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IS THERE AN ALLOCATION PROBLEM?: ACCOUNTING FOR UNPRODUCTIVE LABOR

In the Fall 1993 issue of *Science & Society* the editors observed that Murray Smith's article on the falling rate of profit, which formed the opening contribution to that issue, constituted an important new study that "should be compared with the work of [Thomas] Weisskopf, [Edward] Wolff and [Fred] Moseley" – all of whom have carried out empirical investigations into the rate of profit (Editors, S&S, 1993; Smith, 1993). Yet, in the article itself Smith took pains to contrast his empirical results not so much with the work of these radical economists (two of whom he never mentioned) as with the tradition of thought that he classified as "underconsumptionist," associated with the work of Paul Baran, Paul Sweezy, Joseph Phillips, Harry Magdoff, and the present authors. Indeed, Smith contended that a recent statistical assessment of the economic surplus that we authored (Dawson and Foster, 1991; Dawson and Foster, 1992) contradicted the main theoretical thrust of the tradition we represent, demonstrating that "the (profitability) crises of the 1970s and 1980s cannot be adequately explained on the basis of an underconsumptionist mode of analysis" (Smith, 1993, 282). This clearly requires some response on our part. Before this matter can be addressed, however, it is necessary to scrutinize Smith's central argument with respect to the falling rate of profit and what the S&S editors have referred to as "the allocation problem" (the question of the allocation of unproductive labor within the components of total value: constant capital, variable capital and surplus value) (Editors, S&S, 1993; Laibman, 1993, 227n). Only by scrutinizing Smith's approach to the "allocation problem" is it possible to understand the enormous gulf that separates his analysis not only from that of monopoly capital/stagnation (MCS) theorists like Baran, Sweezy, Magdoff and ourselves, but also from that of most classical-Marxist exponents of the tendency of the rate of profit to fall (TRPF), such as Fred Moseley and Anwar Shaikh.

The Allocation of Unproductive Labor

"Profits," Howard Sherman once wrote, "are the most difficult of all economic quantities to measure. Profit measures the difference between 'revenue' and 'cost,' but these two items are themselves the subject of much controversy as to what should be included and how to measure it" (Sherman, 1968, 20). And if profits by themselves are notoriously difficult to measure the profit *rate* is even more so, since there are also deep disagreements among economists, business analysts and accountants about what kind of base to measure these profits against. Attempts to analyze profit rates from a Marxian standpoint encounter many of these same difficulties, while being confronted with additional problems related to the distinctive character of Marxian theory.

Given the uncertainty that surrounds the measurement of profit rates, the easiest way to make a case for falling profit rates as a basic tendency of the contemporary economy is to find definitional ways of shrinking the numerator and enlarging the denominator of the profit ratio (particularly if the change in definition is such that it produces a systematic tendency toward a shrinking numerator and an expanding denominator). Following Moseley, the rate of profit can be said to equal $(S/V)/(C/V) = S/C$, where V = variable capital or wages, S = surplus value or the residual of value-added once wages are deducted, and C = constant capital stock, or the accumulated stock of fixed and circulating capital invested (Moseley, 1991, 11).[1] Those who emphasize a falling rate of profit as the basic tendency of capitalism are naturally attracted to treatments that increase the

1 Marx expresses the rate of profit (the mark-up) as $S/(C+V)$. If we divide both the numerator and the denominator by V, this gives us $(S/V)/(C/V + 1)$. This means that the rate of profit varies directly with the rate of surplus value (S/V) and inversely with the organic composition of capital (C/V) (see Sweezy, 1984a, 45; Mandel, 1981, 31; Foley, 45). Since our analysis here is concerned with the issue of the profit rate as it is generally treated in the empirical debate, we have defined the denominator as the accumulated stock of *constant* capital (C) invested, which does not however alter the basic relation between the rate of surplus value and the organic composition.

size of C and V in relation to S. Just as naturally those who argue against the contemporary relevance of TRPF may find themselves drawn to those choices – in the definition of the components of value and the empirical measurement of profit rates – that raise S in relation to C and V.

