THREE TOPICAL ECONOMIC ISSUES

There are three areas of the economy that are currently the focus of attention. (1) The Federal Reserve and interest rates. (2) Are productivity figures distorted by the changing mix of new use values? (3) Finally does GDP accurately measure economic activity?

Markets are fed up with the FED.

It is an accepted fact that the Fed speaks in strange tongues. If FED members went inside a betting shop they would be thrown out because they would hold up the queue with their hesitant and indecisive hedging of bets. The markets assume that the central bankers should speak directly and accurately about the course of the economy and their intentions. But central bankers are the modern equivalent of Soothe Sayers. And Soothe Sayers since time immemorial, have always spoken in interpretable languages allowing for opposing conclusions and multiple interpretations. Never being right and never being wrong is the way to maintain the grace of your master.

This is not unexpected. Firstly, the FED like any Soothe Sayer does not understand their world especially the economic world. Any extra-ordinary change throws them. Secondly even if they understood the world, they do not know how to correct it. This does not mean central bankers are always wrong. They are just wrong when it really matters.

The Fed is caught in a dilemma. It recognises that bubbles are emerging in the bond market, the stock market and the housing market. These are being pumped up by abnormally low interest rates. This year the bond markets have already returned 20%, the highest in 30 years. Stock Exchanges are up despite S&P profits falling for five quarters and possibly six when this quarter is taken into account. House prices continue to rise above the rate of inflation making them increasingly unaffordable to the majority of Americans.

On the other hand, the overall economy remains weak. Business sales, production and investment in July was still below the level achieved in July, 2015. Not only are durable orders declining, but the sub-prime car loans which buoyed car sales are now increasingly in default. There are other areas of concern as well including productivity that is flat lining, profits that continue to fall as evidenced by the release of Q2 corporate profits. The GDP growth rate has just been revised downwards and is now running at below 1% for the first six months of 2016. It should be revised down even more because it is only being propped up by Personal Consumption Expenditures (PCE). In turn PCEs are being propped up (fictitiously) by rising rents which are inflating imputed rents and increased medical expenditures. Finally, the rise in employment is not supported by the rise in the taxes paid on this employment. Either the jobs are so badly paid they do not attract tax, or they are sub-contracted out, or the employers are dodging tax. Whatever the case, they are not the kinds of jobs that actually boosts the economy.

It is this conundrum that is forcing the FED to try and speak up interest rates without actually intending to so. It has become the toothless barking dog. The FED or at least some of its hawkish members hope their warnings of rate rises will moderate behaviour in the markets. Fundamentally the FED knows the US economy cannot sustain higher interest rates and with it a higher dollar.

Despite some FED officials saying that economic conditions are improving, if anything they are deteriorating fundamentally. Underlying profitability is declining especially if adjusted for GAAP. Profitability is not only being undermined by rising labour costs in the USA, but the USA no longer commands the lion's share of the surplus value produced by the international value chain. This is primarily due to China moving up the value chain. This is exemplified by the headwinds facing Apple as Chinese Producers bring out comparable smartphones. The US has run out of time. The fall in corporate profits in the second quarter is testimony to this. This quarter will mark two years since the US economy reached peak profitability. It will mark two years wherein the rate of surplus value has fallen and with it the rate of profit. Ever lower interest rates can only delay not reverse the pending economic crisis.

Productivity and the product mix.

Productivity can be measured in one of two ways. The physical output per worker and secondly the value output per worker. Of the two, the latter is the more important. Profits are not measured by physical output; they are measured by value output.

However, the matter is more complicated and the inter-relationship between the two indicators is much more obscure. If we were to assume that the value of money is held constant, then it is possible that the physical output of workers can go up without the value output going up. If the same number of workers work the same number of hours producing five percent more commodities of the same kind and quality, we can assume their productivity has gone up 5%. But if at the same time the prices of these commodities falls by 5% then their value output would be unaltered. Measured monetarily it now appears their productivity has not changed as the value per worker is unchanged.

Capitalism has a very real problem calculating productivity. The only accurate way to capture whether or not productivity has risen is through falling prices. But this requires money being held constant which is an impossibility under capitalism. The statisticians try and get around this by using deflators. If inflation is judged to be 3% and value output has gone up by 5%, then real output they conclude has gone up by 2%. Here the productivity increase is judged to be 2%. But why should the deflator merely reset price rises back to 0% when in fact prices should be falling in line with the fall in actual costs of production – labour time. Hence capitalism always underestimates the actual increase in real productivity because it seeks to reset prices to 0%.

This failure to measure prices accurately is magnified by changes in market conditions. When prices are constrained by insufficient demand, and this is generalised, then productivity will appear to fall when that may not be the case. What occurs now is a problem of realisation. Some of the value produced by workers is lost altogether. Commodities may contain the same labour time but not all of that labour time is turned into money. So the gap between value production and physical production increases and this cannot be compensated for by deflators. The converse is the case as well. In the latter stages of the business cycle, the boom phase, when production has built up its own momentum and prices are rising, the monetary increase in productivity begins to outpace the physical increase.

Only a socialist society can measure productivity accurately because money is now invariable. If the same number of hours produce 4% more product, then the volume of prices will not rise from 100% to 104%, but remain at 100%. But this constant price volume when divided by a product whose physical volume has grown by 4%, means individual prices on average will have fallen 4%. This price fall is the direct measure of productivity. If the number of hours increases by 10% to 110% and productivity by 4% then the volume of production will rise to 114.4 while the volume of prices will rise to only 109.8 yielding the 4% rise in productivity.

