2016-10-24 & 31 From the preparatory notes for Class 25 (2nd part) and Class 26 of the introductory course on political economy: 'The evolution of property and how it rules the world'.

The 'engine of inequality'

There is a formidable **engine of inequality** at work.

While it is important to study the price mechanism, the way competition operates, and the distortions of the market where competition is ineffective, it would be a mistake to think that those distortions are the *basis* of persistent social inequality.

The argument of this course is that, even if we assume competition and equilibrium pricing, the system automatically has the result that **those who have more get more.**

Our study of the evolution of property has shown how **entitlements to the social surplus** have become concentrated in fewer and fewer hands.

This is a phenomenon of the whole world economy.

Recall **the graph by Branko Milanovic.**[1]

From 1988 - 2008, the richest 10% received 60% of global income gains

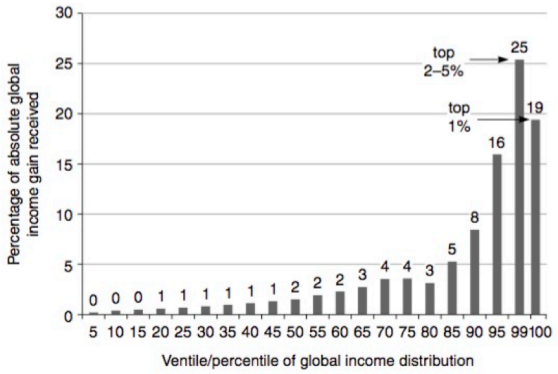

FIGURE 1.2. Percentage of absolute gain in real per capita income received, by global income level, 1988–2008

This graph shows the percentage of total absolute gain in real household per capita income (measured in 2005 international dollars) between 1988 and 2008 received by groups at different points of the global income distribution. We take the increase in total world real income as 100 and calculate how much of it was received by different ventiles (groups of 5% of the population) or percentiles of the global income distribution. The graph shows that the absolute gains in income went mostly to the richest 5% of the world population. The top 1% got 19% of the total global income increase. Data source: Lakner and Milanovic (2015).

Page 25. Milanovic, Global Inequality

And **the similar picture for South Africa.**

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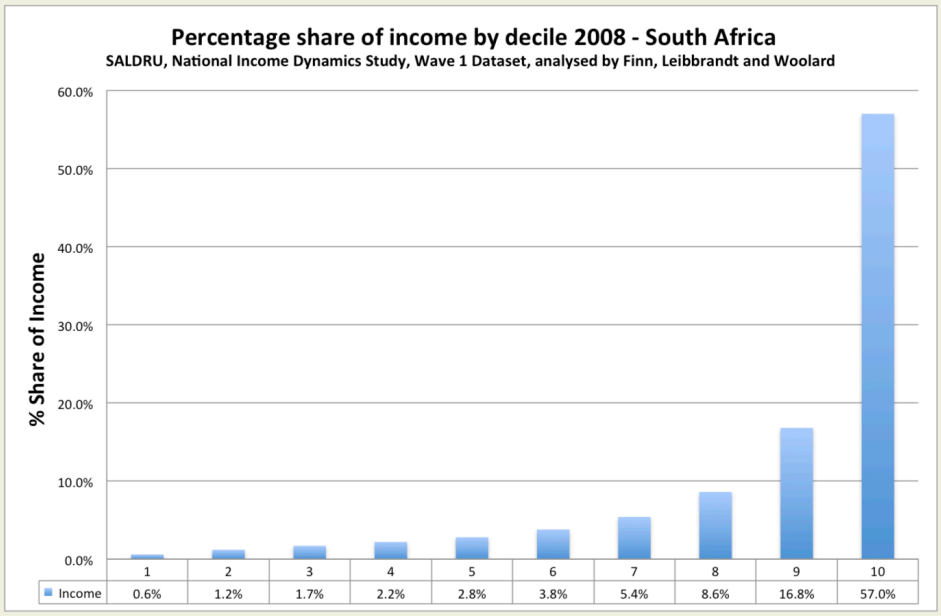
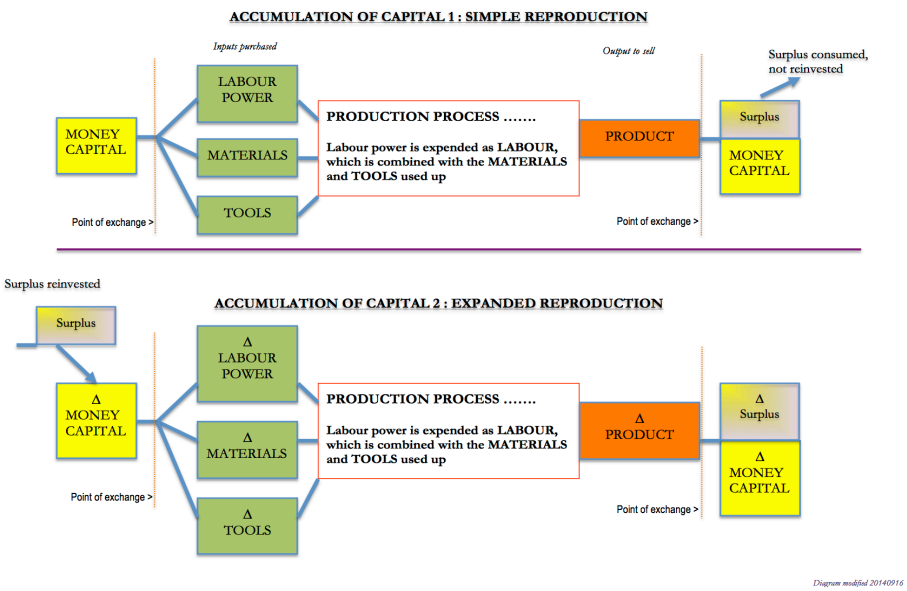
[1] See originally Class 5.



