HOW THE RISE IN INEQUALITY CAN HAVE A DEPRESSIVE INFLUENCE ON THE RATE OF PROFIT.

The above appears to be an oxymoron. Scientific enquiries however often begin with apparent contradictions. But that is the beauty of science. What a boring old world it would be if essence and form always coincided, and if all of life was spontaneously transparent.

The rise in inequality is the relative rise in undivided profits, or the income of capital, versus the relative fall in wages, or the income of labour. It therefore follows, everything else being equal, that a rise in the mass of profits should be associated with a rise in profits. But all is not that simple in the realm of the System of National Accounts.

Our starting point is that rising inequality is usually associated with the growth in servants both personal and professional. It's not only about mansions, it's about staffing them, it's not only about wealth hoards, it's about the accountants, lawyers and financiers needed to manage them. As Marxists we recognise four kinds of labour. Productive labour which is the source of profits. Functional unproductive labour which manages, accounts for and circulates value. Personal unproductive labour which supervises workers and provides the services the rich require to make their lives bearable. Finally, domestic labour which does not concern us here.

I am always surprised at Marxists who are really hot on the distinction between productive and unproductive workers, but who are oblivious to the distinction between the two forms of unproductive labour, and therefore to the enormous growth in the latter. In the mind of the reader, a picture may be forming. If there has been an explosion in personal unproductive labour, then economy wide, outside the corporate sphere, there must have been a rapid growth in wages. After all these workers like all others sell their labour power and intimate powers to their employers.

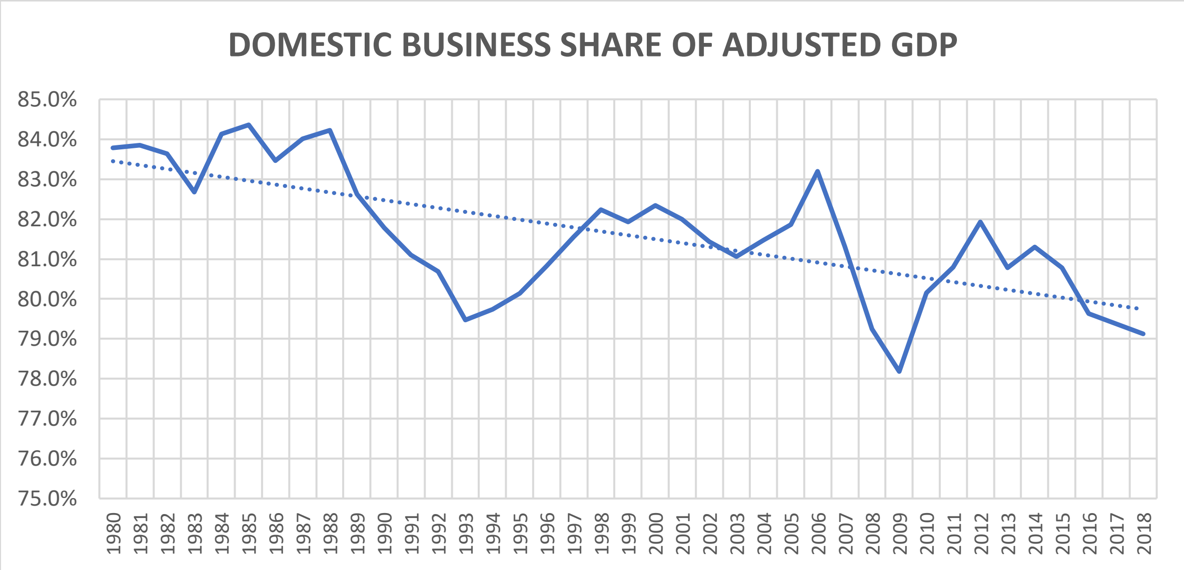
And if there has been a growth in economy wide wages because of the explosion in the wages of servants, then the deduction of these additional wages from value added will yield a smaller surplus and consequently it will reduce the rate of profit because of its depressive effect on the economy wide net surplus. This is exactly the error that Michael Roberts and the Penn statisticians fall into. Read https://wordpress.com/read/feeds/313842/posts/2826304903 A World Rate of Profit: a New Approach by Michael Roberts.

The growth of the household and non-profit sector of the economy.

