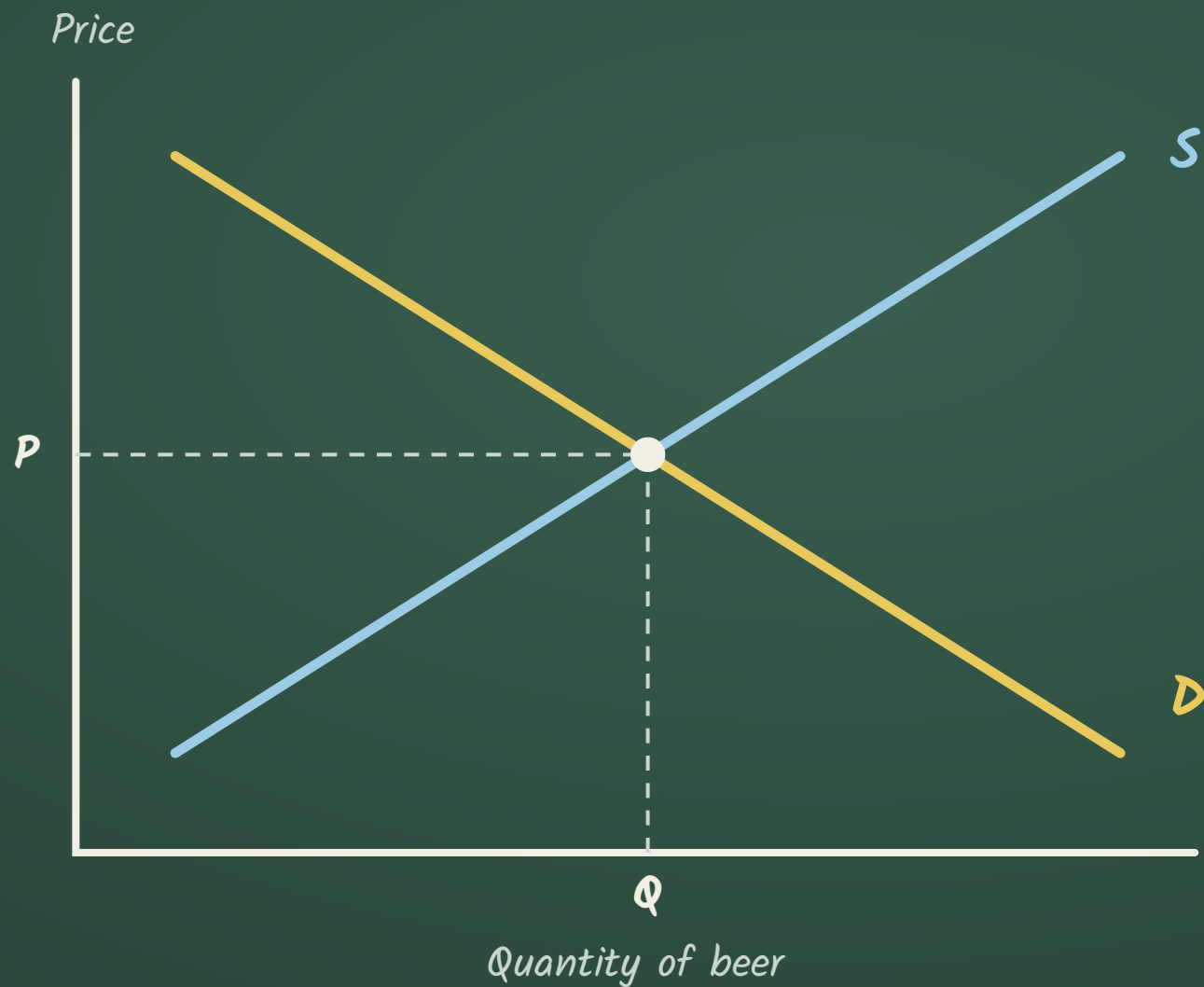
The next slice.