Within radical political economy the most serious division so far in the treatment of the profit rate has revolved around the allocation of unproductive labor. Radical profit squeeze (PS) theorists (those like Samuel Bowles, Herbert Gintis and Thomas Weisskopf, who argue that high wages and the slow growth of labor productivity are squeezing profits) generally deny the distinction between productive and unproductive labor. What Marx called "unproductive labor" is thus subsumed under wage costs in general (Bowles, Gordon and Weisskopf, 1983). In contrast, the vast majority of Marxist economists have followed Marx himself in treating unproductive labor as a deduction from surplus value (see Shaikh, 1987). As Marx wrote,

> The general law is that *all costs of circulation which arise only from changes in the forms of commodities do not add to their value.* They are merely expenses incurred in the realisation of the value or in its conversion from one form into another. The capital spent to meet these costs (including the labour done under its control) belongs among the *faux frais* [dead expenses] of capitalist production. They must be replaced from the surplus-product and constitute, as far as the entire capitalist class is concerned, a deduction from the surplus-value or surplus-product, just as the time a labourer needs for the purchase of his means of subsistence is lost time. (Marx, 1967a, 149.)

It seems clear from this that unproductive labor constitutes a deduction from S. As Paul Sweezy has explained, both the labor and capital associated with what Marx called the "costs of circulation" (which today takes such forms as "product differentiation, branding, advertising, packaging, and the like") are unproductive in the sense that "they consume but do not produce surplus value" (Sweezy, 1984b, 38). Nevertheless, PS theorists (who seldom adhere to Marxian value theory, relying instead on neo-Ricardian or neoclassical value theories) reject the productive/unproductive labor distinction and therefore include all payments to labor (of whatever type) in V. The result is an empirical assessment that tends to point to a much higher squeeze on profits – one that places the main blame on high unit wage costs and that differs little (except in terms of policy perspectives) from the hegemonic neoclassical view of economic crisis.

This difference in the treatment of productive/unproductive labor has naturally resulted in widely divergent empirical results within radical political economy with respect to the rate of profit. Thus PS theorist Thomas Weisskopf's estimates of the profit share of national income (which he uses as a proxy for the rate of surplus value) showed a decline of 31% over the years 1949 to 1975, while TRPF theorist Fred Moseley's estimates of the rate of surplus value increased 14% over the same period. Similarly, Weisskopf's estimates of the rate of profit declined 38% between 1949 and 1975, while Moseley's estimates declined only 18% over this same period. According to Moseley, the differences between Weisskopf's estimates of the rate of surplus value and the rate of profit and his own are "due entirely to the different interpretations of productive and unproductive labor" (Moseley, 1991, 76-87; Weisskopf, 1979).[2]

Given this split between PS theorists and classical-Marxist economists on the allocation of unproductive labor, one might conclude that there is an "allocation problem" within *radical* political economy. Since PS theorists generally do not adhere to Marxian value theory this does not, however, suggest that there is an allocation problem internal to *classical-Marxian* political economy, viewed as a subset of radical political economy. From a classical-Marxist perspective, there is little doubt that Marx excluded unproductive labor from *V*. As Smith writes, "The exclusion of the values flowing to the unproductive sectors of the workforce from the measurement of the category of variable capital is, in my view, the first, elementary step to a specification of Marx's value categories adequate to the task of empirically evaluating his theory on its own terms" (Smith, 1991, 164). Whatever its merits in other respects, then, the profit squeeze approach, which incorporates unproductive labor within *V*, does not conform to classical-Marxian theory in its definition of the rate of profit.[3]

Nevertheless, in his attempt to strengthen the TRPF theory Smith raises a different sort of "allocation problem" (a term introduced not by him but by the S&S editors) directed at classical-Marxian value theory. In his view a "curious convention" has assigned unproductive labor to *S*, the numerator of the profit rate equation, while it really belongs to the constant capital flow, or what Marx called "dead labor." Hence, Smith sharply criticizes

2 Moseley's treatment of unproductive labor affects both the numerator and the denominator of the profit ratio. As he puts it, "labor and material costs of the unproductive functions of circulation and supervision" are included in *S*, while *C* excludes "money expended to purchase the means of circulation and the means of supervision within capitalist enterprises" (Moseley, 1991, 41).

3 There are of course some non-traditional Marxian political economists, like David Laibman, who recognize the classical foundations of the productive/unproductive labor distinction, but reject it on the purely pragmatic grounds that it lacks a consistent definition and means of measurement, and is therefore without "operational significance" (Laibman, 1993, 226–27).

the following Marxian political economists for subsuming unproductive labor under surplus value: Ernest Mandel, Anwar Shaikh, Ben Fine, Laurence Harris, Fred Moseley, Paul Sweezy, Paul Baran, Joseph Gillman, Joseph Phillips, and John Bellamy Foster. The value specifications of such theorists, he claims, "have retained an almost unchallenged grip on Marxist economic theory." In contrast, only Shane Mage (in his 1963 doctoral dissertation) and Smith himself, we are told, have correctly understood the problem of allocation with respect to Marx's economics (Smith, 1993, 266, 270–73, 282–84; Smith, 1991, 185n, 187n).