Attached the reader will find the spreadsheet "Table 1.13 Graphs". It analyses "National Income by Sector, Legal Form of Organization, and Type of Income". I find this Table to be one of the most enlightening ones produced by the BEA. Using this Table, I have isolated the growth of the "household and non-profit sector" of the economy. This is the sector of the economy that is value consuming not value producing. Only one of the two exchanges that forms the capitalist social relation is found here, or M.C…P. This does not stop the BEA describing this sector as an industry. So for example under non-profit, we find the religious industry, truly, how delightful, god is not love but enterprise.

The question is, has this overall sector grown since the acceleration in inequality? The first graph below provides the answer.

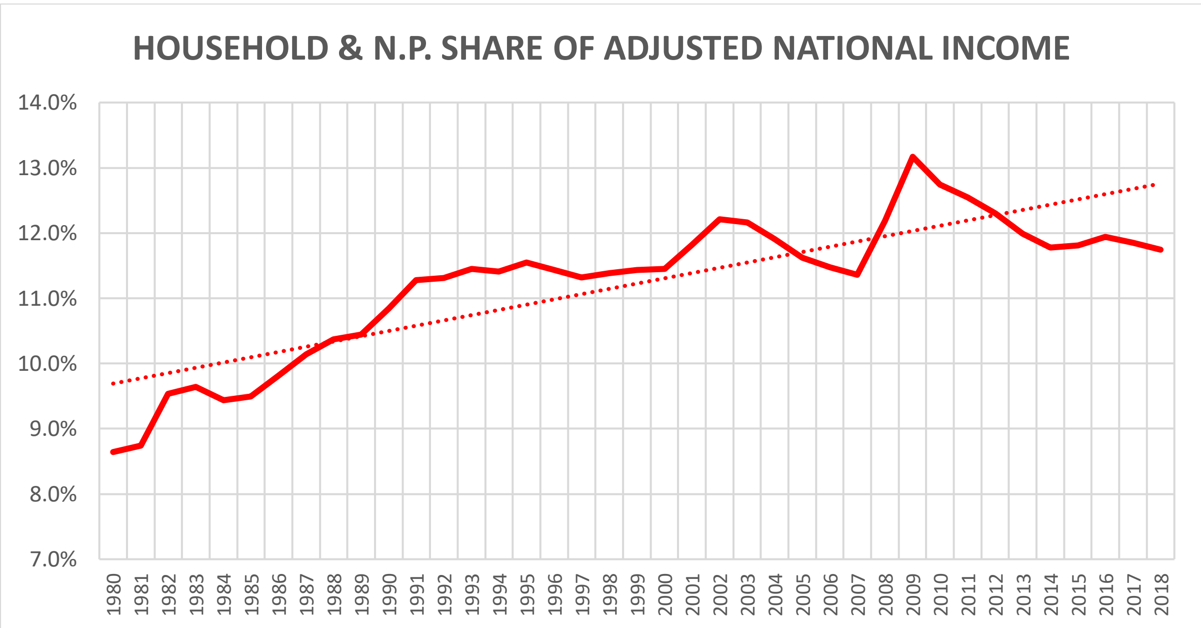
Graph 1.



Yes, it has. Table 1.13 can be divided into three parts. Domestic Industry, Household & Non-Profit and Government. The graph above deducts the government sector from GDP hence the designation adjusted GDP, (Private Industry GDP). Most of the government's expenditure is based on circulating value, tax revenue in, services and disbursements out. Generally, Domestic Industry is where value production takes place and it comprises corporate business as well as non-corporate business.

