

Chapter 22: Division of Profit. Rate of Interest. ‘Natural’ Rate of Interest

Marx begins with a warning.

The object of this chapter, like the various phenomena of credit that we shall be dealing with later, cannot be investigated in detail. Competition between lenders and borrowers, and the resulting short-term fluctuations in the money market, fall outside the scope of our discussion. The circuit which the rate of interest describes during the industrial cycle can only be dealt with after the cycle itself. Nor can we go into the latter here. The same applies for the approximate equalisation of the rate of interest, more or less, on the world market. All that we are concerned with here is the independent form of interest-bearing capital and the way that interest acquires autonomy *vis-à-vis* profit.¹

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If interest is that part of profit which the industrial capitalist pays the money-lending capitalist, then the limits to interest would appear to be (‘leaving aside [...] special cases’²), on the one side, total profit (with nothing accruing to the industrial capitalist), and, on the other, zero (with nothing accruing to the money lender).

If the ratio of total profit and that part of it that ends up as interest is fixed, then interest will rise or fall with total profit (and total profit is in turn determined by the general rate of profit). So, if average profit is 20 % , and interest a quarter of this, the interest rate will be 5 % . If average profit is 16 % , then interest will be 4 % , and so on.

But if this is so, if interest is a constant proportion of average profit, the higher the latter the greater will be the rate of interest, and the greater the *absolute* difference between total profit and interest, and the greater the total profit accruing to the industrial capitalist. If interest is 20 % of average profit, and average profit is 10 % , the rate of interest is 2 % ; and the functional rate of profit for the industrial capitalist 8 % . If average profit stands at 20 % , the rate of interest is 4 % , and functional industrial profit 16 % . And so on. ‘As the rate of profit varies, so different rates of interest can express the same aliquot part of the total profit or the same percentage share in it. With interest such a constant proportion, the industrial profit (the difference between the total profit and the interest) would be greater, the higher the general rate of profit, and *vice versa*.’³

Assuming the ratio between interest and total profit as constant, the industrial capitalist is both able and willing to pay higher or lower interest in function of her own functional rate of profit. ‘In this sense one can say that interest is governed by profit, and more precisely by the general rate of profit. [...] *[T]he average rate of profit should be considered as ultimately determining the maximum limit of the interest.*’⁴

The circumstance we are considering here is that in which total profit is divided into two parts: interest, and functional (industrial or commercial) profit. ‘[T]he first thing that matters’ here is the magnitude of the profit to be divided. This is determined by, one, the magnitude of capital deployed, and, two, average profit. Once we take average profit as given, then, for a given magnitude of capital deployed, interest varies in inverse proportion

¹ Karl Marx, *Capital* volume 3 (Harmondsworth, 1981) [hereafter C3], p. 480.

² C3, p. 480. That this is the case (‘leaving aside [...] special cases’) contradicts Marx’s statement in the previous chapter (C3, p. 478). that how much interest accrues to the money-lending capitalist ‘is something inherently lawless and arbitrary.’ But see Laurence Harris’s comments: (‘On Interest, Credit and Capital’, <http://www.countdowninfo.net/uploads/6/7/3/6/6736569/on_interest_credit_and_capital.pdf>, pp. 149-50.

³ C3, p. 481.

⁴ C3, pp. 481-2; and, again, this is another law-like determination. ‘Since we have seen that the level of the profit rate stands in inverse proportion to the development of capitalist production, it follows that the higher or lower rate of interest in a country stands in the same inverse proportion to the level of industrial development, particularly in so far as the variation in the rate of interest expresses an actual variation in the profit rate. We shall see later on that this need by no means always be the case.’

to the part of profit that remains to the capitalist who operates with borrowed capital. But what determines the magnitude of the profit to be divided, i.e. ‘the value product of unpaid labour’, is not the same as what determines the distribution of this among the industrial capitalist and the money-lender. Given this, the rate of interest and average profit often move in contrary directions.