We have seen how the rise of the company (the corporation), and shareholding in place of individual ownership of enterprises, led historically to a much greater development of the financial system.

We have seen how individual entitlements to surplus have become increasingly indirect, and are mainly exercised via the financial system.

However, **the surplus itself is produced at the base**. Recall **the diagram of simple and expanded reproduction**.[2]



[2] This diagram has previously been handed out to the class.

Recall the two meanings of 'wealth' as (1) objects of real material wealth and (2) socially recognised means of command over those objects.

Related to this, the two meanings of 'value' in ordinary language:

(1) Utility (value in use, or 'use-value')

(2) Value in exchange ('exchange value', or value as command over objects of utility).

> *Example: the expression 'value for money'. What does it mean?*
>
> *And what about 'the value of money'?*

The distinction is vital if we are to have any clarity in our analysis. Adam Smith wrote in *The Wealth of Nations*:[3]

> The word VALUE, it is to be observed, has two different meanings, and sometimes expresses the utility of some particular object, and sometimes the power of purchasing other goods which the possession of that object conveys. The one may be called 'value in use'; the other, 'value in exchange'. The things which have the greatest value in use have frequently little or no value in exchange; and, on the contrary, those which have the greatest value in exchange have frequently little or no value in use.

(In other words, the question of real material wealth and the question of entitlements to that wealth must be kept distinct.)

When we use the word 'value' from now on, without further specification, we shall be referring only to value in exchange. To avoid confusion, we'll use the term 'utility' when we want to refer to what Smith, Marx and others have called 'value in use' or 'use-value'.

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Why do we need a value theory?

Mainly for two reasons:

(1) Because, even if we assume an equilibrium of supply and demand, and therefore an equilibrium price, in the case of every product, we still know nothing about the *relative* equilibrium prices — i.e. the prices of the various products *relative* to each other. We need a theory of the *value* of products in order to understand **the basis for their relative *prices***.

(2) Because, if there is a social surplus, it follows that a component of the *value* of each product sold — and consequently a component of the producer's revenue — will be made up of *'surplus-value'*. We need to know **the effective basis on which, in a market**

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[3] The *Wealth of Nations* (1776), Random House Modern Library edn., 1937, Chapter IV, p. 28. Some 25 years before Smith, the Physiocrat François Quesnay wrote that 'we should not confuse the price of items of exchangeable wealth with their use value, for these two values rarely have any connection with one another.' From his *Encyclopédie* article on 'Men'; translation by Ronald L. Meek, *Economics of Physiocracy: Essays and Translations*. George Allen & Unwin, 1962, p. 90.

economy, society allocates its aggregate surplus by giving a value to each product, and thus allocates and distributes the surplus among the enterprises which have contributed to producing it.[4]

Let's recall that the social surplus is

> **'that part of the total production which [does] not have to be consumed in order to maintain the existing level of production'**.[5]

The social surplus is first allocated at the base of the economy — i.e., allocated to productive enterprises themselves — when the product they have produced (including their contribution to the aggregate surplus product) is exchanged for money in the market. The **return of capital** to the enterprise and the **allocation of surplus-value** to the enterprise is effected simultaneously by means of the **price**.

In our simple model of a single-product CORN economy, with a single input (corn, feeding the producers and providing the seed), and with an annual cycle of production, it was easy to identify and quantify **the surplus product**: net bags of corn.

In a modern economy with a complex division of labour, with billions of different products coming onto the market at different times, **we cannot pin the physical surplus down in the same way**. We can only study it indirectly, by accounting for the **money-value** of all the outputs produced (and sold) during a fixed period of time, and deducting the money-value of all the inputs consumed in production during that time. So we look to *the realm of entitlements* in order to give us some aggregate sense of that quite different thing: *the realm of real material wealth*.

Enterprises keep account of their own **input costs** and **output revenues**. (Revenue means income from sales.)

Enterprises do this:

(a) to be sure they are making a profit not a loss;

(b) to work out what their rate of return (rate of profit) is on capital, so that they can decide whether to continue in that line of business, and even expand it, or rather pack up and invest the capital elsewhere;

and

(c) because the collector of taxes (e.g. SARS) requires proper accounting in order to tax the profit made.

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[4] An enterprise's contribution may be indirect, inasmuch as its product may have made a necessary, integral contribution to a rising social product, even though the quantum of the particular product of the particular enterprise sold into the market may not have increased. (The example of haircuts, discussed elsewhere, would serve to illustrate this.) If the revenues of the enterprise exceed its costs of production, that would indicate that society is awarding it a share in surplus over the period concerned.

[5] Frederic C. Lane, "Economic Consequences of Organized Violence". *The Journal of Economic History*, vol 18 no. 4, December 1958, p. 410.

The difference between the enterprise's **revenue** and its **cost of production** is its gross profit (or loss).

The results of all the different enterprises are then aggregated for general statistical purposes. This can be worked out nationally and also globally if the figures have been recorded.

A so-called 'real' economic result for a period is arrived at by adjusting this aggregate for changes in the value (purchasing power) of money compared with the previous period. But remember the 'Nordhaus' effect, which shows that the money-value statistics can't in fact fully capture the real advances made in the sphere of **utility**, or real material wealth.

We saw previously that **interest** and **ground rent,** as well as **taxes,** are paid out of **surplus**. More specifically, where each enterprise is concerned, they are paid out of the ***gross* profit of enterprise**. What remains is then the ***net* profit of enterprise**.

