The Role of Time Element in the Determination of Price

Importance of time element in the determination of price has been first examined by **Dr. Marshall.** According to him, shorter the time period, greater will be the influence of demand in price determination and longer the period, greater will be the influence of supply on prices.

Marshall, who propounded the theory that price is determined by both demand and supply, also gave a great importance to the time element in the determination of price. Time elements is of great relevance in the theory of value, since one of the two determinants of price, namely supply, and depends on the time allowed to it for adjustment. It is worth mentioning that Marshall divided time into different periods from the viewpoint of supply and not from the viewpoint of demand.

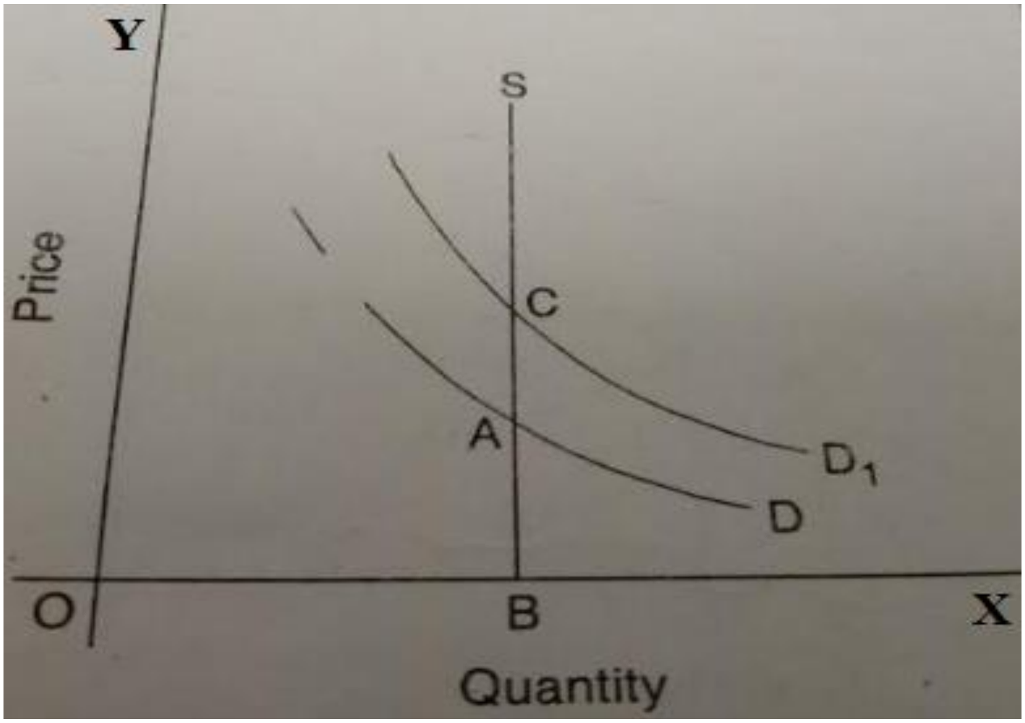
Marshall felt it necessary to divide time into different periods on the basis of response of supply because it always takes time for the supply to adjust fully to the changed conditions of demand.

Marshall divided time into following three periods on the basis of response of supply to a given and permanent change in demand:

(1) Market Period:

The market period is a very short period in which the supply is fixed, that is, no adjustment can take place in supply conditions. In other words, supply in the market period is limited by the existing stock of the good. The maximum that can be supplied in the market period is the stock of the good which has already been produced.