If we consider the turnover cycles in which modern industry moves – inactivity, growing animation, prosperity, overproduction, crash, stagnation, inactivity, etc. [...] – we find that a low level of interest generally corresponds to periods of prosperity or especially high profit, a rise in interest comes between prosperity and its collapse, while maximum interest up to extreme usury corresponds to a period of crisis.⁶

Why does the rate of interest rise during crises? Because, Marx argues, ‘people have to borrow in order to pay, no matter what the cost.’⁷

Quite apart from fluctuations in the rate of profit, the rate of interest displays a tendency to fall. Marx cites two reasons for this: first, with the development of capitalist production, the growth of an increasingly larger *rentier* class;⁸ second, ‘[t]he development of the credit system, the ever growing control this gives industrialists and merchants over the monetary savings of all classes of society through the mediation of the bankers, as well as the progressive concentration of these savings on a mass scale, so that they can function as money capital [...]’.⁹

Thus what determines the rate of interest is, on the one hand, average profit, and, on the other, the proportion into which this is divided. This latter depends on competition between money-lenders and industrial and commercial capitalists. And, in turn, this competition is regulated by the rate profit these last *expect* to realise.¹⁰

To find the *average* rate of interest, we have to find both the average rate of interest over its variation over the business cycle, and the rate of interest in those investment fields where capital is lent for more extended periods.

But: ‘The prevailing average rate of interest in a country [...] cannot be determined by any law. There is no natural rate of interest, therefore, in the sense that economists speak of a natural rate of profit and a natural rate of wages.’¹¹

The ‘coincidence of supply and demand’ (which we discussed in chapter 10) here means nothing. The ‘coincidence of supply and demand’ served earlier ‘as a formula for finding [the] basic rules which are *independent* of competition [...]’; i.e. it is a formula for [...] getting from the variations that accompany competition to the *limits of these variations*.¹² Here there is no determination *other than* supply and demand; and, ‘[w]here, as here, it is competition as such that decides, the determination is inherently accidental, purely empirical, and only pedantry or fantasy can seek to present this accident as something necessary.’¹³

⁵ In other words, the ‘business cycle’, ‘cycles which [...] [fall] outside the scope of our argument to analyse further’.

⁶ C3, p. 482. ‘From summer 1843 onwards there was a period of marked prosperity. The rate of interest, which in spring 1842 was still 4 ½ per cent, fell in spring and summer 1843 to 2 per cent; in September it even fell to 1 ½ per cent [...]. During the crisis of 1847, it rose to 8 per cent and more.’ But, Marx notes, ‘[...] low interest can also be accompanied by stagnation, and a moderate rise in interest by growing animation.’

⁷ C3, p. 483.

⁸ And thus, one assumes, increasing competition among money-lenders. Marx makes this point through means of quoting George Ramsay’s *An Essay on the Distribution of Wealth*. Ramsay (1800-1871) is credited by Marx (in *Theories of Surplus-Value: Collected Works*, vol. 33, pp. 255-6) as being the first political economist to distinguish between, at least *de facto*, constant and variable capital.

⁹ C3, p. 484. This, Marx notes, without developing the idea (‘[m]ore on this later,’ he remarks) ‘must also press down the rate of interest.’

¹⁰ Marx also makes this point by quoting Ramsay, and sadly leaves the last tantalising remark undeveloped.

¹¹ C3, p. 484.

¹² C3, p. 485 (italicisation added).