For present purposes, however, to simplify our analysis, we're going to leave aside the allocation of part of the surplus to interest, ground-rent and tax. We are interested primarily in **the gross value of the surplus product, and how it is allocated initially between the enterprises** which, collectively, have produced it.

The social product is in fact produced collectively, even though, in consequence of the division of labour between enterprises, each enterprise may think it has independently been doing its own thing.

Every exchangeable object of wealth has a **notional price** — the amount of money it is *expected* to fetch if actually exchanged. But one won't know its **actual price** unless and until it is actually exchanged for money. This is because supply and demand are in constant flux, and expectations are constantly having to be corrected.

Our present concern, however, is not with **all** exchangeable objects of wealth. Our concern is with **products — newly produced objects of material wealth — i.e. objects of utility.** These contain the newly produced **material surplus.**

When a product is exchanged for money — when it is sold in the market at a price — it is 'valorised'. That is to say, **its *value* is actualised or '*realised*'** in money**.** In this way, **actually realised prices allocate the social surplus** between enterprises at the moment when each enterprise exchanges its product for money.

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Adam Smith described the question of the value of commodities in exchange as one which is 'in its own nature extremely abstracted'.[6]

(In common English, a 'commodity' simply means an article produced for exchange. Nowadays, however, the word has also taken on a more specialised meaning, referring only to *primary* products such as coal, coffee, copper, wool, wheat and so on — where the individual article is submerged in a mass of articles of the same kind and quality, so that one ton, bag or bale can readily be substituted for another. But when Adam Smith or Karl Marx

[6] *Op cit.,* Chapter IV, p. 29.

spoke of 'commodities', they meant simply products destined for the market. We will be considering the value of 'commodities' in that sense, and, wherever possible, we'll simply call them 'products' to avoid ambiguity.)

In the history of economic thought, the theory of value has played an important and hotly contested role — because it sets out to explain (and thereafter to condemn or justify) the basis on which the production and appropriation of surplus-value takes place.

We cannot trace the whole history here, but will begin with **the mercantilist theory of profit** which dominated western economic thought for hundreds of years. Recall the period of merchant capitalism which we studied previously. The dominant theory of that period was that profit in the economic system came from buying and selling — **from buying cheap and selling dear**.

What do you think of that? [Divide into groups for 10 minutes to allow discussion of this question]

The Mercantilist theory of wealth and profit:

Buying cheap and selling dear:
the merchants' theory of profit:

From *An Outline of the History of Economic Thought*, by Ernesto Screpanti and Stefano Zamagni, Oxford University Press, 2nd edition, 2005, pp 41-42:

"It is not surprising that the mercantilists looked mainly to exchange as the real source of wealth and profit. In fact, the merchant earns profits, not because he controls the productive process (a control which, at least in the first phase of industrial development, was still in the hands of the craftsman), but rather because of the power he manages to exercise on the market. The merchant's profit originates from the difference between the selling and buying prices of goods. He believes, therefore, that it originates from the trading process. Thus a knowledge of the determinants of market prices is crucial in order to understand the origin and growth of profits. Attention must be mainly focussed on the forces that determine the demand for the goods, and demand is easily linked to utility.

cont...

"In 1588 Bernardo Davanzati made an interesting attempt to construct a utility theory of value. He had been impressed by a passage from the *Natural History* by Plinius in which a story is told of a mouse sold at a very high price during the siege of a city. Davanzati explained the phenomenon by arguing that the value of goods depends on their utility and rarity. It is not absolute utility that counts, but rather utility in regard to the quantity available. The effect of greater scarcity would be to increase the use value of the goods and therefore the price at which they can be sold."

However later, with the development of production for exchange:

"... the idea made ground that prices and profits reflected the conditions of production rather than the forces of demand."

(p 44)

Question:

What circumstances must we assume, if profit is to come generally from buying a thing cheap and selling the same thing dear?

There are two possible sets of circumstances to consider.

Question:

What circumstances must we assume, if profit is to come generally from buying a thing cheap and selling the same thing dear?

- **That the buying takes place in one market and the selling takes place in another market, where the conditions of supply and demand are different**

  This means that the demand is restricted but the supply is unrestricted in the first market, where the merchant buys; and the supply is restricted but the demand is unrestricted in the second market, where the merchant sells.

  The "terms of trade" between the two markets are unequal. The profit comes from the unequal terms of trade.

  This cannot continue when the markets are integrated and competition prevails.

Question (continued):

What circumstances must we assume, if profit is to come generally from buying a thing cheap and selling the same thing dear?

- **That the buying takes place in one market and the selling takes place in another market, where the conditions of supply and demand are different (see previous slide); or**

- **That the buying and selling take place in the same market but at different times, when the conditions of supply and demand are different.**

  This second possibility cannot provide a general explanation, because (assuming competition) the necessary conditions for buying cheap and selling dear can only exist in the same market temporarily and are equally liable to be reversed.

In an integrated competitive market, where production takes place for purposes of exchange, supply adjusts to changes in demand.

Therefore while, episodically, profit can be made from buying cheap and selling dear, this cannot provide a general explanation for the source of profit.

Whatever one gains in exchange, another loses. The (+) and (–) quantities cancel out.

Therefore the source of sustained profit in the system as a whole must be found in production, not in exchange.