Before looking at how Smith attempts to justify his analysis it may be helpful to note its implications for the empirical measurement of profit rates. Since unproductive expenditures are without question a rapidly growing portion of the contemporary economy (due to a growing sales effort and the expansion of finance, etc.) Smith's approach will, by removing all such costs from S, produce a much stronger tendency for the rate of profit to decline. His empirical results are thus bound to be similar to those of PS theorists, whose definitions of the numerator and denominator of the profit ratio are quite similar to his own. Indeed Smith indicates some agreement with the PS approach, stating that "a rising strength of labor at the point of production may result in declining industrial productivity (as well as in a possible 'wage-push/profit-squeeze')" (Smith, 1993, 289). Yet for Smith the profit squeeze is primarily a secular tendency toward a declining rate of profit resulting from a rapidly expanding organic composition of capital, and not – as in PS theory – a long-wave downturn resulting from a "social structure of accumulation" that no longer supports robust economic development. Indeed, Smith's "respecification" of the traditional TRPF analysis would seem to present as close an example of a breakdown thesis as one could find today within Marxian political economy. As he states – at the end of a section entitled "Theoretical Advantages of Treating SNUL [socially necessary unproductive labor] as Constant Capital" – this approach is "resistant to a *reformist* perspective, staking its ground on Marx's thesis that the system 'moves in contradiction' and is subject to increasingly severe crisis tendencies" (Smith, 1993, 280–81).

Smith presents himself as a fundamentalist Marxist basing his analysis directly on "Marx's own law" (Smith, 1993, 282). He therefore seeks to establish that it was Marx who first argued that unproductive labor should be treated as constant capital. Ironically, this requires some rewriting and a good deal of creative interpretation of Marx's text. Thus faced with Marx's famous statement (quoted above) that unproductive labor, insofar as it merely alters the form of a commodity, does not add any value and should be regarded as a "deduction from surplus value," Smith argues that this can be made consistent with his own position "if we amend the wording of Marx's [first] sentence," and if we interpret his entire statement in less absolute, more "relative" terms (Smith, 1993, 272).

Quoting, in addition, from Marx's *Grundrisse*, where it says that circulation costs represent "an increase of necessary labor in relation to surplus value," he contends that this contradicts the dominant Marxist view that "circulation costs are 'paid out of' surplus value" (*Ibid.*; Marx, 1973, 548). Unless one interprets "necessary labor" here in the sense of variable capital (which Smith himself would not do) one has no difficulty however in perceiving that unproductive labor is a necessary form of labor that is also a deduction from what might be called gross surplus value. For individual capitals the effect is to reduce their net profit rates (after the overhead costs associated with unproductive labor are deducted). In no way does any of this lend support to Smith's assertion that unproductive costs should be treated as a form of constant capital.

The best textual evidence that Smith is able to pull out of Marx to defend his position is a statement in Volume III of *Capital* where Marx says that, since they reduce the profit rate, the capitalist seeks to keep the "expenses of circulation down to a minimum, just as his expenses for constant capital" (Marx, 1967b, 299). Yet later in the same paragraph (in a sentence Smith doesn't quote) Marx observes: "To what extent profit is the *precondition* for these outlays [on circulation], is seen, among other things, from the fact that with the increase of commercial salaries, a part of them is frequently paid by a share in the profit" (emphasis added). Marx thus remains consistent in seeing such unproductive expenditures as deductions from *S*. There is no real support here then for Smith's assertion that unproductive labor should be treated as an element of constant capital flow, *i.e.*, dead labor.

The truth is that Smith is unable to find a single explicit statement in the thousands of pages on economic theory written by Marx that suggests that unproductive labor should be subsumed under constant capital. According to Mage, "Marx never explicitly defines the 'unproductive but necessary expenses' of capitalist production as part of the *constant* capital" (Mage, 1963, 67).

