Theories of the essence and source of profit in capitalist economics

Prof. Dr. Muostafa El-Abdallah Al-Kafry

Contents

Theories of the essence and source of profit in capitalist economics

Prof. Dr. Muostafa El-Abdallah Al-Kafry

Introduction:

Profit is another type of income arising from ownership besides interest and rent. The concept of profit for economists differs from the concept of profit for accountants. Profit, according to the accountants' point of view, is the amount that remains for the capitalist after he pays wages, interest and rent, after he pays the value of inputs, and deducts a percentage equivalent to the depreciation of buildings and equipment. Economists differ in this from accountants because they believe that the costs of opportunity for work, capital and land contributed by the owner of the enterprise should be deducted. 1

Capitalist profit, regardless of the form in which it appears, is achieved through the exploitation of wage workers, this one category that creates all the material goods that are produced within the process of capitalist production.

The ambition of capitalist firms to make as much profit as possible is the main driver of the growth and development of production and exchange in the capitalist economy. This means that if we cannot clarify the essence and source of profit, we cannot fully understand the essence of the capitalist mode of production.

It seems at first glance that profit is achieved when a capitalist sells his goods at a price higher than the purchase price. This clarification is insufficient. That's because the exchange of goods doesn't create any new value. Indeed, the value added in the overall economy does not result from uneven exchange. When the sale is made above the value, this means that the profit is made to the seller against the loss suffered by the buyer, that is, the profits of the sellers

[1] - Edwin Mansfield Nariman Behravish, Economics, Arabization of the Jordanian Book Center, Amman 1988, p. 645.

will be equivalent to the loss of the buyers, and the value remains the same without any increase.

From the foregoing, we find that profit is not achieved in the field of goods circulation, but only in the field of production, and the means of production used in the production process cannot be a source of profit, because these means of production cannot be transferred to the final product with a new value greater than their value if used in the production process. Thus, the labour force used by workers in the production process is the only source of profit, because labour power can appear in the final product at a greater value than the value the worker sold to the capitalist during the production process. In other words, the worker receives a part of the value of the labor force sold by the capitalist, in the form of wages, and the rest goes to the pocket of the capitalist, in the form of surplus value, and this happens because the capitalist owns the means of production, while the worker has only his ability to work, and he is forced to rent them to the capitalist who owns the means of production in order to secure the means of subsistence for him and his family. Thus, the labor force in the capitalist system is the only commodity that has special characteristics that make it capable of creating new value that is distributed between the wage of the paid worker and the profit of the capitalist. 2

I - Factors of emergence of economic profit:

When industrial enterprises operate under full competition, where there is complete freedom to enter or exit a specific branch of industry, and if we assume that the level of technical knowledge is constant, so that all enterprises in this branch use the same technical level in the production process, and if all enterprises operate in conditions of complete certainty regarding the marketing process and its future, under all these circumstances, no profits will be made. But the reality is very different from the above picture and the

[2] - See: J.Nowicki Zarys Ekonomi Politgcznej Kapitalizmu P.W.E - Warszawa 1977 r. , Str, 67

conditions that institutions are going through, and the differences that occur between institutions and entail factors to make a profit from them:

1 - Innovations:

Creativity and innovation continue in industrial activity, and innovations are the discovery of new methods by which production is improved in quantity and quality. Some economists see profits as the return that innovators receive. Due to competition between producers and the imitation of innovations, the profits resulting from the discovery of an innovation decrease, but this is an incentive to develop innovations and discover others in order to maintain those innovative profits.

2 - Risk and uncertainty conditions:

In order for entrepreneurs to be tempted to employ their money and take the risk of investing in certain economic activities, there must be a return (profit) for taking those risks. Profits vary depending on the degree of risk that characterizes economic activity, and these profits are called risk profits.

3 - Monopoly Profits:

Sometimes a producer may enjoy a monopoly position in the market when he buys one of the factors of production in full, so that this product makes profits as a result of the monopoly position, and these profits are called monopoly profits, and the profit resulting from the purchasing monopoly is estimated by the difference between what the producer actually pays to the owner of the monopoly production factor, what he could have received in the event that full competition prevailed in the market of the production worker.

The producer may make monopolistic profits as a result of having a monopoly position when selling its production on the market, and the profit from the monopoly on sale is estimated to be the difference between what the actually monopolized product receives and what it would have received had it not enjoyed that monopoly position.