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The Physiocrats

The 'Physiocrats' were a bourgeois modernising tendency — a school of thought — of the eighteenth century, located within and close to the aristocratic regime in France.[7] As economic modernisers but political conservatives, the Physiocrats looked both forward and back. They wanted major reforms to be carried out by the *ancien regime*. In this respect at least their project would be swept away in the French Revolution which overthrew the King and the landed aristocracy. But their forward-looking contribution was of great importance. The historian and translator Ronald Meek says that 'the birth of Physiocracy was in fact the birth of the science of economics in the broad general form in which it has come down to us today.'[8]

The Physiocrats were interested in the market — indeed they were pioneers of *laissez-faire* ['let it happen'] and free trade in opposition to the restrictive and protectionist theories of the Mercantilists — but they analysed the market from the point of view of **production**. Their aim was to promote policies which would expand production and, so they believed,

[7] They themselves would have objected to being called 'bourgeois', because they held the *urban* bourgeoisie in some contempt. They were promoting the development of *agricultural* capitalism, and so in that sense were objectively bourgeois. See e.g. Fox-Genovese, Elizabeth. *The Origins of Physiocracy: Economic Revolution and Social Order in Eighteenth-Century France*. Cornell University Press, 1976, pp. 27-30.

[8] Meek, *op cit*., p. 9.

alleviate the plight both of the impoverished small peasantry and of the rising capitalist farmers (the *fermiers*) who hired the land from the landlords.

The term 'physiocracy' comes from the Greek for 'government of nature'.[9] The Physiocrats maintained that nature — more specifically **the land** — was the sole source both of the means of subsistence **and of the surplus produced**. The **landowners** (i.e. the landlords, whose hereditary position they accepted as a natural right) were thus **entitled to receive the entire social surplus**. To be more precise, the Physiocrats recognised also the claims on surplus of the King (through taxes, which they wanted to reduce) and the clergy (through tithes, which they wanted to reduce or eliminate). In essence, however, **the surplus flowed to the landlords in the form of rent**. In the view of the Physiocrats, some of this surplus should be relinquished by the landlords so as to enable the *fermiers* to invest.

As Marx put it, the Physiocrats 'regarded rent as the only surplus, and capitalists and labourers together merely as the paid employees of the landlord'[10] — the landlords being naturally entitled to that position despite producing nothing at all. The French Revolution would reveal the absurdity of that notion of entitlement, also demolishing under the hammer-blow of events the extraordinary assertion of the Physiocrats that the landlords were a *necessary* class because, by using their rentals to buy agricultural and manufactured products, they in fact sustained these branches of production and thus the livelihood of all. Ruling classes have never been short of theorists to justify their exploitation. Or of conservative reformers merely trying to *persuade* the ruling class to give up some of its gains for the greater good of society.

In the Physiocratic conception, since the surplus was derived solely from the land:

> **the farmers** were the 'productive' class (they produced the surplus by working on the land);
>
> **the manufacturers** were the 'sterile' class (they could add nothing to the original surplus provided by nature, whatever quantity of manufactured goods they might produce); and
>
> **the landlords** were the 'distributive' class (who, by their consumption of the surplus product, which they paid for with unearned rent, ensured in effect the return of capital to its starting point, and so kept the annual cycle of production going).

François Quesnay (1694–1774) was the founder and leading light of the Physiocrats. His *Tableau Économique* (economic table), the classic for which he became renowned, was first published in 1758 when he was in his mid sixties. He was a medical doctor in the royal palace of Versailles: physician to Madame de Pompadour, surgeon-in-ordinary to Louis XV, and a martyr to gout.[11]

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[9] https://en.wikipedia.org/wiki/Physiocracy. Fox-Genovese, *op. cit.*, p. 9.

[10] Marx, *Theories of Surplus Value*, Lawrence & Wishart, 1969, vol 2, p. 162.

[11] J. R. McCulloch, 'Sketch of the Life and Writings of Francis Quesnay' in *Treatises and Essays on Subjects Connected with Economical Policy*, Adam and Charles Black, Edinburgh, 1853, p. 432.

Quesnay's father was an impecunious lawyer, and the family had lived as tenant farmers not far from Versailles in the Île-de-France. The boy had worked on the farm until becoming apprenticed to a village surgeon at the age of sixteen. Thereafter, by aptitude and application, he raised himself to prominence in the field of medicine, gained favour in the royal circles, and was rewarded with noble status by the king.

Quesnay studied the ideas of the Confucians which then predominated in China under the Qing (Ch'ing) dynasty. It was a period of relative prosperity in China, in which encouragement to peasant farmers was combined with low taxes.

Quesnay's basic argument went like this:

> [T]he wealth which constitutes the costs of agriculture differs greatly, as regards its employment, from industrial wealth. It is the former which causes revenue to be generated, whereas the product of industrial wealth is confined to goods which are worth only the expenses which they entail. The worker who makes a piece of cloth purchases the raw material and incurs expenses for his needs while he is making it. The payment he receives when he sells it returns him the purchase price and his expenses; the gain which his labour procures for him is confined to the restitution of the expenses he has incurred, and it is through this restitution that he is able to continue getting a living by his labour. The competition of workers who are trying to procure for themselves a similar gain in order to get a living restricts the price of manufactured goods to the level of this gain itself. Thus this gain, or restitution of expenses, is not, like the revenue of landed property, an original form of wealth representing a pure profit. On the contrary, this gain, even when it exceeds the restitution of the expenses, can exist only through the original and ever-renascent wealth which pays for the work of manufacture. Wealth in the form of manufactured goods is procured only through wealth in the form of revenue from landed property, and these goods in themselves constitute only sterile wealth which can be renewed only through the revenue of landed property. A nation subsists only through perpetual consumption and reproduction; the wealth which maintains a nation in being consists only in perpetual reproduction; thus sterile wealth, being simply wealth which is confined to consumption, is destroyed by consumption itself, and is unable, unless it is reproduced through other wealth, to perpetuate the existence of men and the successive existence of their wealth.[12]

Quesnay's conception of the economic linkages and the flows of value depicted in the *Tableau Économique* was, said Marx —[13]

> an attempt to portray the whole production process of capital as a *process of reproduction*, with circulation merely as the form of this reproductive process; and the circulation of money only as a phase in the circulation of capital; at the same time to include in this reproductive process the origin of revenue, the exchange between capital and revenue, the relation between reproductive consumption and final consumption; and to include in the circulation of capital the circulation between consumers and producers (in fact between capital and revenue); and finally to present the circulation between the two

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[12] From Quesnay's *Encyclopédie* article on 'Taxation'. Translation by Meek, *op cit.*, p. 105. Note that 'gain' here does not refer to a net product (or surplus) but to the producer's own living, which is part of the costs of production. Thus manufacturers 'gain' from producing, but no surplus accrues to them in principle.