Nevertheless, Smith encourages us to believe that "*implicit*" statements to that effect can be found in Marx's work. Thus we are told that unproductive labor and constant capital are similar in that they both have indirect effects on the formation of value (and surplus value). Moreover, Smith argues that "Marx's own imagery" supports his position. Here he introduces us to a passage in which Marx metaphorically says: "One merchant (considered here merely as the agent of the formal transformation of commodities, as mere buyer and seller) . . . should then be considered as a *machine*." From this Smith leaps to the conclusion that, in conformity with Marx's theory, the concept of machinery can be broadened into a concept of "social machinery," encompassing both machines and unproductive labor: "Simply expressed, the production of value requires the existence of special 'social machinery' (including unproductive living labor) specific to capitalism." In the end we are told that anyone who sees constant capital primarily in terms of machinery (understood as a particular use value) and does not expand this to a concept of "social machinery" (encompassing unproductive labor) is guilty of "capital fetishism" (Smith, 1993, 271–78; Smith, 1991, 172–75).

All of this strikes us as idiosyncratic. Indeed, in our view Smith's analysis does not succeed in its main objective of establishing that there is an "allocation problem" that requires the "respecification" of classical-Marxian value categories. His treatment of unproductive labor as a form of constant capital is too antagonistic to the basic structure of Marxian political economy to be taken seriously in that respect. Yet, Smith is right that unproductive expenditures are costly for capital. To understand the larger significance of this it is useful to look at Smith's criticism of Baran and Sweezy.

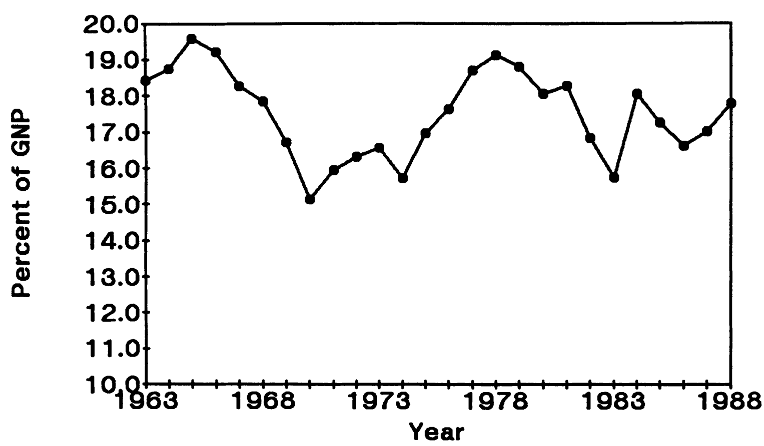
Smith's Criticism of MCS Theory

For Smith the school of Marxian economic thought most opposed to his own is the one associated with Baran and Sweezy's *Monopoly Capital*. "By rapidly expanding the estimates of surplus value" this tradition, Smith argues, "minimizes the decline in the average rate of profit, emphasizes a rise in the rate of surplus value and disputes the notion of a rise in the organic composition of capital" (Smith, 1993, 281; Smith, 1991, 162; Baran and Sweezy, 1966; Foster 1986). What he objects to of course is the inclusion of the costs of unproductive labor (viewed as social overhead costs) within *S* (in this case the economic surplus), since this leads to empirical results directly opposite to Smith's own.

Specifically, Smith argues that MCS theory has only been able to establish a tendency of the surplus to rise by incorporating unproductive labor within economic surplus. According to Smith the data provided by Phillips (in the statistical appendix to *Monopoly Capital*) reveals (once one defines surplus in Smith's terms rather than Baran and Sweezy's) "a tendency exactly opposite to what Baran and Sweezy attribute to 20th-century advanced capitalism"; while our own data (once Smith's definitions for surplus are substituted for our own) likewise fail to demonstrate a tendency for the surplus to rise (Smith, 1993, 281; Baran and Sweezy, 1966; Dawson and Foster, 1991; Dawson and Foster, 1992). He makes this criticism most explicit in relation to our study, where he writes: "Significantly, a recent study updating this data series shows that between 1963 and 1988 the (actual) surplus percentage (inclusive of adjusted corporate profits, estimated profits of unincorporated business, rental income, net interest, and the profit element in corporate officer compensation) persistently fluctuated in the 16% to 20% range, displaying no clear-cut trend over the 25 year period." For Smith this provides conclusive proof that the law of the tendency of the surplus to rise is merely a statistical sleight of hand, resulting from the improper incorporation of unproductive labor within the economic surplus.

