

Surplus value and the rate of profit

Nick Beams

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Dear Mr. Beams,

If I am understanding your argument correctly, business profits are derived from the fact that the worker is only paid for a fraction of his working day, more or less as follows below:

Let's describe the process for producing a widget that costs \$1,000 to produce but sells for \$1,200, rendering the capitalist a profit of \$200 per widget. At the start of the widget production process, the capitalist has a sum of money, \$1,000 available to him to facilitate production of the widget. That money is expended to procure the material factors of production, capital and raw materials. Let's say \$800 is expended for such "dead labour" commodities.

Now the capitalist employs a worker who will work for him for eight hours to produce the widget but who reproduces the value of his labour in, let's say four hours. The capitalist pays the worker \$25 per hour, or \$200 for the worker's eight hours of work. Now we have accounted for the full \$1,000 of money capital (as stated above) which is being put to work in our production process. Our capitalist has spent \$800 for dead labour and \$200 for living labour (living labour that actually adds \$400 of value each working day).

Now let's say that the commodity produced in this process, the widget, sells not for \$1,000 but for \$1,200, which accounts for an extra \$200 profit, above and beyond the original \$1,000 money outlay by the capitalist. This \$200 represents pay for the four hours of the day after the worker has already reproduced the value of his own labour and is now working only for the capitalist, rendering surplus value to the capitalist just as surely as if he were his slave or serf for those last four hours of the day. If it were not so, and no surplus value was pumped out of the worker in the widget production process, the capitalist would not be in a position to earn a profit on his widget enterprise.

I think when you look at the above situation you see an immediate problem. Business firms differ greatly in their degree of labour intensiveness. \$1,000 spent on one product may result in \$800 (80 percent) being spent on living labour in one production process, but the same \$1,000 spent on a more "capital intensive" commodity may result in only \$50 being spent on living labour (5 percent). Therefore, if as Marxists say, that surplus value is always extracted at the point in the economy where living labour is set in motion, it would seem that those points in the economy where living labour is most lavishly employed (the most labour intensive industries) would also be the points of the greatest extraction of surplus value, of profit, true?

Now our every day experience contradicts this because it is obvious that the rate of profit tends to settle to a specific and uniform "rate of return" across every branch of capital, regardless of whether each branch is more or less labour intensive. Profits are expressed as a percentage rate of return (say 10 percent) and that percentage is calculated by dividing the annual profit by the amount of capital in use (notwithstanding whether more or less or even no "living" labour is used in the production process).

Indeed, it is possible to imagine a production process so capital intensive that NO living labour whatsoever is needed—a completely automated process—such as an automatic carwash that has no service attendant at all (and let's ignore the need for repairs and maintenance for simplicity's

sake by saying that these expenses are covered by a separate "service charge" added to the price of each car wash). In that case we would need to assume that any profit made by such an enterprise could only come from taking the surplus value away from other sections of capital. Indeed, this is exactly what Marxists do say about rent, because they can see that money must be expended for the use of land, but land, unlike capital, cannot be said to contain any "dead labour" whatsoever, therefore the Marxist explains the payment of rent as a deduction from the surplus value in those firms that actually employ living labour, and which therefore directly "pump" this surplus value from the worker.

Now Marxists claim that the only point where surplus value can be pumped from the proletariat is at the point where living labour is employed. However, the actual "appearance" of the extracted surplus value—or the point in the economy where surplus value first makes its appearance in a financial form—seems to depend on the amount of capital employed in the firm, without regard to the amount of living labour employed.

Specifically, what is the mechanism by which capitalism takes the surplus value extracted in one department of production (more labour intensive) and transports it to the profit and loss statement of another department of production (more capital intensive)? If the profit (or "surplus value") is pumped from the worker in the labour intensive production process of Firm A, then how does this surplus value migrate, to appear on the income statement of the more capital intensive Firm B, or on the income statement of the landlord?

I don't know if my question is sufficiently clear, by I am hoping you can shed some light on this for me.

Sincerely,

MM

Dear MM,

As you draw out in your e-mail, there is a contradiction between the determination of the value of a commodity by labour time and the observable fact that profit rates across all industries, whether they are capital or labour intensive, tend to the same level.

This contradiction can be stated as follows. If the market price of a commodity is determined directly by its value (that is, by the socially necessary labour it embodies) then the rate of profit will vary across different industries—higher if they are more labour intensive, lower if they are more capital intensive. This means there is no average rate of profit, to which every industry tends—a result that contradicts one of the most clearly observable tendencies within capitalism.

On the other hand, if the rate of profit in each industry tends towards the same average level, then how can the prices of commodities be determined by value? Clearly those that are more labour intensive will sell below their value, while those that are more capital intensive will sell above their value.

This contradiction had been a major concern for the two central figures of classical political economy—Adam Smith and David Ricardo. Smith maintained that the law of value was applicable in a simple commodity-producing society but not in capitalism. Here value was determined on a cost plus basis, meaning that if wages went up then the value of the

commodity would also rise. Ricardo insisted from the outset that: “The value of a commodity ... depends on the relative quantity of labour which is necessary for its production, and not on the greater or less compensation which is paid for that labour.”