[13] Karl Marx and Frederick Engels, *Collected Works*, International Publishers, *(MECW)* vol. 31, pp. 239-40.

> great divisions of productive labour — raw material production and manufacture — as phases of this reproduction process; and all this depicted in one *Tableau* which in fact consists of no more than 5 lines which link together 6 points of departure or return — [and this was] in the second third of the eighteenth century, the period when political economy was in its infancy—this was an extremely brilliant conception, incontestably the most brilliant for which political economy had up to then been responsible.

Here is the table from the first edition of the *Tableau Économique*:

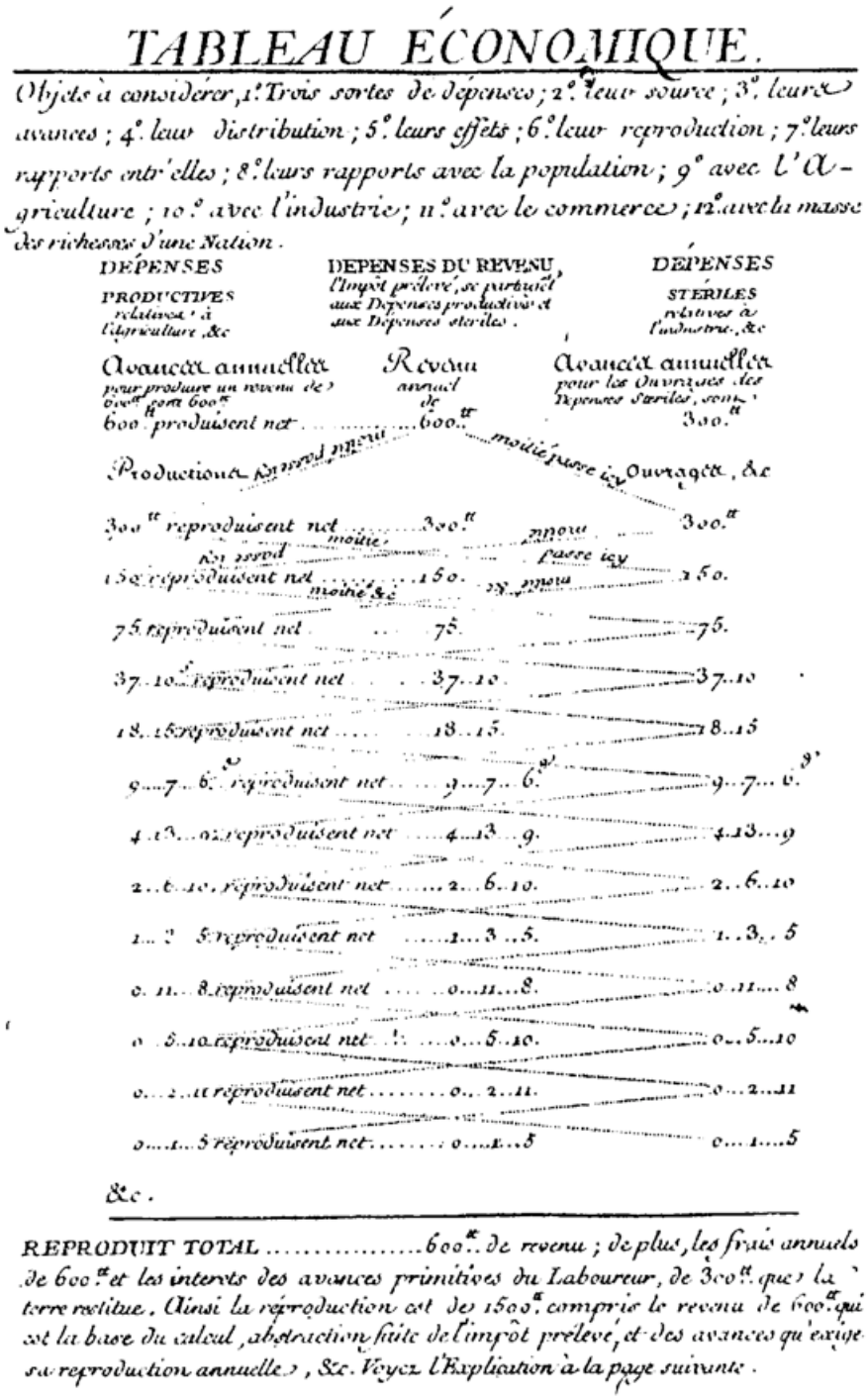


TABLEAU ÉCONOMIQUE.

