FACULTY OF JURIDICAL SCIENCES

Lecture-3

CLASSICAL THEORY

Classical economics is a broad term that refers to the dominant school of thought for economics in the 18th and 19th centuries. Most consider Scottish economist Adam Smith the progenitor of classical economic theory. However, Spanish scholastics and French physiocrats made earlier contributions. Other notable contributors to classical economics include David Ricardo, Thomas Malthus, Anne Robert Jacques Turgot, John Stuart Mill, Jean-Baptiste Say, and Eugen Böhm von Bawerk.

- Classical economic theory was developed shortly after the birth of western capitalism. It refers to the dominant school of thought for economics in the 18th and 19th centuries.
- Classical economic theory helped countries to migrate from monarchic rule to capitalistic democracies with self-regulation.
- Adam Smith's 1776 release of the *Wealth of Nations* highlights some of the most prominent developments in classical economics.
- Theories to explain value, price, supply, demand, and distribution, were the focus of classical economics.
- Classical economics was eventually replaced with more updated ideas, such as Keynesian economics, which called for more government intervention.

Self-regulating democracies and capitalistic market developments form the basis for classical economics. Before the rise of classical economics, most national economies followed a top-down, command-and-control, monarchic government policy system. Many of the most famous classical thinkers, including Smith and Turgot, developed their theories as alternatives to the protectionist and inflationary policies of mercantilist Europe. Classical economics became closely associated with economic, and later political, freedom.

The Rise of Classical Economics

Classical economic theory was developed shortly after the birth of western capitalism and the Industrial Revolution. Classical economists provided the best early attempts at explaining capitalism's inner workings. The earliest classical economists developed theories of value, price, supply, demand, and distribution. Nearly all rejected government interference with market exchanges, preferring a looser market strategy known as laissez-faire, or "let it be."

Classical thinkers were not completely unified in their beliefs or understanding of markets although there were notable common themes in most classical literature. The majority favored free trade and competition among workers and businesses. Classical economists wanted to transition away from class-based social structures in favor of meritocracies.

The Decline of Classical Economics

The classical economics of Adam Smith had drastically evolved and changed by the 1880s and 1890s, but its core remained intact. By that time, the writings of German philosopher Karl Marx had emerged to challenge the policy prescriptions of the classical school. However, Marxian economics made very few lasting contributions to economic theory.

A more thorough challenge to classical theory emerged in the 1930s and 1940s through the writings of British mathematician John Maynard Keynes. Keynes was a student of Alfred Marshall and admirer of Thomas Malthus. Keynes thought that free-market economies tended toward under consumption and under spending. He called this the crucial economic problem and used it to criticize high-interest rates and individual preferences for saving. Keynes also refuted Say's Law of Markets.

Keynesian economics advocated for a more controlling role for central governments in economic affairs, which made Keynes popular with British and American politicians. After the Great Depression and World War II, Keynesianism had replaced classical and neoclassical economics as the dominant intellectual paradigm among world governments.