



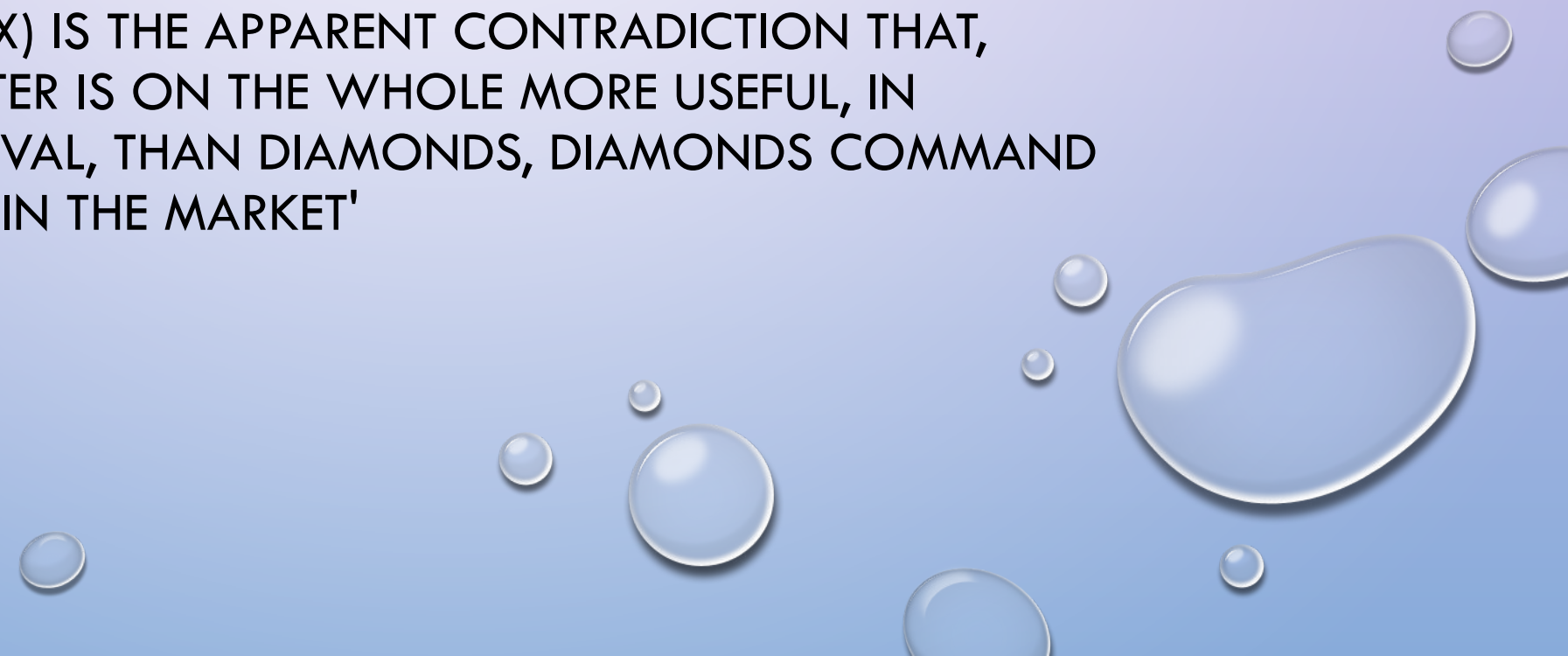
DIAMOND AND WATER PARADOX





DEFINITION

"THE PARADOX OF VALUE (ALSO KNOWN AS THE DIAMOND-WATER PARADOX) IS THE APPARENT CONTRADICTION THAT, ALTHOUGH WATER IS ON THE WHOLE MORE USEFUL, IN TERMS OF SURVIVAL, THAN DIAMONDS, DIAMONDS COMMAND A HIGHER PRICE IN THE MARKET'