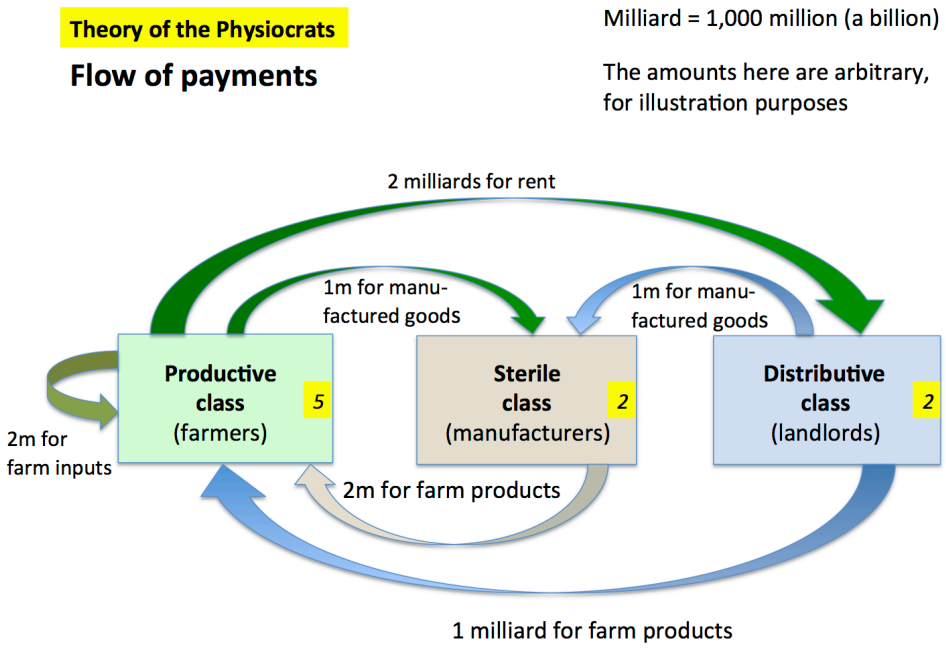
Objets à considérer, 1°. Trois sortes de dépenses; 2°. leur source; 3°. leurs avances; 4°. leur distribution; 5°. leurs effets; 6°. leur reproduction; 7°. leurs rapports entr'elles; 8°. leurs rapports avec la population; 9° avec l'Agriculture; 10°. avec l'industrie; 11°. avec le commerce; 12°. avec la masse des richesses d'une Nation.

DÉPENSES PRODUCTIVES relatives à l'agriculture, &c	DEPENSES DU REVENU, l'impôt prélevé, se partage aux Dépenses productives & aux Dépenses stériles.	DÉPENSES STÉRILES relatives à l'industrie, &c
Avances annuelles pour produire un revenu de 600 tt, sont 600 tt	Revenu annuel de 600 tt	Avances annuelles pour les Ouvrages des Dépenses stériles, sont 300 tt
600 produisent net	600 tt	
Productions	moitié passe ici	Ouvrages, &c
300 tt reproduisent net	300 tt	300 tt
150 reproduisent net	150.	150.
75 reproduisent net	75.	75.
37..10 reproduisent net	37..10	37..10
18..15 reproduisent net	18..15.	18..15
9...7..6. reproduisent net	9...7..6.	9..7...6.
4..13...9. reproduisent net	4...13..9.	4..13...9
2..6..10. reproduisent net	2...6..10.	2..6..10
1...3..5 reproduisent net	1...3..5.	1..3..5
0..11..8 reproduisent net	0...11...8.	0..11...8
0..5..10 reproduisent net	0...5..10.	0...5...10
0...2..11 reproduisent net	0...2..11.	0...2..11
0...1...5 reproduisent net	0...1...5	0...1...5

&c.

REPRODUIT TOTAL ..... 600 tt. de revenu; de plus, les frais annuels de 600 tt et les interets des avances primitives du Laboureur, de 300 tt que la terre restitue. Ainsi la reproduction est de 1500 tt compris le revenu de 600 tt qui est la base du calcul, abstraction faite de l'impôt prélevé, et des avances qu'exige sa reproduction annuelle, &c. Voyez l'Explication à la page suivante.

We can simplify it by means of the following diagram:



Adapted from the diagram in *An outline of the history of economic thought* (2nd ed., p. 57) by Screpanti and Zamagni

The **basic fallacy** of the Physiocratic conception comes to light when one considers the question of **economic growth** — the very thing they were concerned to promote. If the extent of agricultural land is not increased, an increased agricultural product on a sustained basis can only come from additional investment in raising the productivity of the same land. **And where would that investment come from, if not from surplus? Similarly, how would manufacturing expand except by the investment — in fact the *re*investment — of surplus?** The Physiocratic conception could only account for expanded investment on the assumption that the landlords were relinquishing to the farmers and manufacturers a part of the surplus naturally due to themselves. Since such an assumption was hardly plausible, and since the whole system of production for exchange was expanding spontaneously through reinvestment, the basic Physiocratic dogma could not stand.

However, in Marx's view the Physiocrats were correct in seeing all production of surplus-value, and thus also every development of capital, as resting on the productivity of agricultural labour as its natural foundation:[14]

> If men are not even capable of producing more means of subsistence in a working day, and thus in the narrowest sense more agricultural products, than each worker needs for his own reproduction, if the daily expenditure of the worker's entire labour power is only sufficient to produce the means of subsistence indispensable for his individual needs, there can be no question of any surplus product or surplus-value at all. A level of productivity of agricultural labour which goes beyond the individual needs of the worker is the basis of all society, and in particular the basis of capitalist production, which releases an ever growing part of society from the direct production of

[14] Marx *Capital*, vol 3 (Penguin edition), p. 921.

> means of subsistence, transforming them, as [Sir James] Steuart says,[15] into 'free hands' and making them available for exploitation in other spheres.

Economic development has rested historically on producing an agricultural surplus and applying it to investment in industrial production.

