



SAY'S LAW OF MARKETS

Md. Zikrullah Khan
Assistant Professor & HoD
Department of Economics

Say's Law of Market

- Say's Law of Markets is the core of classical theory of employment.
- A famous French Economist **Jeane Baptiste Say** enunciated the formal statement that “**Supply creates its own demand**”
- It implies that the supply of goods generates sufficient income to create demand for goods equal to its supply.
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- Therefore, there is no possibility of over production and unemployment in the economy.
- Even if there is some unemployment in the short run, the economy automatically tends towards full employment in the long run.

Assumptions of Say's Law of Markets

- ❑ There is free Market Economy.
- ❑ No Government intervention.
- ❑ Automatic adjustment of economic system due to flexibility of wages, interest and prices.
- ❑ Extent of Market is limitless.
- ❑ Closed Economy, no trade links with any other country.
- ❑ Money is only a medium of exchange.
- ❑ Validity of long run.
- ❑ Optimum allocation of resources.

Important facts of Say's Law

- **PRODUCTION CREATES DEMAND FOR GOODS**
- With the use of inputs in production process, income is generated. This income is distributed to the owner of inputs which they ultimately spend on purchasing goods for their use. This causes demand for produced goods. This is how supply creates its own demand.
- **BARTER AND MONETISED ECONOMY**
- Say's Law holds good in barter economy. It is because, goods are produced for self consumption or to get other goods in exchange for the produce. When people offer their produce in barter for other goods, they create demand for the goods. This law is also valid in monetised economy. In this economy money is used to buy or sale goods and services. The inputs used in production generate money incomes in the form of wages, interest, rent and profits. The incomes are spent on purchasing the goods produced. It creates demand. It implies that if there is demand for goods whose production creates income. Thus, supply creates its own demand for goods whose production creates income.. Thus, supply creates its own demand.

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□ **NO GENERAL OVERPRODUCTION**

- Say's law states that there is no general overproduction. When there is an increase in production, there is also increase in income of related factors. Consequently new demand is created and there is no general over production. General overproduction may exist in the short run but it is automatically adjusted by the market forces of demand and supply in the long run.

□ **SAVING AND INVESTMENT EQUALITY**

- Generally income is spent on consumption. When some amount of income remains unspent on consumption or saved, overproduction may exists. But it is rate of interest which plays important role to make a decision for both the consumers and producers about saving and investment. How much to save and how much to invest, depend on rate of interest. The interaction for demand for and supply of saving as a capital determines equilibrium rate of interest in market at which the equality between saving and investment is restored and there is no over production.

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LABOUR MARKET

Labour always seek higher wage rate but it causes a fall in demand for labour and rise in unemployment. In a free market economy flexible rate of wages automatically restores full employment through the interaction of demand for and supply of labour.

Implication of Say's Law

The implications of the law are as follows:

SELF ADJUSTMENT MECHANISM

According to Say's law, the self-adjustment mechanism brings up equilibrium in different markets. So equilibrium is a temporary situation. In a capital market, equality between saving and investment is restored by the flexible interest rate, while in the labour market, equality between demand for and supply of labour is maintained by the wage rate.

WAGE CUT CREATES FULL EMPLOYMENT

This law assumes that a wage cut helps to restore full employment by reducing production cost and price level and increasing demand for goods. It denies the wage rigidity policy in the economy.

NEUTRAL ROLE OF MONEY

This law is based on a barter system where goods are exchanged for goods. There is also assumed that money is just a medium of exchange; it does not affect the production process. So the role of money is neutral.

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□ **FULL EMPLOYMENT IN THE ECONOMY**

- According to Say's law there is full employment in the economy. It is because increase in production means increase in employment and production continues until the full employment is reached. In such a condition production will be maximum.

□ **PROPER UTILISATION OF RESOURCES**

- This law is based on full employment in the economy. According to which the proper utilisation of idle resources are ensured which will further help to produce more and also generate more income.

□ **NO GENERAL OVERPRODUCTION**

- There is no general overproduction and no unemployment. Increase in production generates income for inputs and further demand is created for the produce.