Surplus Value

ANWAR SHAIKH

Profitability regulates the health of capitalist society. In this regard, Marx identifies two distinct sources of profit: profit on transfer (or even forcible appropriation) of wealth, which dominates the Mercantilist period; and profit on production of surplus value, which comes into prominence under Industrial Capital. Since trading activities can be linked to either source of profit, it is useful to begin with trading profits.

Individual trading profit arises whenever a commodity is re-sold at a profit. To the merchant who acquires a commodity of £100 and resells it for £200, it is his entrepeneurial ability to 'buy cheap and sell dear' which determines his gain (which covers trading costs and profit). But from the perspective of the system as a whole, the chain of transactions from initial to final sale simply serves to share out the total selling price among the various transactors, including the merchant. This holds true whether or not the transactions are fair or unfair, free or forced.

The merchant's gain is his 'balance of trade surplus'. But it is crucial to distinguish between a situation in which the overall 'balance of trade' is zero because the merchant's surplus is offset by a corresponding deficit somewhere else in the chain; and one in which the total balance is positive because the merchant's gain is merely his particular share in some overall surplus whose ***origin therefore lies outside of trading activities themselves.*** The former case corresponds to profit on the transfer of wealth, and the latter to profit on the production of surplus value. We will consider each in turn.

PROFIT ON TRANSFER OF WEALTH. A system-wide profit on the transfer of wealth appears mysterious because the surplus of the merchant does not seem to be counterbalanced by any corresponding deficit. Suppose merchant capitalists barter goods costing them £100 for those of a non-capitalist community or tribe,

which they then resell for £200. This swap leaves the combined wealth of the participants unchanged. Yet it gives rise to a profit on the capitalist side without any corresponding loss on the non-capitalist side, so that a net profit appears *for the system as a whole.* How is that possible?

The tribe's participation in trade may be motivated by fear. by ceremonial considerations, or by the hope of gaining objects which are socially more desirable. In all cases, it is a social assessment which stands behind the trade. But for the merchants, the important thing is that the tribal objects they acquire can be resold for a monetary gain. In Marx's terminology, the tribe is operating within the simple commodity circuit CC', in which one set of use-values C is exchanged for another useful set C'; while the merchants are operating within the capital circuit $M-C-C'-M'$, where a sum of money M = £100 is ultimately transformed into a larger sum M' = £200, through the exchange of one set of use-values C for a more valuable set C'.

The above circuits form the two poles of the transaction However, because only one of these poles is assessed in monetary terms, any monetary gain recorded there has no counterpart at the other pole. A net monetary gain can thus appear for the system as a whole. Note that this would not be the case if both poles were treated in the *same* terms. If the tribe's goods were valued at their final selling price of £200, it would be obvious that the tribe had exchanged a set of commodities worth £200 for another worth only £100, thereby losing in monetary value exactly as much as the merchants gam. In the end, it is *inequality of exchange* which underlies profit on transfer of wealth (profit on alienation) (Marx, 1863, ch. 1).

Interestingly enough, neoclassical economics tends to treat profit as simply profit on alienation. This is why the analysis of 'pure exchange' occupies so prominent a position within the theory. For instance, a classic illustration depicts a prisoner-of-war camp in which all prisoners receive equal (Red Cross) packages of commodities. An entrepeneur among the prisoners then mediates a more desirable distribution of the total mass of commodities, a part of which he pockets as his own reward. Since the other prisoners all gain in terms of their respective subjective (and hence non-comparable) utilities, that portion of their collective endowment which is gained by the entrepreneur is not treated as their loss. On the other hand, for the entrepreneur it is precisely this transferred wealth which is counted as his profit. With one pole of the transaction in subjective utility and the other in material gain, profit seems to be created out of thin air. Instead of attempting to dissolve this false appearance, neoclassical economics concentrates on presenting profit as the just reward of the capitalist class (Alchinn and Allen, 1969, chs. l-4).