However, is was **a fundamental fallacy** for the Physiocrats to maintain that nature does **not** add to the physical product and the physical surplus when **manufacturing** production takes place. As Marx puts the matter in *Capital*,[16] the physical bodies of commodities

> are combinations of two elements, the material provided by nature, and labour. ... When man engages in production, he can only proceed as nature does herself, i.e. he can only change the form of the materials. **Furthermore, even in this work of modification he is constantly helped by natural forces.** As William Petty says, labour is the father of material wealth, the earth is its mother.

The sentence highlighted in yellow provides the answer to the Physiocrats' idea that manufacturing is 'sterile' when it comes to the production of the social surplus — even on the basis of their own assumption that external nature alone provides the surplus product. But in fact this assumption is mistaken. It is **nature + labour** that generates the product, including the surplus product. But more of that in due course.

'It was an immense step forward,' writes Marx in the *Grundrisse*,[17] 'for Adam Smith to throw out every limiting specification of wealth-creating activity — not only manufacturing, or commercial or agricultural labour, but ... labour in general.' Whereas the Physiocrats had advanced what was essentially a 'land' theory of value — or, if you prefer, a 'land + agricultural labour' theory of value[18] — Adam Smith articulated a value theory based on

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[15] Steuart, *An Inquiry into the Principles of Political Economy*, vol. 1, Dublin, 1770, p. 396.

[16] Marx, *Capital*, vol 1 (Penguin edition), pp. 133-4. Emphasis in bold type added.

[17] Penguin edition, p 104.

[18] It can be argued that the Physiocrats advanced a *'land + agricultural labour'* theory of value insofar as, in their conception, agricultural labour participates uniquely in the production of surplus from the land. However, it is difficult to sustain that argument consistently. To go into the matter fully is beyond the scope of this course — a brief note will have to suffice. First, there is a problem in thinking that the Physiocrats singled out agricultural labour when it came to creating 'value'. Second, it is by no means clear that the Physiocrats regarded labour of any kind as itself *creating* 'value' at all.

As to the first difficulty: Quesnay in fact makes no distinction between agricultural and non-agricultural labour when it comes to contributing 'value' in exchange. The only distinction he makes between agricultural and manufactured products in this regard is that in the case of the former the nation gains not only the 'value' of the labour expended, but 'also the value of the materials produced by the land. Thus ... trade in raw produce is always proportionately much more advantageous' in value terms. (Passage from Quesnay's *Encyclopédie* article on 'Corn', translated in Meek, *op cit.*, pp. 74.) His point is simply that, in the case of manufacturing, there is no addition of materials from nature, but only a further refinement or elaboration of the original materials.

As to the second difficulty: Quesnay insists that *only* the land provides the surplus product (the *produit net*). But, in physical terms, the *net product* can only be what remains of the *gross product* after some of the latter has been *consumed* or set aside for consumption. In that case, how could the land be the sole source of the *net* value product unless it has first been the sole source of the *gross* value product? On this approach, agricultural labour is to be treated simply as a cost of production to be deducted from the gross value product of the land. At the same time, inconsistently, Quesnay treats costs of production as a component of the exchange value of all products. (In the case of manufacturing, it is the sole component, in his view, since no additional surplus can be produced there.)

Thus his value theory seems to vacillate uneasily between two unsatisfactory conceptions: on the one hand, a

productive labour in general.

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Adam Smith was by no means the first to rely on a 'labour' theory of value, but he gave it what has since been regarded as its classical expression. In *The Wealth of Nations* (1776) he began his famous exposition of value theory with these resounding words:

> Every man is rich or poor according to the degree in which he can afford to enjoy the necessaries, conveniencies, and amusements of human life. But after the division of labour has once thoroughly taken place, it is but a very small part of these with which a man's own labour can supply him. The far greater part of them he must derive from the labour of other people, and he must be rich or poor according to the quantity of that labour which he can command, or which he can afford to purchase. The value of any commodity, therefore, to the person who possesses it, and who means not to use or consume it himself, but to exchange it for other commodities, is equal to the quantity of labour which it enables him to purchase or command. Labour, therefore, is the real measure of the exchangeable value of all commodities.
>
> The real price of everything, what everything really costs to the man who wants to acquire it, is the toil and trouble of acquiring it. What everything is really worth to the man who has acquired it, and who wants to dispose of it or exchange it for something else, is the toil and trouble which it can save to himself, and which it can impose upon other people. What is bought with money or with goods is purchased by labour, as much as what we acquired by the toil of our own body. That money or those goods indeed save us this toil. They contain the value of a certain quantity of labour which we exchange for what is supposed at the time to contain the value of an equal quantity. Labour was the first price, the original purchase-money that was paid for all things. It was not by gold or by silver, but by labour, that all the wealth of the world was originally purchased; and its value to those who possess it, and who want to exchange it for some new productions, is precisely equal to the quantity of labour which it can enable them to purchase or command.[19]

A person's fortune is greater or less, Smith went on,

> precisely in proportion to ... the quantity either of other men's labour, or, what is the same thing, of the produce of other men's labour, which it enables him to purchase or command. The exchangeable value of everything must always be precisely equal to the extent of this power [to purchase or command] which it conveys to its owner.[20]

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physical substance theory of exchange-value, in which the substance of all exchange-value is at root solely the contribution of the land; and, on the other hand, an *adding-up* or rather *subtraction* theory of exchange-value, in which the *entitlement* of the producer to recover his costs forms one component and the *entitlement* of the land (in the person of the landowner) forms the remainder (the remainder being surplus-value). But before you can have a *remainder*, you must have a *total* — and how does one get to that? Moreover, how does one choose between these mutually contradictory alternatives? Since the fundamental feature of the Physiocratic doctrine is that the land is the sole contributor of surplus-value, it seems better to see their value theory in essence as a land-substance theory. We may note here in passing that Quesnay failed to observe his own earlier admonition to keep the physical product and its utility distinct from its value in exchange (see n 3 above).—RP

[19] Smith, *op cit.,* Chapter V, pp. 30-31.