Ricardo represents a considerable advance over Smith for he clearly points to the origin of surplus value. He insists that an increase in wages does not bring a rise in the value of the commodity but rather a diminution of profit. But Ricardo was not able to explain the existence of an average rate of profit on the basis of the labour theory of value.

The contradiction was only resolved when Marx developed his theory of prices of production. In Volume I of *Capital*, Marx, starting with the cell-form of capitalist society, the commodity, derives the theory of value and discloses the origin of surplus value in the sale of labour power (capacity to work) by the worker to the owner of capital. Surplus value arises from the fact that the value of labour power (determined by the amount of socially necessary labour needed to feed, clothe and house the worker) is an altogether different magnitude from the value which is added by the expenditure of this labour power in the course of a working day.

In Volume III of *Capital*, Marx sets out the resolution of the contradiction between the determination of value by labour time and the existence of an average rate of profit. He explains that the prices of commodities in the market will fluctuate not around their values but around their “prices of production”. These prices of production are such that each section of capital (whatever its composition) will return profit at the average rate. This average rate is determined by the ratio of the surplus value extracted from the working class as a whole to the mass of capital in society as a whole. Each section of capital will receive surplus value, in the form of profit, in proportion to its share of the total capital in society. “So far as profits are concerned,” Marx writes, “the various capitalists are just so many stockholders in a stock company in which the shares of profit are uniformly divided per 100, so that profits differ in the case of the individual capitalists only in accordance with the amount of capital invested by each in the aggregate enterprise, i.e., according to his investment in social production as a whole, according to the number of his shares” [Marx, *Capital Volume III*, p. 156].

In other words, the average rate of profit is determined by value relations, according to the analysis of Volume I operating not at the level of the individual firm but of society as a whole. The price of the individual commodity will no longer fluctuate around its individual value, but its price of production—that is, the price which brings profit at the average rate to the section of capital that produced it.

On the basis of this analysis, Marx explains how competition, the struggle between different sections of capital, gives effect to these economic laws. If the price of a commodity is consistently above its price of production, giving the capital in that industry a rate of profit higher than the average rate, then capital will move into that industry, increasing the supply of commodities and reducing the price in the market until profit falls to the average rate. In the same way, if the profit rate in a particular industry is below the average, then capital will leave that industry, leading to a reduction in supply and bringing an increase in the price of the commodity until the average rate of profit is reached.

This is the social process by which the mass of surplus value extracted from the working class as a whole is distributed among the different sections of capital. In the first case, a particular section of capital was receiving more than its share of the available surplus value. The migration of capital to that industry, forcing down the price of commodities, ensured that profit rates were restored to the average rate. In the second case, where capital was receiving less than its share, the exit of capital restored profits to the average rate.

Marx’s theory reveals the origin of rent. The equalisation of profits—the distribution of surplus value among the different sections of capital—is effected through the continuous movement of capital, into areas of higher

profit, out of areas of lower profit and so on. However, if there are barriers preventing the entry of capital into a particular sphere of production, such as the ownership of land, or the ownership of copyrights on particular processes of production, the price of the commodity in the market will remain above the “price of production.” This means that capital in that particular sector will enjoy “super profits” or that the owner of a particular resource, say land, will be able to receive a rent while the capital employed in that industry still receives profit at the average rate.

Like all great scientific advances, Marx’s theory of the prices of production, not only resolves previous theoretical problems but also lays bare the source of continuing errors, especially those concerning the origin of surplus value.

Because there is no necessary correlation between the extraction of surplus value in a particular industry and the profit accruing to that section of capital (a highly labour intensive industry will enjoy the same rate of profit as a high capital intensive industry, or a completely automated one) it appears that there is no relation between the exploitation of labour and the accumulation of profit. In fact, profit appears to arise not from labour but from capital because a given amount of capital will yield profit. And because the ownership of land brings rent, this further conceals the origin of surplus value. These illusions assume their most fantastic form in the financial markets where it appears that money simply begets money.

Marx makes the point that not only is the “true nature and origin of profit” concealed from the capitalist “who has a special interest in deceiving himself on this score, but also the labourer” [Marx, *Capital Volume III*, pp. 165-166].

The competitive struggle between different sections of capital in the market actually conceals the underlying process. Viewed from the standpoint of the market, average profits are independent of the amount of labour employed, prices of production are determined by the rise and fall of wages, market prices fluctuate not around values but prices which diverge from value.

“All these phenomena,” Marx writes, “*seem* to contradict the determination of value by labour-time as much as the nature of surplus-value consisting of unpaid surplus-labour. *Thus everything appears reversed in competition.* The final pattern of economic relations seen on the surface, in their real existence and consequently in the conceptions by which the bearers and agents of these relations seek to understand then, is very much different from, and indeed quite the reverse of, their inner but concealed essential pattern and the conception corresponding to it” [Marx, *Capital Volume III*, p. 205].



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