PROFIT ON PRODUCTION OF SURPLUS VALUE. With the rise of industrial Capital, it became increasingly clear that industrial profit was quite different from profit on alienation. The latter was dependent on trade and unequal exchange, while the former was tied to production, wage labour and apparently equal exchange (Meek, 1956, Ch. 1). It is exactly in order to locate the fundamental difference

between the two that Marx insists on explaining industrial profit even when all exchanges are essentially equal (Marx, 1867, Ch. 5).

Marx begins by noting that every society must somehow direct the labour time at its disposal toward the production of the goods and services necessary to sustain and reproduce itself. In the case of class societies, the reproduction of the ruling class requires that it be able to extract a surplus product from the subordinate classes. This means that every ruling class must somehow get the subordinate classes to work beyond the time necessary to produce their own means of consumption, for it is this *surplus labour time* which creates the requisite surplus product (see EXPLOITATION).

The same basic process operates in capitalist society, but it is hidden under the surface of exchange relations and money magnitudes. To show this, Marx starts by assuming that the money price of each commodity is proportional to the total abstract labour time socially necessary for its production (its labour value). In the case of wage-labour, this means that money wages are proportional to the number of hours (v) workers must put in a given day in order to produce their collective daily means of consumption. Under the above circumstances, all commodities, including labour power (the capacity to work), exchange in proportion to the labour time socially necessary for their reproduction. All exchanges are therefore equal in a fundamental social sense, so that (for the moment) profit on alienation is ruled out of consideration.

During the production process a particular quantity of means of production (raw materials and machines) is used up each day. The abstract labour time (c) which was previously required to reproduce them is thereby transferred to the product. If we add to this the labour time worked by workers in a given day (l), the resultant sum ($c + l$) represents the total abstract labour time socially necessary to produce the daily product.

If exchange is proportional to labour times, then the price of the total social product is proportional to $c + l$. But the corresponding money cost of producing this product is proportional to $c + v$, since c represents the abstract labour cost of the means of production used up and v represents the corresponding costs of the workers employed. It follows from this that aggregate profits will exist only if $c + l > c + v$, which implies $l > v$. In other words, when prices are proportional to labour values (equal exchange), profit is the direct monetary expression of surplus labour time $s = l - v > 0$. This surplus labour time, performed by workers who produce commodities for capitalists (i.e. who produce commodity-capital), is what Marx calls *surplus value*.

Even when exchange is no longer proportional to labour value, the connection between profit and surplus value continues to hold, but in a more complex manner. In effect, when prices deviate from proportionality with labour values, this can give rise to transfers of value from one set of transactors to another. Now total profits can depart from proportionality with total surplus value even though in the aggregate the gains and losses due to transfers of value exactly cancel out! This apparent paradox, which has long bedevilled the extensive literature on the so-called Transformation Problem, is easily resolved once one

recognizes that the profit is a measure which only picks up a portion of the overall transfers of value involved. By definition, aggregate profit is simply the difference between the price of aggregate output and the price of that portion of this output which corresponds to the flows of commodities used up as 'inputs' into production, either directly as means of production or indirectly as wage goods. Thus, insofar as value is transferred between total output and these particular inputs, what capitalist producers as a whole may gain in revenues through a higher selling price is at the same time what they thereby lose through higher input costs. Total profits are therefore unchanged, because feedback between the price of outputs and the prices of these particular inputs prevents any overall transfer of surplus value. But the same cannot be said for those transfers involving the remaining portions of aggregate output, which enter respectively into the capital stock of the firm (as inventories, plant and equipment) or into the possession of the capitalists themselves as consumption goods. In the former case, any transfers are reflected in the balance sheets of the firms and are at best only partially transmitted to costs; whereas in the latter case, any gain in profits through a higher selling price of capitalist consumption goods is reflected in a corresponding loss in the personal accounts of the capitalists themselves, rather than in increases in business costs. Because the measure of profit only picks up a subset of the value transfers, total profit can end up departing from proportionality with surplus value within strict limits. This is *merely the same principle which underlies mercantilist projit.* It was well known to Marx himself (Shaikh, 1984).

