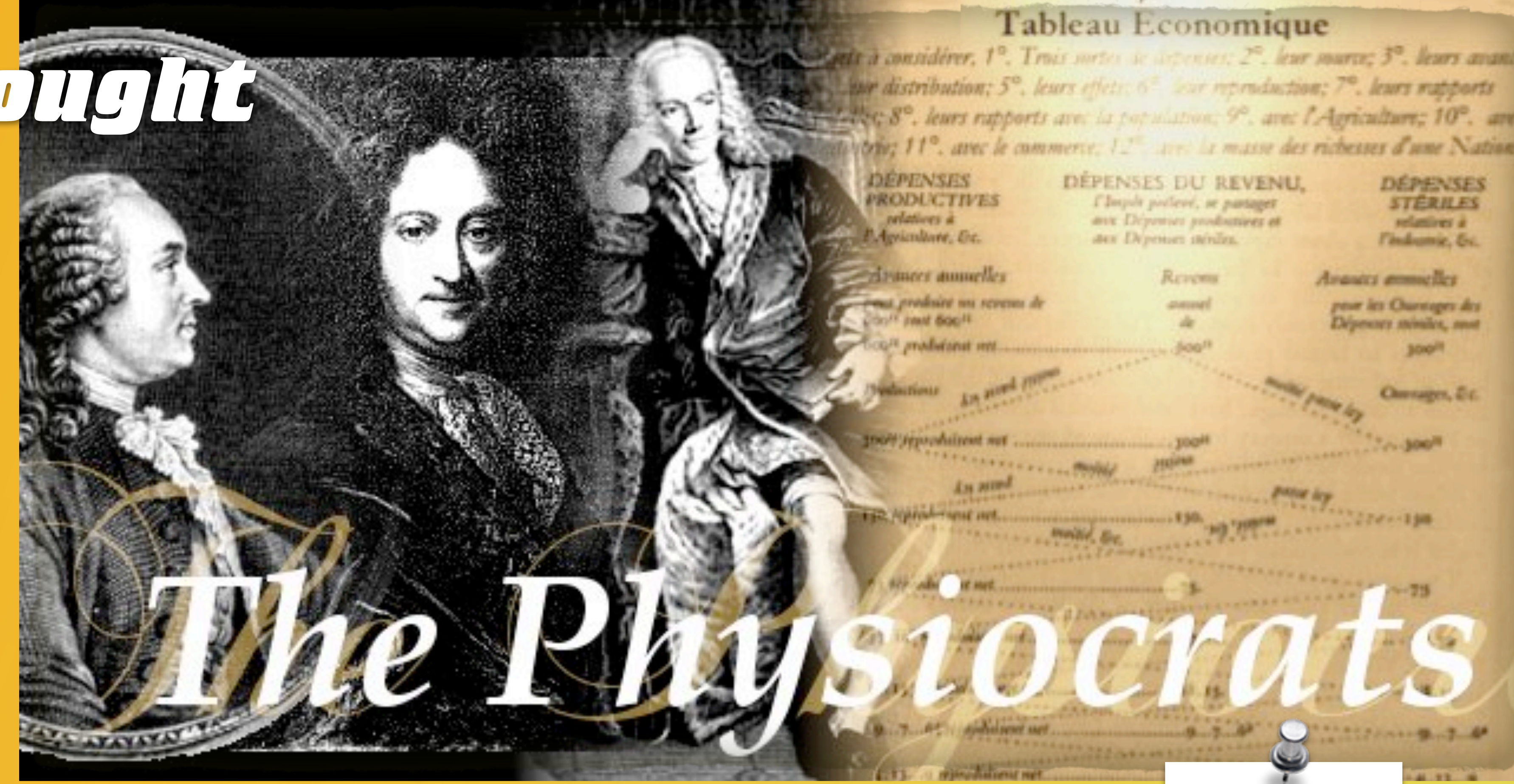
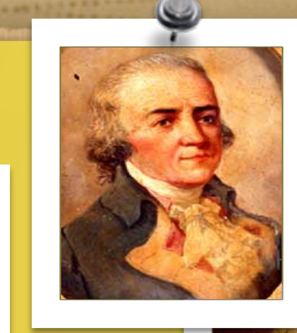
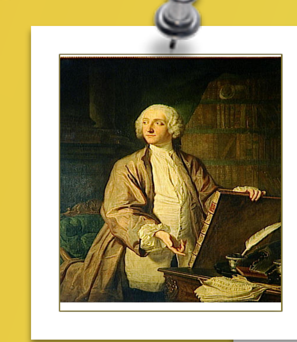
# The history of economic thought




*The Physiocrats were a group of economists who believed that the wealth of nations was derived solely from agriculture. Their theories originated in France and were most popular during the second half of the eighteenth century. The term "Physiocracy" itself, introduced by Dupont de Nemours (1767) literally translates to "the rule of nature." Physiocracy is perhaps the first well developed theory of economics. It immediately preceded the first modern school, classical economics, which began with the publication of Adam Smith's The Wealth of Nations in 1776.*