Falling prices is the economic incentive and motive force of a society based on collective production. It replaces the profit motive of capitalism. But falling prices under socialism is so much more. Its fall expresses the rise in productivity. Its fall expresses the efficiency of investment. Prices in all its aspects, now paves the way for the conscious planning of production.

The final question is the predicament thrown up by the neo-Ricardian infatuation with the physical properties of commodities rather than their social properties. This year's 50inch flat screen television may be different to last year's similarly sized flat screen. This year, Dolby Sound has become the norm and is enforced by competition. Last year it was absent. In terms of usability, this year's TV sounds better than last year so it should cost more. Rubbish. If the cost of the other components that enter into the production of the TV fall by more than the additional cost of Dolby, the TV will be less valuable, especially if its assembly time falls as well.

Or take computers. According to Intel, processing speeds currently double every 2.5 years. Accordingly, today's computers on average are twice as powerful as ones produced in 2013. Does this mean that today's computer should be counted as 2x a 2013 model? Not at all. It may actually cost 10% less to produce a 2016 model than the 2013 model it replaced. In that case, measured by use value it is 2x, but measured by the more important exchange value it is 0.9x. The fact that any remaining 2013 models left unsold will see their prices tumble due to their lower speeds does not support the neo-Ricardian view.

Productivity here is measured in two distinct ways. As far as the productivity increase relating to the actual computer goes, this depends on the labour time socially necessary to produce a 2016 computer versus a 2013 computer. It is likely less labour time is expended on a 2016 computer than a 2013 computer despite the faster processing speed. So the productivity of the workers producing the computer resides in the price of the computer. Secondly, the productivity of those operating the computer in a commercial setting is enhanced. They can now complete tasks faster because their computer is faster. Hence the actual cost of producing these tasks is reduced because they are produced more speedily. Therefore, it is only when the productivity of the producer of a piece of equipment and the productivity of the user of this piece of equipment is aggregated, that productivity in the round is measured. The mere fact that the computer is now twice as powerful is of itself, only a matter of technical interest. It only becomes actual when it is used by the operator and its effect on their labour time can be measured.

Hence those who claim that the increase in the specifications of products separated by time make them incommensurable, miss the point. The increase in specification is important, but only in so far as competition forces independent producers to adopt these specs. What is really important is how these specs affect labour time. If the adoption of these specs increases the actual cost of production then the price of the computer will rise, but if, despite the higher spec, production costs have fallen, then that computer could be cheaper than the less powerful one it replaces. The new computer will appear more expensive than the previous computer only because the market price of the earlier model is discounted because of its now lower spec and not because the new computer has risen in price.

GDP remains the best measure of exchange value.

The slowdown in the world economy has predictably led the less able commenters to query whether or not the world economy is being measured accurately. They feel that GDP cannot cope with the growth of immaterial production and the knowledge based economy. Frustrated by a car that is failing to gather speed they want to tamper with the speedometer rather than fix the car.

GDP is derived from the second volume of Das Kapital, and was transported to the West by two emigres who left Stalin's Russia. The basis of the modern system of national accounts, the input-output tables were first used by Marx, the method for not duplicating value is his, and so too are the three great presentations of GDP; value added (income side), expenditure side and production side.

GDP has two major failings. It cannot capture all the labour expended by society because not all labour becomes social, it is not turned into the exchange value which GDP measures. The largest component of this is domestic labour which is unpaid private labour performed within the confines of the home. Its second failing is that it breaks Marx's injunction against the double counting of exchange value. Statiticians turn the mere exchange of money into value creation, or they impute (create) sales where no sale occurs and finally they turn intermediate sales into final sales. Duplicated value amounts to over 25% of the economy. So on the one hand GDP undercounts the expenditure of labour and on the other it overcounts it.

But this is not what the critics of GDP point to. What they point to is the change in use values and the increase in their quantity which GDP apparently does not pick up. They point to music streaming for example compared to the older CDs. The amount of music downloads exceeds the number of CDs sold by many factors of numbers. And yet the revenue of the music industry has actually gone down. This is not surprising. Setting aside artist royalties, the cost of streaming is but a hundredth the cost of a CD. To produce a CD, oil must be mined, then converted into plastic, the plastic must then be stamped into a CD blank on the one side and a case on the other, the CD is then "pressed" before being coated while the case is printed, whereupon both are placed into a box, stored, transported, displayed in a shop before being sold. Streaming on the other hand is much simpler and quicker. The music is recorded, sent via the internet to a provider who sells it on to the final consumer to download. Human intervention is minimal due to the level of computerisation. So instead of oil, plastic, coatings, cardboard, ink, petrol for transport, rent for retail etc. etc. being used to produce CDs a series of electronic ones and zeros is sent down fibre optic and copper cables to the final consumer of the music.

This cheapening of production should lead to a lower GDP not a higher GDP. As a result of the death of the CD less oil needs to be mined, less plastic, card, ink, petrol, bricks and mortar is produced. This reality is captured by GDP which falls as the value added by the aforementioned industries shrink. Everything is in order contrary to the neo-Ricardians who dominate academia and economics. Their foolish assumption that GDP should rise merely because volumes of replacement products rises is just that, foolish, because GDP measures exchange value and not use values which are quite distinct. Therefore, in inverse relation to the technical conquests of capitalism stands the intellectual accomplishments of its economic professors.