The next hour of studying, against the next hour of sleep.

The next worker, against the wage.

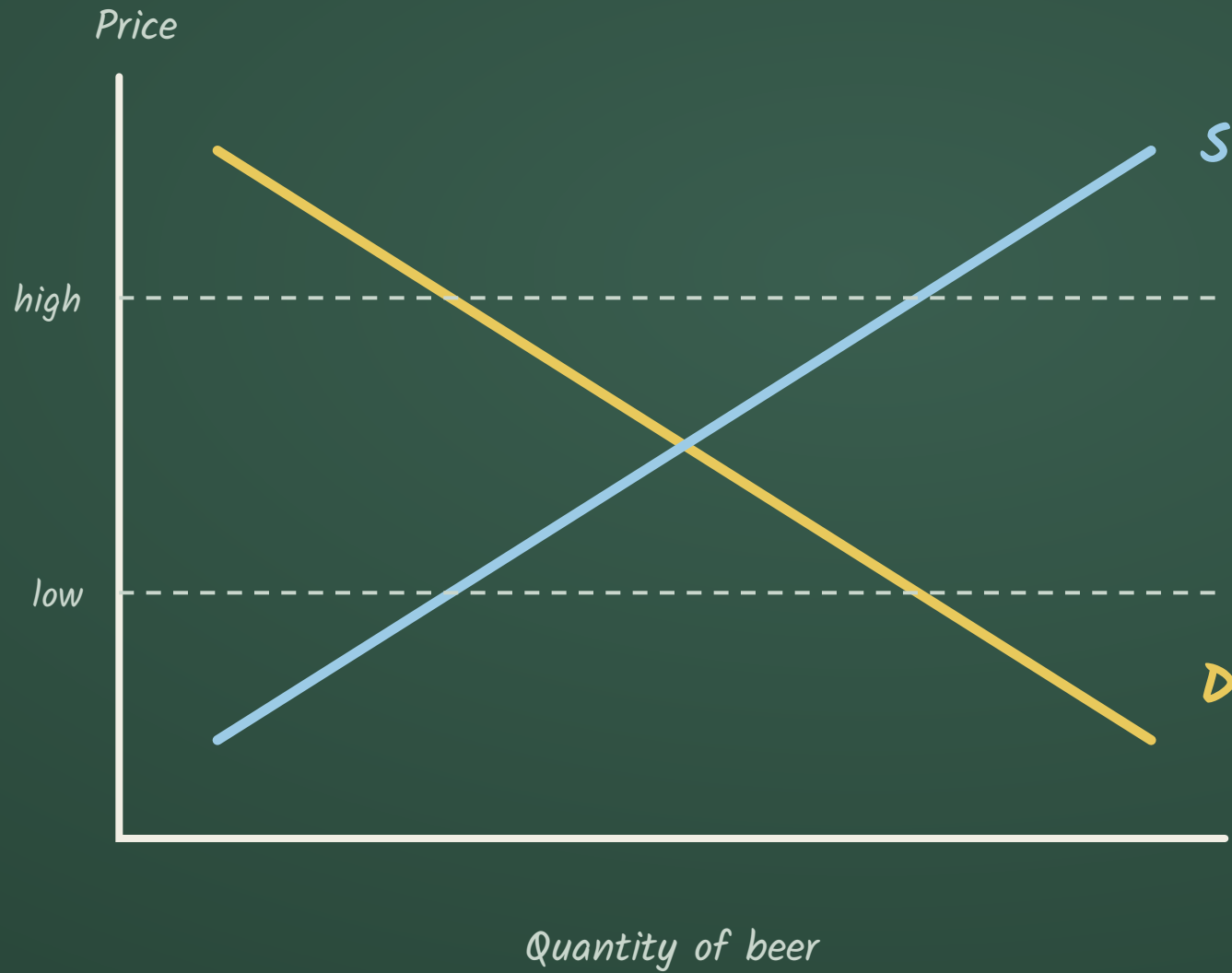
The next beer, against eight dollars.