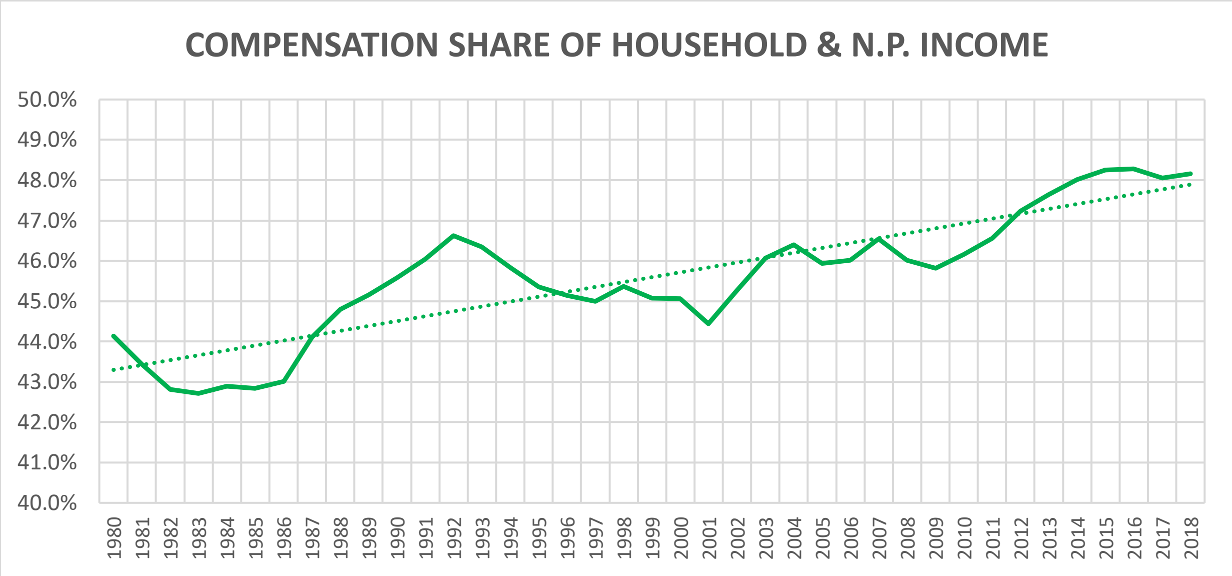
We note that within the period 1980 to 2018 (the most recent figure) this sector of the economy has fallen by 4% of national income. This is consistent with the growth of inequality which has boosted household spending. This is better seen in the graph below.

Graph 2.



Not only has the household and non-profit sector grown as a share of adjusted GDP, but within this sector so too has compensation. All those gardeners, decorators, chauffeurs, pilots, personal assistants, physical trainers, entertainment organisers; dammit being rich is an expensive business.

Graph 3.

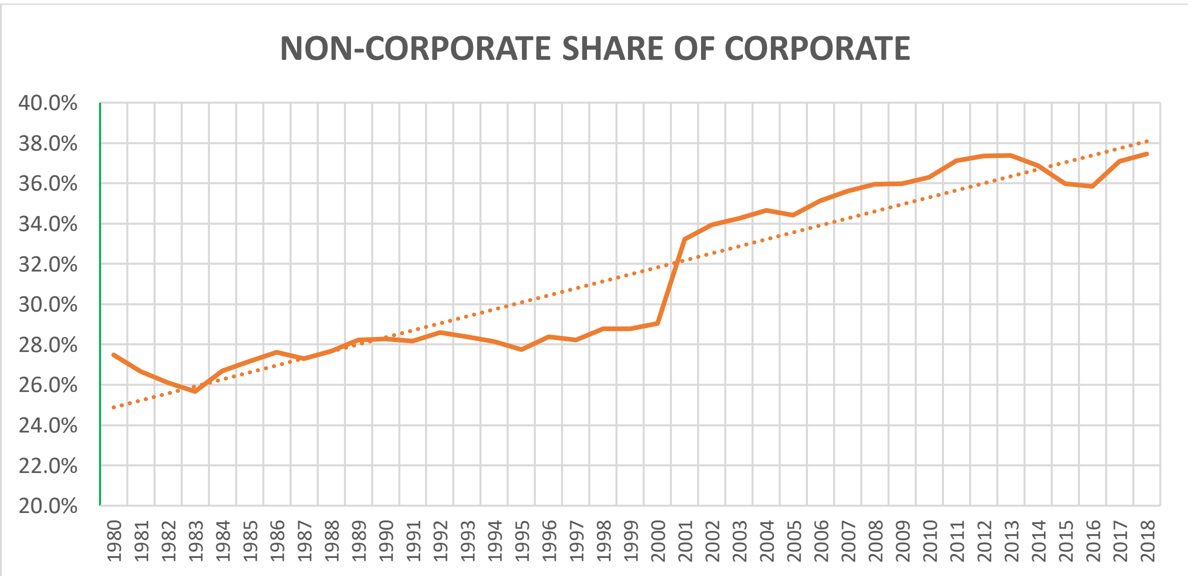


The relative growth of the non-corporate business sector.