To clarify what is at issue here we have put the data that Smith takes from our study and that he refers to as the "actual surplus" on a graph (Figure 1). A quick glance at this shows that – far from showing "no clear-cut trend" – "actual surplus" as a percentage of GNP has shown a flat trend over the period concerned. (As elementary statistics teaches us, a flat trend is itself a discernible trend.) What this means is that the increase in "actual surplus" basically kept pace with the growth of GNP, despite the fact that the period covered by our data was one of slow growth in the U. S. economy (when compared to the decades immediately following the Second World War). What Smith calls the "actual surplus" is not however the whole story. Our data for gross economic surplus as a percentage of GNP over the years

FIGURE 1
SMITH'S "ACTUAL SURPLUS": United States, 1963–1988



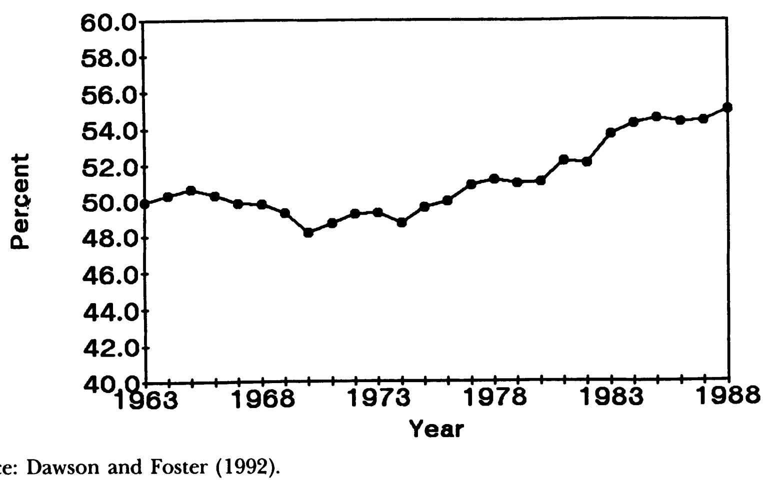
Source: Dawson and Foster (1992).

1963–1988 are shown in Figure 2, where a tendency for the surplus to rise is clearly evident.

All of this demonstrates that there is a wide gap separating Smith's approach from our own. In our analysis, like that of Baran and Sweezy, economic surplus (or surplus value) can no longer be viewed mainly in terms of profits + rent + interest, since it assumes many disguises and leaves its statistical trace in inflated depreciation allowances, taxes, corporate officer payments, advertising costs, surplus employee compensation (*i.e.*, employment in finance, insurance, real estate and legal services), etc. If for Smith unproductive labor is part of the *social machinery* of capitalist production and belongs to constant capital or dead labor, for us it is a social overhead cost arising from the *class management* of the system, and thus is best understood as an outlay deducted from *S*, the social accumulation fund of the capitalist economy. To ignore this complex reality of surplus appropriation in today's society is, in our view, to make Marxist economics largely irrelevant as a critical framework of analysis.

None of this is meant to suggest that unproductive labor does not represent a cost to capital. As Duncan Foley has written, "The United States economy has reached very high absolute levels of labor productivity, and as a result the rate of surplus value and the mass of surplus value are both extremely large. But most of this surplus value is consumed in the process of distributing the product and coping with the conflicts engendered in

FIGURE 2
GROSS SURPLUS AS SHARE OF U.S. GROSS NATIONAL PRODUCT



Source: Dawson and Foster (1992).

the production of value." Thus while Foley estimates that $1.5 trillion in surplus value was produced in 1983 – which compares to our own estimate of $1.49 trillion in net economic surplus (gross surplus minus depreciation) for that year – "the largest share, $1,000 billion, went to pay the wages of unproductive workers in business and government" (Foley, 1986, 123; Dawson and Foster, 1992, 63).

In its monopoly capital stage, characterized by chronic excess capacity, the system quite obviously cannot live without this high overhead associated with the *class management* of the economy. Nevertheless, such outlays are deducted from surplus value and are not available to form direct property income (Wolff, 1987, 177–79). This is a problem that one cannot even begin to understand in terms of the classical law of the TRPF. Yet it constitutes one of the major conundrums of accumulation on the brink of the 21st century.

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RECONSTRUCTING MARXISM: SOME COMMENTS ON COMMENTS

1. *Introduction: Scope of Present Comments.* The Spring 1994 of *Science & Society* contains two sets of comments on my earlier critical essay (Suchting, 1993) on a recent book on Marxism (WLS, 1992). The authors of the latter (WLS, 1994; henceforth simply "WLS") write: "in the vast majority of instances, Suchting misrepresents our positions. In others, he seems not to realize that we agree with what he claims we deny." They continue: "It would be tedious to elaborate on these claims in great detail. We therefore offer a few illustrative examples" (53; cf. 55). However, "there does appear to be a genuine disagreement between Suchting and ourselves about