The market for beer



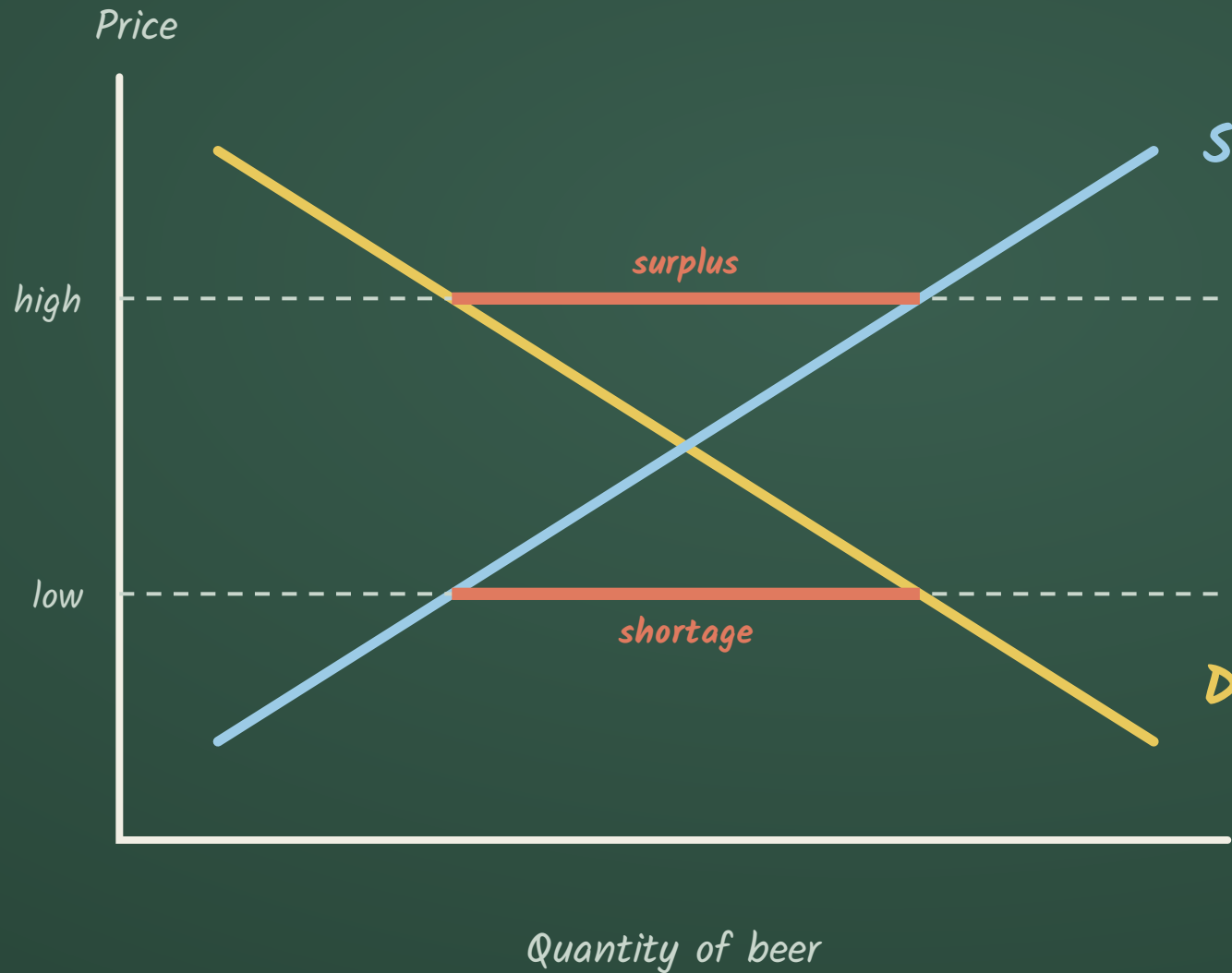
Where the lines cross:
buyers want to buy
what breweries want to sell.