HISTORY



- IT WAS FIRST PRESENTED BY THE ECONOMIST ADAM SMITH IN THE 1700S.
- CARL Menger PUBLISHED THE NEW THEORY OF VALUE IN 1871
- IN THE SAME YEAR ENGLISH ECONOMIST WILLIAM STANLEY JEVONS INDEPENDENTLY PUBLISHED SIMILAR THEORY

EXPLANATION

- GETTING ENOUGH WATER TO SUSTAIN LIFE TYPICALLY HAS A LOW PRICE, WHILE A PIECE OF DIAMOND JEWELRY HAS A HIGH PRICE
- WHY DOES AN ECONOMY PUT A MUCH LOWER VALUE ON SOMETHING VITAL TO SUSTAINING LIFE COMPARED TO SOMETHING THAT SIMPLY LOOKS SHINY AND SPARKLES?
- Menger believed that value is completely subjective: A product's value is found in its ability to satisfy human wants.
- THE ACTUAL VALUE DEPENDS ON THE PRODUCT'S UTILITY IN ITS LEAST IMPORTANT USE.
- IF THE PRODUCT EXISTS IN ABUNDANCE, IT WILL BE USED IN LESS-IMPORTANT WAYS.

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- AS THE PRODUCT BECOMES MORE SCARCE, HOWEVER, THE LESS-IMPORTANT USES ARE ABANDONED, AND GREATER UTILITY WILL BE DERIVED FROM THE NEW LEAST-IMPORTANT USE.
 - THIS IDEA RELATES TO ONE OF THE MOST IMPORTANT LAWS IN ECONOMICS, THE LAW OF DEMAND, WHICH SAYS THAT WHEN THE PRICE OF SOMETHING RISES, PEOPLE WILL DEMAND LESS OF IT.)
 - SMITH NOTED THAT, EVEN THOUGH LIFE CANNOT EXIST WITHOUT WATER AND CAN EASILY EXIST WITHOUT DIAMONDS
 - DIAMONDS ARE, POUND FOR POUND, VASTLY MORE VALUABLE THAN WATER
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- WATER IN TOTAL IS MUCH MORE VALUABLE THAN DIAMONDS IN TOTAL BECAUSE THE FIRST FEW UNITS OF WATER ARE NECESSARY FOR LIFE ITSELF
 - BUT, BECAUSE WATER IS PLENTIFUL AND DIAMONDS ARE SCARCE, THE MARGINAL VALUE OF A POUND OF DIAMONDS EXCEEDS THE MARGINAL VALUE OF A POUND OF WATER.
 - AT LOW LEVELS OF CONSUMPTION, WATER HAS A MUCH HIGHER MARGINAL UTILITY THAN DIAMONDS AND THUS IS MORE VALUABLE.

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- PEOPLE USUALLY CONSUME WATER AT MUCH HIGHER LEVELS THAN THEY DO DIAMONDS AND THUS THE MARGINAL UTILITY AND PRICE OF WATER ARE LOWER THAN THAT OF DIAMONDS.
 - IN HIS WORKS, SMITH POINTS OUT THAT PRACTICAL THINGS THAT WE USE EVERY DAY OFTEN HAVE LITTLE OR NO VALUE IN EXCHANGE.
 - ON THE OTHER HAND, THINGS THAT OFTEN HAVE THE GREATEST VALUE IN THE MARKET HAVE LITTLE OR NO PRACTICAL USE

FOR EXAMPLE


- AN OLD PIECE OF ART.
- THERE ISN'T MUCH ELSE WE CAN DO WITH THE ART. SO, WHY ARE THINGS VALUED THIS WAY?
- UNDERSTANDING WHY THE PARADOX EXISTS CAN HELPED BY UNDERSTANDING THE ECONOMIC TERMS KNOWN AS MARGINAL UTILITY AND SCARCITY.