II - Functions and role of profit:

Economists believe that profits have an important role in the capitalist economic system, as profits in the capitalist system have many functions, the most important of which are: 3

(a) Profits are the indicator that defines areas of economic activity where employment is directed towards areas that generate the most profits while employment comes out in areas that suffer losses. This will continue until the so-called optimal use of resources is achieved.

(b) Profits are a catalyst for creativity and innovation, as an enterprise that invents means that lead to the use of its resources more efficiently receives higher profits in return.

(c) Profits are an incentive for entrepreneurs to break into new investment areas and take on increased risks. It opens up new areas for the productive process, to support the national economy.

(d) Profit is a guide to economic development, since the pursuit of profit is directed by the owners of enterprises to direct their economic activity.

Since profit in a capitalist system is usually proportional to the amount of capital invested, capitalists generally seek to convert a large part of their profits into new capital that generates more profits for them. The pursuit of profit also gives way to the development of different regions and countries. Profit attracts newcomers to new areas and pushes for the establishment of facilities necessary for the exercise of economic activity. 4

III - Bourgeois theories in the interpretation of profit:

The pioneers of the Mercantile business school believed that profit appeared in foreign trade, because capitalists sold goods outside the borders of the country where they were produced, at prices higher than their purchase prices within the state and thus made a profit.

---

[3] - Ibid., pp. 358-359.

[4]- D. Matanius Habib, Political Economy, Publications of the Faculty of Economics, Damascus University, Damascus, p. 212.

Then came Adam Smith and David Ricardo from the pioneers of the traditional (classical) school, explaining that profit appears in production and does not appear in trading. They added that the value that workers add to the value of materials during production is divided into two parts:

- The first - goes as wages for the workers who carried out the production process,
- The second – the profit that employers receive.

The English economist Marshall views profit as a reward that the director of the institution receives for the services he provides to society. This remuneration, he believes, is compensation for the following three main elements: the capital element, the workers' component, and the organization of business, which combines the first and second elements and pushes them to movement and activity. A large number of bourgeois economists argue that profit is a reward for the work done by the employer in organizing production. Profit is not achieved as a result of the effort and work of all capitalists, but only for those capitalists who succeed.

From the foregoing, we note that bourgeois theories assume that profit is a legitimate phenomenon in the economic system and necessary for the continuation of economic progress. We also note that there are a number of theories that explain profit on this basis, the most important of which are:

1 - Theory of Return on Capital:

Three main factors contribute to the productive process: labor, capital and land, and the three factors of production mentioned are sources of three types of incomes, each of which is independent of the other:

- Work - the source of wages.
- Capital - the source of profit.
- Land - the source of real estate rent.

Since the means of production are capital, the profit here is a return on the capital that has been employed in the productive process.

2 - The theory of (profit for the work done by the capitalist):

The capitalist has an important role in the productive process, and the function of the capitalist lies in the collection and organization of factors of production and the management of the productive process. Thus, the profit he receives is the wage he deserves for the work he does to contribute to the productive process. When the job of the workers is to carry out executive work, the job of the capitalist is the organizational work. (The wages of the workers and the profits of the capitalists are therefore also necessary social incomes and a fair reward for necessary social jobs.) 5

3 - Theory (profit is a reward for the risk borne by the capitalist):

Products produced in a market economy are exposed to two types of risks:

traditional risks such as theft, fire and others, Economic risks associated with the market economy, fluctuations in demand and unpredictability of the future. Here the capitalist is exposed to a number of questions that are difficult to answer or the answer is a number of possibilities, and since it is the market that decides the right or wrong of any choice, so either the capitalist achieves success and profit or he is exposed to loss and bankruptcy. Thus, the profit that the capitalist receives is the reward he receives as a result of being exposed to risk during the productive process.

4 - Theory (profit is the price of innovation):

Some bourgeois economists see "profit in essence as the result of the implementation of a new organization". Thus, it is the organized capitalist who drives and drives economic activity. The profit he receives is nothing but a reward for the capitalist's diverse innovations: the implementation of a new product, the improvement of an old one, the discovery of a modern technology, the

[5] - Ibid., p. 216.

modernization of the technical mode of production, the increase in production. This means that profit is nothing but the price of monopolistic work, an innovation that the capitalist has accomplished and for which he deserves to be rewarded.

These theories have tried to explain and justify the capitalist's access to profit without looking for the primary source of profit. Then came Marxist theory and interpreted profit as a transformed form of excess value with an exploitative character.

Prof. Dr. Muostafa El-Abdallah Al-Kafry

Faculty of Economics – Damascus University