But the changes in the household and non-profit sector is not confined to the household & non-profit sector, it has also shaped the non-corporate business sector. We would expect that with the rise in inequality and its bastard child, speculation, that the non-corporate sector would have grown disproportionately, and it has. In this sector are located many of the professional personal servants that have profited from the rise in inequality. From Hedge Funds through to accountancy firms through to legal firms many of whom are partnerships, to landscape gardeners, security services and so on. (Unfortunately, the BEA does not provide a division between partnerships and sole proprietors.) And here sadly are also to be found the millions of self-exploited, oops self-employed, many of whom are refugees from the world of salaried employment.

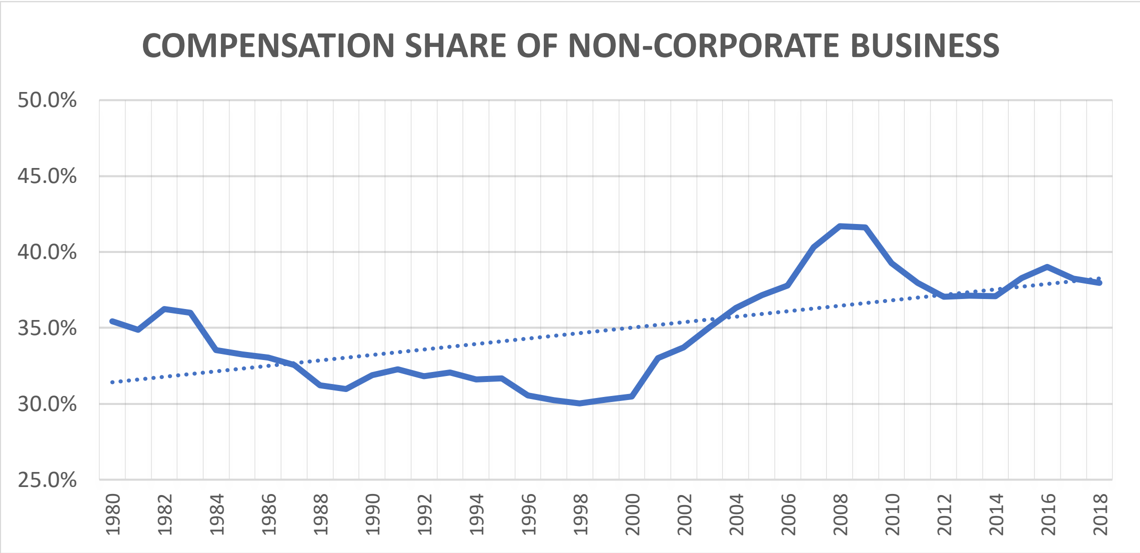
Our fourth exhibit or graph below shows the relative expansion of the non-corporate world.

Graph 4.