¹³ C3, p. 485. But see Laurence Harris (‘On Interest, Credit and Capital’,

<http://www.countdowninfo.net/uploads/6/7/3/6/6736569/on_interest_credit_and_capital.pdf>, pp. 149-50):

But what explains the apparent lawless-like nature of the determination of the rate of interest? Marx answers that this is so because of the *nature of interest itself*. Interest is no more than a part of average profit. “The same capital appears in a double capacity, as capital for loan in the hands of the lender, and as industrial or commercial capital in the hands of the functioning capitalist. *But it functions only once, and produces profit only once.*”¹⁴ The magnitude of value created in production is determined in and by production. The division of this value between the qualitatively different elements of wage-labour and capital is determined by production and the conditions of production: by the new value – socially necessary labour – contained in the products of production and the value – socially necessary labour – of the labour-power that creates it; the rate of profit is then determined by the relation between that part of the new value created accruing to the capitalist(s) and the capital laid out.¹⁵ ‘With the division between surplus-value and wages [...], two quite different elements are involved, labour-power and capital. It is the functions of two independent variables which set limits to one another, and the *quantitative division* of the value produced emerges from their *qualitative distinction*.’¹⁶ But ‘[i]n the production process itself, *the character of capital as loan capital does not play any role.*’¹⁷ The division of profit between profit and interest ‘stands a purely empirical fact, pertaining to the realm of chance, just as the respective shares in the common profit of a business partnership are distributed among its various members. [...] With interest [...], the *qualitative distinction* proceeds from the *purely quantitative division* of the same piece of surplus-value [...].’¹⁸

There can be, therefore, no ‘natural’ rate of interest: ‘the average [...] rate of interest [...] cannot be given limits by a general law, since what is involved is simply a distribution of the gross profit between two persons who possess capital under different titles [...].’¹⁹

To the degree that the rate of interest *is* determined by the rate of profit, it is the *general* rate of profit and not those specific rates of profit prevailing in particular branches of industry that determines. In addition, while the actually existing *market* rate of interest may fluctuate, ‘the average rate of interest is constant over long periods, because the general rate of profit changes only in the long run [...]. And the relative constancy of the profit rate is precisely reflected in this more or less constant character of the average or common rate of interest.’²⁰

‘Marx’s statements on the “accidental” and “empirical” nature of the rate of interest concern only the status of interest within value theory. Interest-bearing capital is a commodity with a use-value and exchange-value, but its exchange-value or its price cannot be related to the socially necessary labour time involved in its production [...]. Its ability to yield interest to its owner is quantitatively determined not by the qualitative differences between classes but by “competition” between different fractions of the bourgeoisie, or, in other words, by supply and demand for loanable capital. Thus, the level of the rate of interest is “accidental” only in the sense that the law of value plays no part in determining the equilibrium or average tendency of the rate of interest, the rate which exists when demand and supply “coincide”. [Therefore] [t]he fact that the rate of interest is (like the price of any commodity) determined by the forces of supply and demand and that (unlike other commodities) this occurs without the law of value acting as a determinant or central tendency does not mean that the determinants of the rate of interest lay outside of Marx’s field of enquiry.’

¹⁴ C3, p. 486.

¹⁵ ‘The general rate of profit is determined in fact (1) by the surplus-value that the total capital produces; (2) by the ratio of this surplus-value to the value of the total capital [...].’ C3, p. 489. Marx goes on to add: ‘and (3) by competition, but only in so far as this is the movement through which the capitals invested in particular spheres of production seek to draw equal dividends from this surplus-value in proportion to their relative size.’

¹⁶ C3, p. 486. ‘We shall see later on that the same thing takes place with the division of surplus-value between rent and profit.’

¹⁷ C3, p. 486 (italicisation added).

¹⁸ C3, p. 486.

¹⁹ C3, p. 487.

²⁰ C3, p. 488. In addition, while ‘[i]t is certainly true that the interest rate itself is always different according to the class of security provided by the borrowers, and according to the duration of the loan as well; but for each of these categories, it is uniform at a given moment of time. This distinction, therefore, does not militate against the fixed and uniform character of the rate of interest.’