FURTHER ISSUES. First of all, it is important to note that only at an abstract level of analysis is money profit (with or without the equalization of the rate of profit) the sole expression of surplus value. At a more concrete level, surplus value appears as producers' profits, gross trading margins, rents, interest, taxes and dividends. Similarly, one can develop the analysis to account for profits across industries, across firms within industries, across regions, and across nations. Contained within this movement from the abstract to the concrete is a subtle and powerful theory of competition and pricing, on whose basis this analysis can be developed (see the essay on Market Value and Market Price).

Secondly, our earlier discussion of profit on alienation should alert us to the fact that surplus value is not the only source of profit. This understanding is one of the great strengths of Marx's analysis of the determinants of profit. It is also an important historical and empirical issue in its own right. Even in the modern capitalist world, where surplus value is clearly the dominant basis for profit, one must be careful to account for transfers of wealth and value from non-capitalist spheres (petty commodity and non-commodity production) to capitalist ones – particularly in analysing the so-called Third World.

Thirdly, it should be noted that the very concept of the *transfer* of wealth and value is predicated on a distinction between those activities which produce the goods and services (use-values) comprising the annual wealth, and those which serve to transfer this wealth from one set of hands to another. This distinction

is in turn merely part of a more general one between production and non-production activities. In the latter camp we find not only the familiar category of personal consumption activities, but also the classical notion of social *consumption* activities such as those involved in the exchanging of goods, services and money; general administrative activities in both the private and public sectors; and various other social activities such as defence, etc. Production uses up use-values in order to produce more use-values. Personal and social consumptions use up use-values in order to achieve some other desired end. As such, the distinction between them has nothing to do, *per* se, with other distinctions such as those between necessary/unnecessary, desirable/undesirable and basic/non-basic activities. More importantly, the distinction between production and non-production activities has profound implications for the manner in which the wealth of capitalist nations is measured and analysed (Shaikh, 1978, section IV.C).

Fourthly, within the general category of production activities. a further difference arises between those which produce surplus value (i.e. produce surplus labour for a capitalist employer), and those which either produce value (petty commodity producers) or produce use-values for direct use (households, non-commodity producing communities). Though all these labours are productive of social wealth, only the first is directly productive of surplus value. This is why Marx singles out this particular form of labour as that labour which is productive-of-capital i.e. which is 'productive labour' from the point of view of capital. As a corollary to the above, it is then necessary to distinguish between the rate of exploitation (which applies to all workers employed by capital) and the rate of surplus value (which is the rate of exploitation of 'productive labour', since it alone produces surplus value) (Marx, 1867, Appendix, part II).

Lastly, it is important to recognize that the preceding categories interact in complex ways. For example, surplus value is simply the difference between the length of the working day (I) of productive workers, and that portion of it (v) which is required to produce the commodities they and their families consume. But the quantity of social labour time represented by v is not at all the same as the total social labour time required to reproduce productive workers, because the latter generally includes household and community labour involved in the reproduction of labour-power. To the extent that these non-capitalist labours are responsible for the bulk of the use-values consumed by productive workers, only a small amount of commodities will be involved. But since capitalists need only pay workers just enough to acquire the commodity portion of their standard of living. v will be low and s correspondingly high. Then. as capitalist production erodes village and/or household production, commodities will begin to comprise an ever greater portion of the standard of living of workers even as this overall standard may itself decline. To the capitalists, workers will be getting progressively more 'expensive' as their commodity requirements rise. Yet the workers themselves may be getting ever poorer if their overall standard of living is declining. Over certain periods, a rising real wage is perfectly compatible with a falling standard of living – as the history of many a developing capitalist

country demonstrates. All this goes to show that no analysis of a concrete social formation can afford to ignore the *interrelationships* between profit on transfer of wealth and profit on production of surplus value, between production and non-production activities and between capitalist and non-capitalist labour.

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