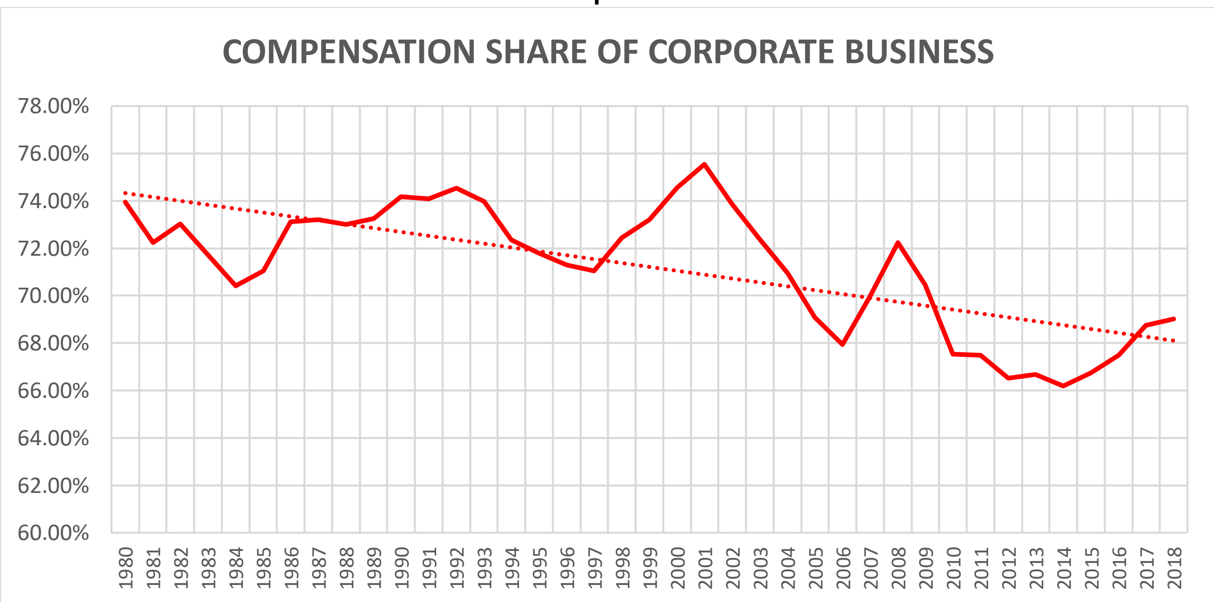
Non-corporate's share has grown by half from under 26% to just under 38%. The changing shares are quite significant and some of it is due to financialization which serves the rich. But not only that. Professional services and financial croupiers is a labour-intensive affair. So exhibit five should show a structural change within non-corporate with evidence that the share of compensation has grown.

Graph 5.



This is a graph of two parts. First compensation falls in the period up to 2000, then it rises by over 10%. This rise of 10% has played an important role in depressing the whole economy rate of profit this century. Not only has the share of compensation grown but it has done so within a growing non-corporate sector. And this compensation trajectory is the opposite to that found in the corporate sector. This corporate compensation trajectory is closer to the expected trajectory most observers would anticipate.

Graph 5.



Conclusion.

This posting is but a rough sketch of the structural changes that have taken place in the US economy since Raygun. It does not pretend to be a forensic investigation of these changes. Rather it has set itself one task, to show, how via duplication, wages have expanded because of the growth of personal services.

Why duplication? Imagine a situation. Mr Smith of Smith and Son, a venerable and long-established firm, spends some of his profits buying a shirt. The sale of this shirt is logged in the retail sector of the economy by the BEA, and adds to its size. One of his male-servants, a Mr Butler, is over-impressed by the shirt as is he with his boss. So unbeknown to Mr Smith he buys an identical shirt to impress his friends off property. Again, this sale is logged in the retail sector.

But there is a difference. Mr Butler has paid for his shirt with the wage that Mr Smith has paid him, a wage payment which has boosted national income because it has boosted the household sector. Thus, this wage has a different effect on National Income and GDP to the wage paid to the functional unproductive worker who is intricately involved in the metabolism of capitalism. The functional unproductive worker, whether they are employed in accounts, administration, buying, sales or marketing, are paid a wage that appears on the Loss side of the Profit and Loss Account of the Firm. Their wage is treated as an expense and it results in a loss of profits. There is thus no duplication.

The opposite is the case with personal unproductive wages. Their wages are paid outside the realm of production and circulation. They are paid out of revenue. Their wages do not reduce the amount of profits logged by the BEA, but it does add to the mass of recorded wages. Hence the duplication. Here there is no plus followed by a minus, simply a plus. In fact, all that has happened is that Mr Smith has converted part of his profit into a wage leaving his original profit unaltered.

No new value has been created, only money has changed hands. A simple example will suffice. Originally total undivided profit equalled $1 trillion and total wages equalled $1 trillion. National Income therefore amounted to $2 trillion. This ratio of profits to wages yielded a rate of exploitation of 100%. Now if we add in $100 billion of new personal wages, the following holds true. Profit remains at $1 trillion but wages have risen to $1.1 trillion. National income is now $2.1 trillion and the rate of exploitation has fallen to 91% or $1 trillion divided by $1.1 trillion.