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EXAMPLE OF WATER AND DIAMOND




WATER

- THERE IS PLENTY OF WATER IN MOST PARTS OF THE WORLD, WHICH MEANS THAT, AS CONSUMERS, WE USUALLY HAVE A LOW MARGINAL UTILITY FOR WATER.
 - IN ATYPICAL SITUATION, WE AREN'T WILLING TO PAY A LOT OF MONEY FOR ONE MORE DRINK OF WATER.
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DIAMOND

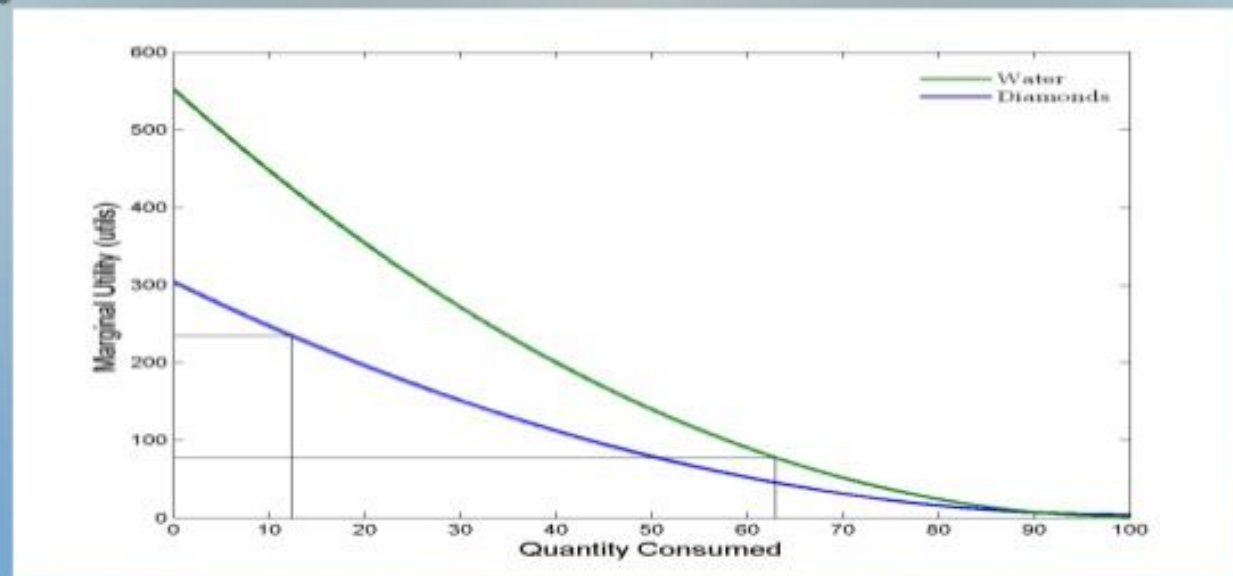
- DIAMONDS, HOWEVER, ARE SCARCE.
 - DIAMONDS ARE HARDER TO FIND AND ATTAIN.
 - OUR MARGINAL UTILITY (ADDITIONAL SATISFACTION), FOR ADDING A DIAMOND TO OUR COLLECTION IS MUCH HIGHER THAN SOMEONE OFFERING US ONE MORE DRINK OF WATER.
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ALTERNATIVE CASE

- IF ONE IS DYING OF THIRST, THEN THIS PARADOX MIGHT NOT MAKE SENSE.
- - THE MARGINAL UTILITY FROM ANOTHER DRINK OF WATER WOULD BE MUCH HIGHER THAN THE ADDITIONAL SATISFACTION OF OWNING A DIAMOND.

The background is a smooth gradient from light purple at the top to light blue at the bottom. In the top-left corner, there are several realistic water droplets of varying sizes, some overlapping. In the bottom-right corner, there are more water droplets, including a large, prominent one and several smaller ones scattered around it.

GRAPH SHOWING WATER-DIAMOND PARADOX



THANK YOU