[20] *Id.*, p. 31. Smith was here referring to 'exchangeable value' which corresponds to 'real' or 'natural' price as he conceived it, and which is not by circumstances raised above or depressed below that mark.

The whole foundation of Smith's conclusion is his premise that, once the division of labour has thoroughly taken place, everyone is obliged to live by the exchange of *labour products*. Yet surely this premise is gravely flawed. It is in reality not labour alone, but rather *external nature and labour together*, which provides the greater part of the 'necessaries, conveniencies and amusements of human life'. Few of these are ever provided by labour alone.

While it is true that we must derive the far greater part of the things we need or want from the labour of other people rather than from our own labour, it does not follow that we must be rich or poor according merely to the quantity of *labour* commanded. In fact a person is rich or poor according to the quantity of *products of nature and of labour* which she or he can command or afford to purchase.

The question necessarily arises: who commands the contribution made by nature to the production of a commodity, and on what basis is it commanded? The answer is surely that the *owner* of the contribution commands the contribution — the basis being the social recognition of the proprietary entitlement.

It is no accident that, in Smith's value theory, *property itself is reduced at first to being a product of labour:*

> Labour was the first price, the original purchase-money that was paid for all things. It was ... by labour, that all the wealth of the world was originally purchased.

Surely not so. Even a study of barter, of the earliest episodic exchanges of surplus products, would not sustain this assertion.[21]

The whole long and often turbulent development of class and caste; of the seizure by conquest of land, implements, crops, herds and people; of tribal and national aggrandisement; of ancient slavery and feudal serfdom; of clearances and other means of primitive accumulation; of the colonisation of continents and peoples — the very stuff of the materialist conception of history — speaks against it. As a theory of the origin of property, and also of the evolution of property, it is demonstrably one-sided and accordingly false.

The 'division of labour', as we have seen, is in reality also a division of the materials upon which labour works, and of the implements with which it works. If there is a division of entitlements to the products of labour, there is presupposed a division of entitlements to the various contributions made by nature to those products. As Marx and Engels put it in *The German Ideology*:[22]

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[21] See David Graeber, *Toward an Anthropological Theory of Value : The False Coin of Our Own Dreams*, Palgrave Macmillan, 2001, pp. 153-154: '[Marcel Mauss] notes that, contrary to the speculations of the likes of Hobbes, or Adam Smith, or modern economists, the first voluntary, contractual relations were not between individuals but between social groups: "clans, tribes and families". ... It has often been noted that when something resembling barter *does* occur in stateless societies it is almost always between strangers, people who would otherwise be enemies.' Cf also Michael Mann, *The Sources of Social Power*, vol 1, Cambridge University Press, 1986, pp. 41-46.

[22] 'The German Ideology', in *MECW*, vol 5, at p. 86.

> The division of labour implies from the outset the division of the *conditions* of labour, of tools and materials, and thus the fragmentation of accumulated capital among different owners, and thus, also, the fragmentation between capital and labour, and the different forms of property itself.

Marx would later rebuke the German Social Democrats for stating in their program of 1875 that 'labour is the source of all wealth'.[23]

> Labour [wrote Marx] is *not the source* of all wealth. *Nature* is just as much the source of use values (and it is surely of such that material wealth consists!) as labour, which itself is only the manifestation of a force of nature, human labour power. The above phrase is to be found in all children's primers and is correct insofar as it is implied that labour is performed with the appurtenant subjects and instruments. But a socialist program cannot allow such bourgeois phrases to pass over in silence the *conditions* that alone give them meaning. And insofar as man from the beginning behaves toward nature, the primary source of all instruments and subjects of labour, as an owner, treats her as belonging to him, his labour becomes the source of use values, therefore also of wealth. The bourgeois have very good grounds for falsely ascribing *supernatural creative power* to labour; since precisely from the fact that labour depends on nature it follows that the man who possesses no other property than his labour power must, in all conditions of society and culture, be the slave of other men who have made themselves the owners of the material conditions of labour. He can only work with their permission, hence live only with their permission.

Therefore, to correct Adam Smith, we would have to say this:

After the division of labour has once thoroughly taken place it is but a very small part of the 'necessaries, conveniencies, and amusements of human life' *which a person's own labour and own command of nature's contribution* can supply to him or her. The greater part, certainly, must be obtained by entering regularly into relations of exchange. It is by means of exchange that the product of *others' labour and of others' command of the contribution of nature* can be obtained.

If we had more time, which we don't, we could pursue the argument and see in detail how Adam Smith himself was driven to depart from his own 'labour-value' theory as soon as he analysed the workings of a society **in which land has been appropriated and 'stock' (implements, machinery etc) accumulated** — in other words a society characterised by **unequal property**. He then began to see exchange-value as made up rather of what are really property-based *distributive shares*. But he failed in the end to present a consistent value theory.

The conception that 'labour-value' — the labour-content of products — is the social substance that constitutes the exchange-value of those products, **comes down to a purely dogmatic assertion**. The premise advanced by Smith for that assertion was mistaken. David Ricardo followed Smith in adhering both to the premise and to the assertion. Marx rejected the premise, yet maintained the assertion; we shall examine in due course whether he was able to support that assertion on other grounds.

Next time: **Marx's theory of value and exploitation.**

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[23] 'Critique of the Gotha Program', in *MECW*, vol 24, p. 81.