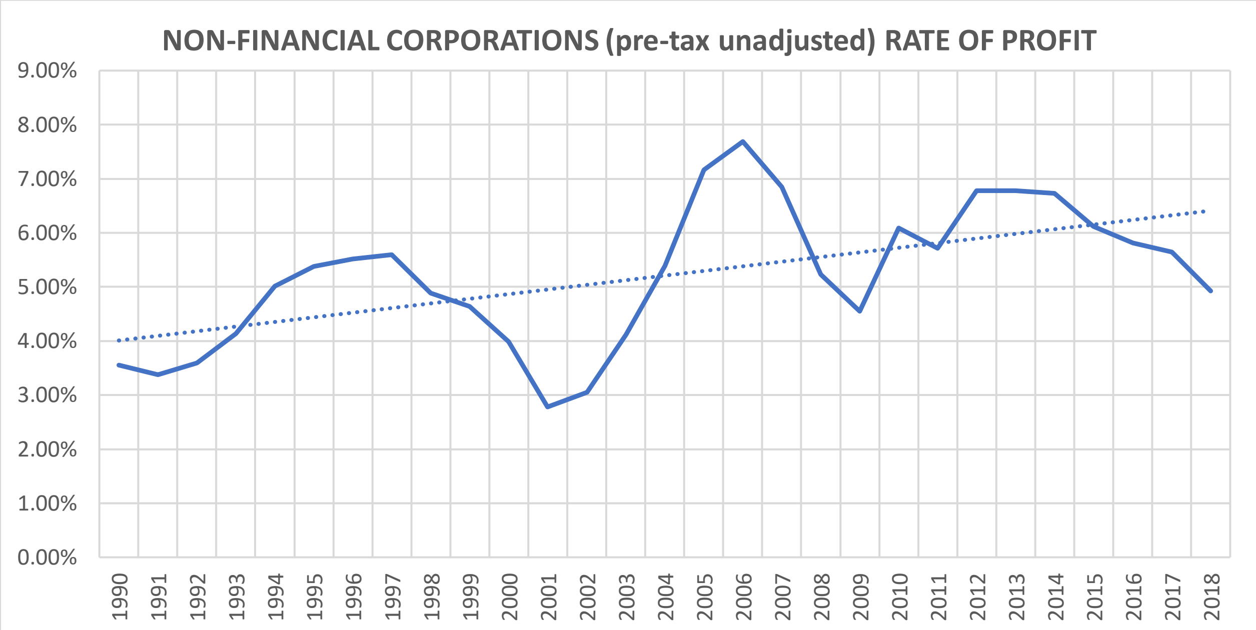
I believe the evidence is convincing, the inflation in personal wages has depressed profitability when viewed across the economy through the prism of the SNA. I have cautioned repeatedly that the biggest sector that can be mapped, the sector where value production dominates, and where duplication is tolerable, is the corporate sector. That is why I have rejected Michael Roberts approach.

The final exhibit compares the rate of profit found in the non-financial corporate sector with the rate of profit found in the whole economy minus government, what is called Total Private Industry. In both cases the same methodology is used. I apologise that the periods do not match, but since the 2012 revisions, the data used here to calculate Total Private Industry extends back only to 1997 as can be seen in the attached spreadsheet: “Whole Economy Rate of Profit”.

Before proceeding it is important to note that it is the enterprise rate of profit which determines the rhythm of investment not the economy wide rate. The enterprise rate of profit is non-financial pre-tax corporate profits divided by fixed and circulating capital. If it is true that personal wages amongst other things found outside the corporate world distorts the rate of profit, the two rates should diverge.

We begin with the enterprise rate of profit (Graph 6). I would argue it truly captures the nature of the period. It bears witness to the acceleration in globalisation, to the incredible rise of China and the US’s monopolisation of the commanding heights of the global value chain. It describes the rise of Cisco, Microsoft, Intel and especially Apple which once enjoyed 90% of global smartphone profits. All reflected by the rising rate of profit up to 2014.