What determines the market level of interest at any given time is the relationship between the supply of loan capital and the demand for it: with the development and concentration of the credit system – in which loan capital attains ‘a general social character’ – ‘all capital for loan confronts the functioning capital as an overall mass’ on the money market.²¹

Interest-bearing capital thus ‘becomes a commodity *sui generis* with interest as its price, and this price, just like the market price of an ordinary commodity, is fixed at any given time by demand and supply. The market rate of interest, though in constant flux, thus appears at any given moment as every bit as fixed and uniform as the momentary market price of any commodity.’²² Supply here is given by the money capitalists who supply this commodity; demand by the industrial and commercial capitalists who buy it. This is the process by which the rate of interest is established.

Marx is at great pains here to differentiate the determination of the appearance of a given rate of interest and the determinations governing the general rate of profit. In the case of the former, the determination is one of the relation between the supply of loan capital and the demand for it. The general rate of profit, on the other hand, ‘only ever exists as a tendency, as a movement of equalisation between particular rates of profit. The competition between capitalists – which is itself this movement of equalization – consists here in their withdrawing capital bit by bit from those spheres where profit is below the average for a long period, and similarly injecting it bit by bit into spheres where it is above this; or, alternatively, in their dividing additional capital between these spheres in varying proportions.’²³ Average profit thus appears as a *tendency*, not a given fact: ‘[i]t appears only in the fluctuations and equalisations that reduce the market prices of commodities to their production prices; not *as the direct establishment of an average profit*.’²⁴ This appearance is due to the fact that ‘the general rate of profit [...] obtains its determination in quite different and far more complicated ways than does the market rate of interest’; while the latter, on the other hand, ‘is directly and immediately determined by the relation of supply and demand, and [...] therefore [appears as] [...] a palpable and given fact [...]’.²⁵

Hence, on the one hand, ‘[a]verage profit does not appear as a directly given fact, but rather as the end-product of an equalization of opposing tendencies that can only be established by investigation’,²⁶ while, on the other, ‘[w]here it is a universal governing rule, which occurs at least locally, [the interest rate] [...] is a fact fixed every day, a fact that even serves industrial and commercial capital as a presupposition and postulate in their operating calculations. *It becomes a general property of any sum of £100 that it will yield 2, 3, 4, 5 per cent.*’²⁷

Marx closes the chapter with a fundamentally important observation. Given that on the money market the commodity on offer has the form of money,

[a]ll particular forms of capital, arising from its investment in particular spheres of production or circulation, are obliterated [...]. It exists in the undifferentiated, self-identical form of independent value, of money.[...] Here capital really does emerge [...] as *the common capital of the class* [...]. Money capital on the money market [...] really does possess the form in which it is distributed as a common element among [...] the capitalist class, quite irrespective of its particular application [...]. On top of this, with the development of large-scale industry

²¹ C3, p. 488.

²² C3, p. 489.

²³ C3, p. 488.

²⁴ C3, p. 489 (italicisation added).

²⁵ C3, p. 489-90. ‘In stressing this distinction between the interest rate and the profit rate, we have so far left aside the following two factors, which favour the consolidation of the interest rate: (1) the historical pre-existence of interest-bearing capital and the existence of a general rate of interest handed down by tradition; (2) the far stronger direct influence that the world market exerts on the establishment of the interest rate, independently of the conditions of production in a country, as compared with its influence on the profit rate.’

²⁶ ‘The particular profit rates in the various spheres of production are themselves more or less uncertain; but insofar as they do show themselves, it is not their uniformity that is apparent but rather their variation. The general rate of profit itself simply appears as the minimum limit of profit, not as an empirical and directly visible form of the actual profit rate.’

²⁷ C3, p. 490 (italicisation added).

money capital emerges more and more, in so far as it appears on the market; as not represented by the individual capitalist [...], but rather as a concentrated and organized mass, placed under the control of the bankers as representatives of the social capital in a quite different manner to real production. The result is that, as far as the form of demand goes, capital for loan is faced with the entire weight of a class, while, as far as supply goes, it itself appears *en masse* as loan capital.²⁸

²⁸ C3, pp. 490-1.