Chapter 12: The Marginalist School

The Historical Background of the Marginalist School

Even after 100 years after the beginning of the industrial revolution serious economic and social problems remained unsolved. Poverty was widespread although productivity increased dramatically. The extreme uneven distribution of wealth and income created much dissatisfaction even though the general standard of living was increasing. Business fluctuations affected many people indirectly, individuals could no longer depend exclusively on their own initiative and ability to overcome conditions that were thrust upon them.

Farmers and farm labourers had their difficulties, many drifted into town for better opportunities. Industrial accidents often brought serious hardships to workers and their families before workers' compensation laws were there. Long working hours and dangerous and unhealthy working conditions, the economic power of employers in bargaining with workers, the rise of monopolistic enterprises, and insecurity in old age were among the many problems that cause people to seek alternative solutions.

The major Tenets of the marginalist School

* Focus on the margin: The school focused its attention on the point change where decisions are made, in other words, the margin.
* Rational economic behaviour: The marginalists assumed that people act rationally in balancing pleasures and pains, in measuring utilities of different goods, and balancing present against future needs.
* Microeconomic emphasis: Instead of considering the total economy, or macroeconomics, the marginalist school considered individual decision making, market conditions for a single type of good, the output of a specific firm.
* The use of abstract deductive method: The marginalists rejected the historical method in favour of analytical, abstract approach.

* The pure competition emphasis: The marginalists based their analysis on the assumption of perfect competition. This world is small, individualistic, independent entrepreneurs, numerous buyers, many sellers, homogeneous products, uniform prices, and no advertising.

* Demand-orientated price theory: For the early marginalists, demand became the primary force in price determination.

* Emphasis on subjective utility: Demand depends on marginal utility. Costs of production include the sacrifices and the ~~irration~~ irritation of working, managing a business, and saving money to form a capital fund.

* Equilibrium approach: Economic forces generally tend towards equilibrium - a balancing of opposing forces.

* Merger of land with capital goods: The marginalists lumped together land and capital in their analysis and spoke of interest, rent, and profits as being the return to property resources.

* Minimal government involvement: The marginalists continued the classical school's defense of minimal government involvement in the economy as the most desirable policy.

Whom Did the Marginalists Benefit or Seek to Benefit?

① They sought to benefit all mankind through promoting a better understanding of how a market system efficiently allocates resources and promotes economic liberty.

② They benefited the employers by opposing unions and by attributing unemployment to wages that were artificially high, inflexible on the down side, or both.

③ They defended land owner's against Ricardo's rent theory.

④ They benefited the wealthy who generally opposed the government intervention and the distribution of income.

How was the marginalist school valid, useful or correct in its time?

☺ → The marginalists developed new and powerful tools of analysis, especially geometric diagrams and mathematical techniques. Thanks to the marginalists economics became a more exact social science.

☺ → Conditions of demand were given their rightful importance as one set of determinants for prices of both final goods and factors of production.

☺ → They emphasized individual decisions, this was valid in a world where such decisions were significant in determing the course of economic activities.

☺ → The method of partial equilibrium analysis champicned by many members of this school was useful for abstrating from the complexity of the real world. This approach (allowing one variable at a time to change while holding all other variables temporarily constant) enabled investigators to look at this complicated phenomenon one step at a time. As they introduced successive variables, they eventually approached more realistic situations.

☺ → The microeconomic approach of marginalists complements the macroeconomic approach, which may overlook many problems by viewing the economy as a whole.

Which were the lasting contributions of the marginalist school?

* → Many marginalist theories remained relatively untouched and they are found in contemporary textbooks on principles of microeconomics.

* → The marginalist school was eventually absorbed by the broader neoclassical school, which, together with variations of Keynesian macroeconomics, dominates economic analysis in Western countries and shares the international field with socialism.

* → These economists and their forerunners developed lasting contributions as mathematical economics, the basic monopoly model, a theory of duopoly, the theory of diminishing marginal utility, the theory of rational consumer choice, the law of demand etc.