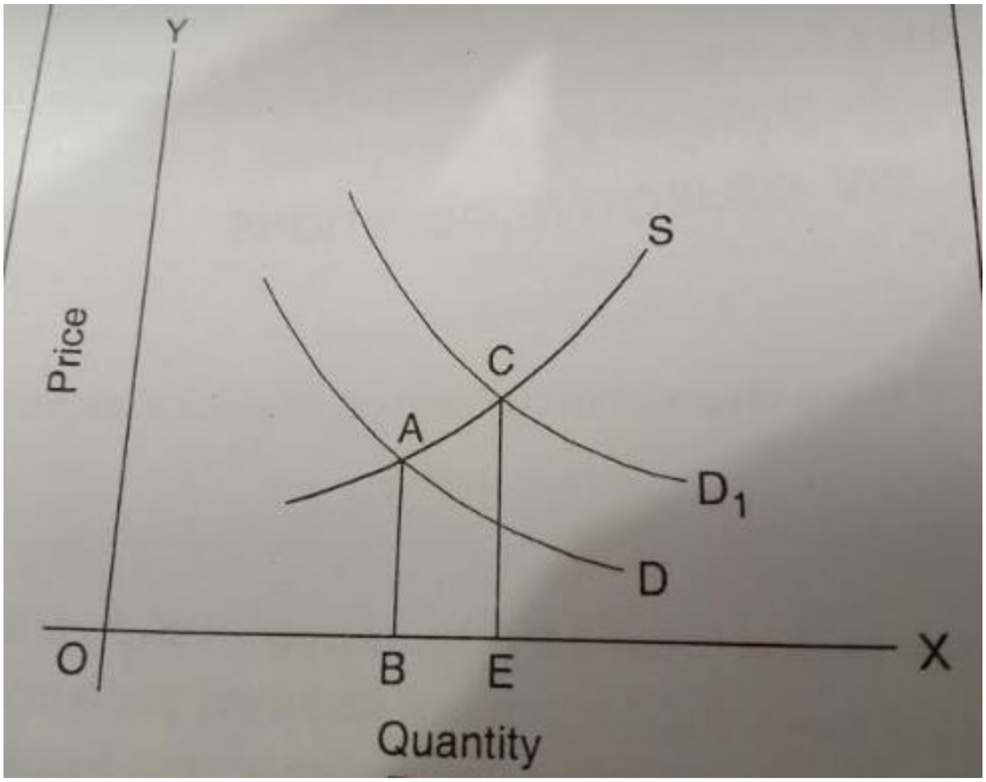
In this period more good cannot be produced in response to an increase in demand. This market period may be a day or a few days or even a few weeks depending upon the nature of the good. For instance, in case of perishable goods, like fish, the market period may be a day and for a cotton cloth, it may be a few weeks. This we understand perfectly with the help of figure-



As shown in figure, price rises from AB to CB. This is due to rise in demand as shown by shift in demand curve. Market price is an extremely short period equilibrium price.

(2) Short Run:

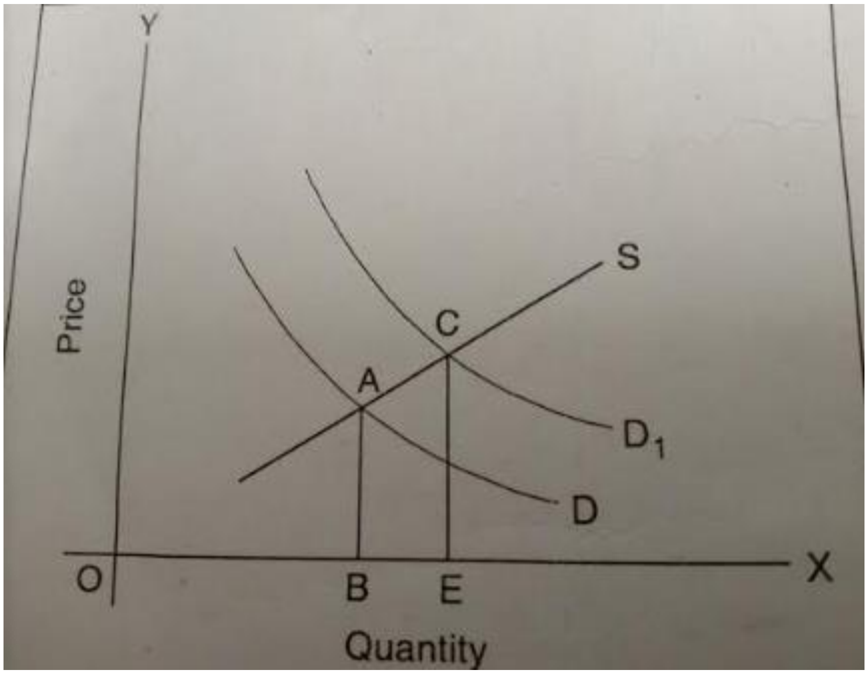
Short run is a period in which supply can be adjusted to a limited extent. During the short period the firms can expand output with given equipment by changing the amounts of variable factors employed. Short periods is not long enough to allow the firm to change the plant or given capital equipment. The plant or capital equipment remains fixed or unaltered in the short run. Output can be expanded by making intensive use of the given plant or capital equipment by varying the amounts of variable factors. Here, supply factor might assume importance but still demand side is predominant. Figure-



As shown in figure, When price rises from AB to CE, but the rise in price is less than before. This is due to adjustment in supply

(3) Long Run:

The long run is a period long enough to permit the firms to build new plants or abandon old ones. Further, in the long run, new firms can enter the industry and old ones can leave it. Since in the long run all factors are subject to variation, none is a fixed factor. During the long period forces of supply fully adjust them to a given change in demand; the size of individual firms as well as the size of the whole industry expands or contracts according to the requirements of demand. During long period, marginal cost of production will influence the price. Here, the supply curve in the long run will have a less. Figure-



As shown in above figure, the supply curve cuts the new demand curve at C, the new price is CE which is higher than price AB but it is not much. This is due to impact on the cost of production in the long run. The long run equilibrium price known as normal price. Market price fluctuate around the normal price. It means that the market price is influenced by changing condition in demand, but tends to settle at level of normal price.