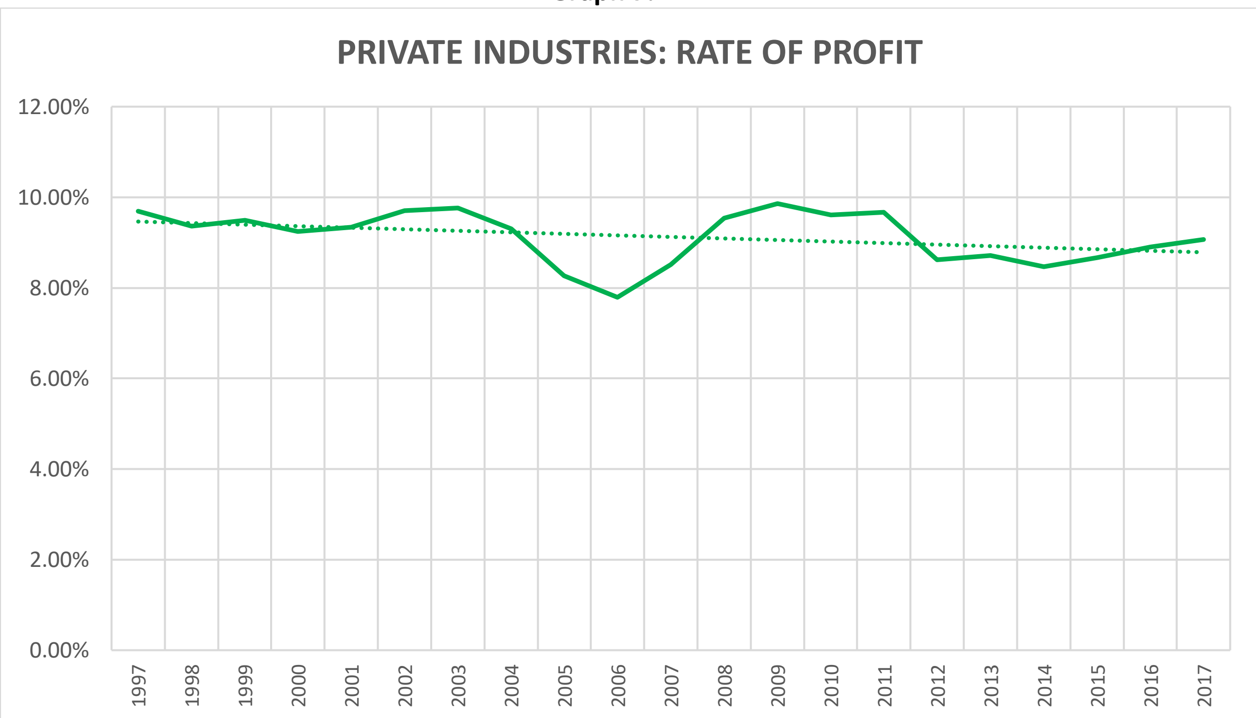
Graph 6.



And we also see the unrelenting fall in the rate of profit after 2014, signifying the exhaustion of the period of globalisation, and whose fall has accelerated to this day to the lowest point since the end of the War. It is this enduring fall in the rate of profit that is the driver of the conflict between China and the USA, because this fall not only constricts the USA, but China and the rest of the world.

And yet when we view the economy wide rate of profit based on the same methodology, we get a different picture. There is no fall in the rate of profit after 1997. There is no rise in the rate of profit up to 2006. And most important of all, instead of falling after 2014, the rate rises. Could this be the same economy being described by Graph 6?

Graph 7.



Graph 7 is closer to the Graphs drawn up by Michael Roberts which shows a fall in the rate of profit post-2008 and from which he draws his conclusions.

Capitalism is a chameleon. It changes its spots and hues over time. But this can only be seen with the complexity of colour, it cannot be appreciated in simple black and white. If we are to do justice to our analysis, we cannot use the same measure without accounting for the changes in that which is being measured. Using the all-economy wide rate of profit as a constant and fixed measure, turns us into Inspector Plod who misses all the clues.

Traversing the system of national accounts needs some insight. Otherwise it lays traps for the unwary. However, once we understand the duplications, or how to locate the final sales which have been substituted for intermediate sales, or how to adjust for imputed sales, then the SNA becomes a valuable to tool for analysing the health of the capitalist economy and plotting its trajectory.

The capitalists may admire their physical assets, but they always measure their wealth financially. They base their decisions on financial calculation and no other. Their finances are the result of value production and that alone. That is why GDP is the only way to measure the wealth of a capitalist society, for in the end, despite all its shortcomings, GDP is merely the sum total of the value produced in a given year by the army of productive workers whose product takes the form of exchange value.

Brian Green, 29th July 2020.