Keep in mind



*Below the crossing?
Above it?
What does each do
to the price?*

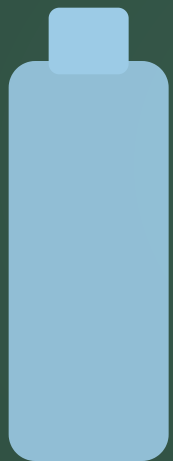
Below and above the crossing



Below the crossing: buyers want more than sellers offer. That shortage pushes the price up.

Above it: sellers offer more than buyers take. That surplus pushes the price down.

The water-diamond paradox



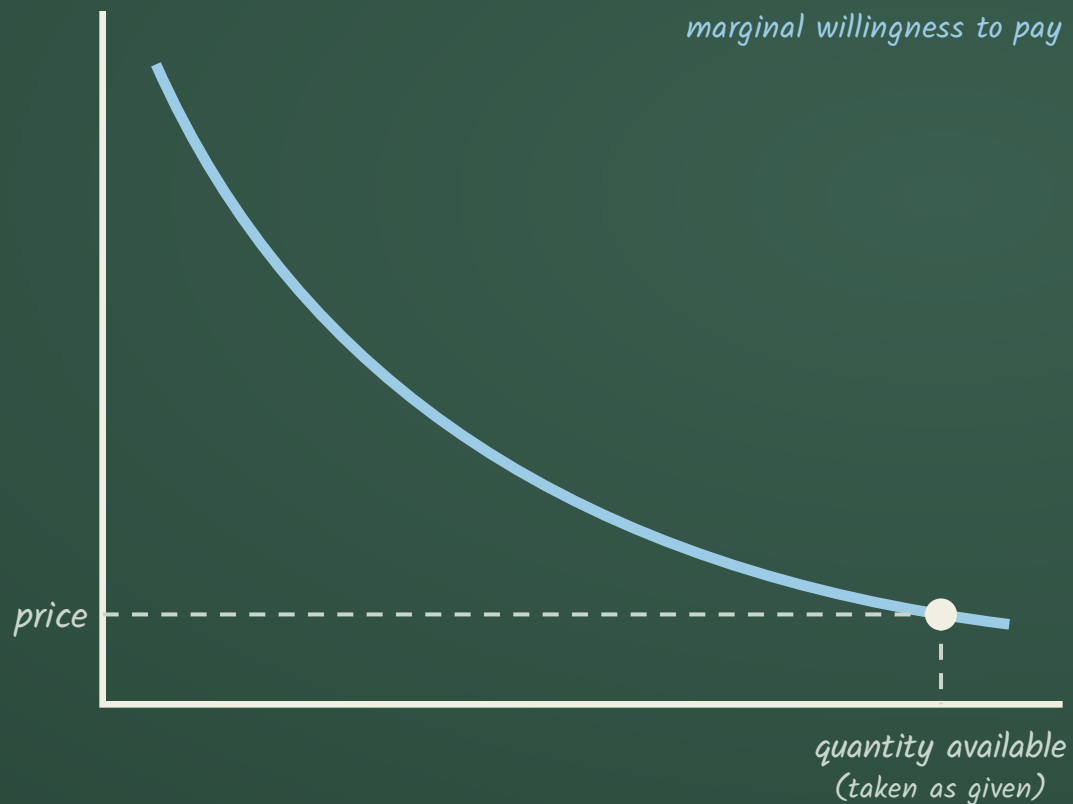
\$1.79



\$6,000

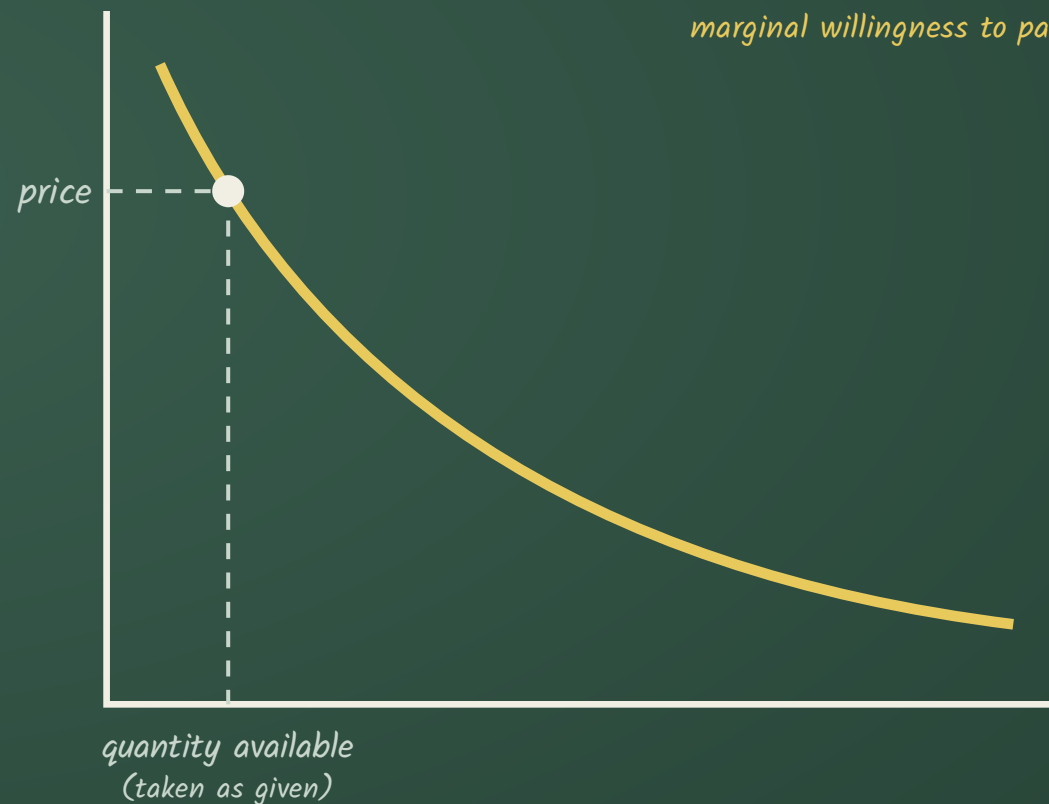
ECONOMICS APPEARS TO HAVE MADE A MISTAKE.

Water



Lots of it. The next gallon is worth little.

Diamonds



Few of them. The next one is worth a lot.

*The price reflects the value
of one more unit,
given how much we already have.*

Not all the water in the world. Not all the diamonds. One more.

The marginal revolution, 1870s: Jevons, Menger, Walras.

The diamond complication

*For most of the last century, one company controlled most of the world's rough diamonds.
It stockpiled stones and released them slowly.*

1947: "A Diamond Is Forever."

*Part of the scarcity is natural.
Part of it was managed.
Part of the demand was advertised.*

Your turn

Pause the video.

Three questions before Part 3.

Your turn

1

A price went up: gas, rent, eggs, tickets.

What explanation did you hear from friends or family?

Which of the 1900 stories was it?

What did it leave out?

Your turn

2

Have you used economics to explain something that actually happened?

Which market? What was your explanation?

What evidence would make you revise it?

Your turn

3

When oil moves, a lot of other prices move.

*Trace one chain from a barrel of oil
to something you buy.*

Does every link move the same direction?

Next

Part 3: How markets change

*Start from the beer graph.
Then move the lines.*

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Companion page: [link in the video description](#)