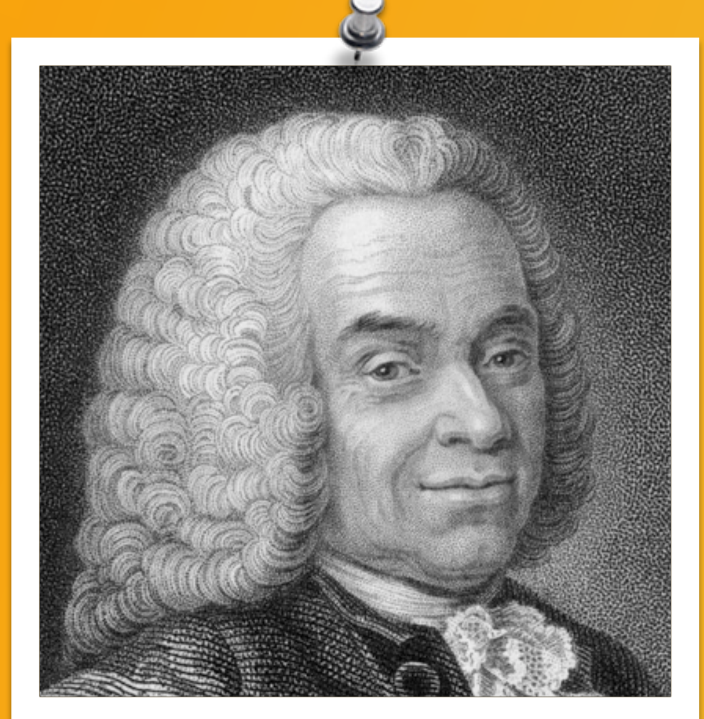
## The main representatives are:

- *François Quesnay,*
- *Anne-Robert-Jacques-Turgot*
- *Marquis de Mirabeau,*
- *Dupont de Nemours*

## Physiocracy

- *The cornerstone of the Physiocratic doctrine was an axiom that only agriculture yielded a surplus - what they called a net product.*
- *Physiocrats took up as much value as inputs into production as it created in output, and consequently created no net product.*
- *Physiocrats believed that the wealth of a nation lies not in its stocks of gold and silver, but rather in the size of its net product.*
- *artisans and manufacturers should come to France only in proportion to the size of the internal market for their goods*
- *country should concentrate on manufacturing only to the extent that the local availability of raw materials and suitable labor enabled it to have a cost advantage over its overseas competitors*
- *Anything above that amount should be purchased through trade.*
- *industry produces no gain in wealth*
- *redirecting labor from agriculture to industry will in effect decrease the nation's overall wealth*
- *population expands to fill available land and food supply*
- *therefore, population must go down if the use of land does not produce food*
- *believed that trade and industry were not sources of wealth*



## Quesnay's Tableau Économique

- *the foundation of the Physiocrats' economic theories*
- *agricultural surpluses, by flowing through the economy in the form of rent, wages and purchases, were the real economic movers*
- *As land is the only source of wealth, then the burden of all taxes bears down on the landowner.*
- *So instead of levying a complicated collection of taxes, it is most efficient to just go to the root and tax land rents directly, so called "single tax"*

*The model Quesnay created consisted of three economic movers:*

- *The "Proprietary" - only landowners*
- *The "Productive" - agricultural laborers*
- *The "Sterile" - artisans and merchant*

*The economy produces a surplus of food, and neither the farmer nor the artisan can afford to consume more than a subsistence level of food. The landlord is assumed to be consuming at a level of satiation; therefore, he cannot consume any more. Since food cannot be stored easily, it is necessary to sell it to someone who can use it. This is where the merchant provides value.*

## The laws which the Physiocrats discovered operating in the economy were the following:

- *the natural tendency of mercantilism is to produce wealth, so that mercantilism left to its own devices would increase the wealth of a nation;*
- *the natural tendency of merchants is to serve their self-interest, but in pursuing their self-interest everyone benefits from the excess wealth they create;*
- *mercantilism naturally results in increasing the productivity of labor.*
- *Government interference in mercantilism—through taxes, regulations, price controls—hinders the activities of merchants and so prevents these natural laws of economics to take place; none of the benefits—increased wealth, increased productivity—will be realized by regulated mercantilism.*
- *The Physiocrats argued, then, that government leave the economy alone and allow individuals within the economy to do as they please in attempting to realize their own selfish interests; this doctrine they called laissez faire, or "let them do."*

*None of the theories concerning the value of land could work without strong legal support for the ownership of private property. Combined with the strong sense of individualism, private property becomes a critical component of the Tableau's functioning.*

***Jacques Turgot** was one of the first to recognize that "successive applications of the variable input will cause the product to grow, first at an increasing rate, later at a diminishing rate until it reaches a maximum".This was a recognition that the productivity gains required to increase national wealth had an ultimate limit, and, therefore, wealth was not infinite.*
*Both Quesnay and Turgot recognized that capital was needed by farmers to start the production process, and both were proponents of using some of each year's profits to increase productivity. Capital was also needed to sustain the laborers while they produced their product. Turgot recognized that there is opportunity cost and risk involved in using capital for something other than land ownership, and he promoted interest as serving a "strategic function in the economy."*

*The Physiocrats, based on Quesnay's analysis, had identified three classes in the economy:*
*the "productive" class (agricultural laborers and farmers), the "sterile" class (industrial laborers, artisans, and merchants) and the "proprietor" class (who appropriated the net product as rents). Incomes flowed from sector to sector, and thus class to class.*
*A "natural state" of the economy emerged when these income flows were in a state of "balance," that is, where no sector expanded and none contracted. Once the "natural state" was achieved, the economy would just continue, reproducing itself indefinitely.*
*The Physiocrats, unlike many of their contemporaries, continued to view the state as a parasitical entity, living off the economy and society, but not part of it. According to this view, government has no prescribed place in the ordre naturel. Its only role is to set the laws of men in a way that permits the God-given laws of nature to bring the natural order about. They regarded any attempt by the government to influence the economy against these natural forces as leading to imbalances which would postpone the arrival of the natural state and keep the net product below what it would otherwise be. A general laissez-faire policy and the "single tax" were the speediest, least distortionary, and least costly ways of arriving at the natural state.*