Question about the 'Falling Rate of Profit' Theory

[This is a query from a friend on March 26, 2010, and my response. –S.H.]

Sent: Friday, March 26, 2010
Subject: question about economics

Hi Scott. I was trying to remember something you might have said about the tendency for the rate of profit to fall and its relation to overproduction. Do you agree with the former? I can't quite remember what it even means. Could you point me to something to refresh my memory please?

L.

[Scott's Response, also on March 26, 2010:]

Hi L---,

Well, regarding the "tendency for the rate of profit to fall" as a (or "the") cause of capitalist economic crises, opinions among Marxists differ tremendously!

Marx himself has three major theories of crisis:

1) The *overproduction of capital* [because: A) the growth of the market cannot keep pace with the growth of production, and so the capitalists have all this excess surplus value around; and B) because they extend credit to consumers and the government, which artificially expands the market for a time; and therefore C) because they build up the means of production to a much greater extent than is actually rational.] When the debt bubble starts to pop in the form of a financial crisis (as it is doing at present), the whole precarious edifice crashes down in an overproduction crisis.

2) The *anarchy theory* [that the capitalists produce not in accordance with an overall production plan, but more or less blindly because they do not know what the real market will be in the future and how much the other capitalists will produce]. This is at most only a very secondary cause of crises (and in some ways actually serves to postpone crises, because it leads to waste and other forms of production that would not otherwise occur). Nevertheless, some Marxists (following Lenin's early writings) unaccountably view this as the major cause of economic crises.

3) The *falling rate of profit theory*. Marx talks about this in 3 chapters of Vol. III of *Capital*. The basic idea here is that profits (from the generation of surplus value) only come from the direct exploitation of labor, and not from machinery. [This is already wrong in my view—though this is a rather heretical

view—since I believe that machinery allows the continued exploitation of *past* labor in the form of machines in the *present* production process. For more on this see some of my essays and letters on the labor theory of value in the political economy section on www.massline.org.]

Anyway, the way Marx sees it, the capitalists constantly increase the proportion of machinery to labor (or in other words, constantly increase the value of "constant capital" [machinery, etc.] relative to "variable capital" [labor power] in the production process). Marx calls this the general increase in the "organic composition of capital". Supposedly, since profits only come from the direct exploitation of labor, and since labor itself makes up an ever decreasing part of their total capital, there is a strong overall tendency for profits to fall over time.

Marx does talk about a variety of countervailing tendencies which very much cloud the issue. One such, for example, is to greatly increase the rate of extraction of surplus value, which becomes feasible in part because of the much increased productivity that the new machinery allows. There are disputes within Marxist economic circles about whether these "countervailing factors" might actually overpower any tendency for the rate of profit to fall! Marx by no means *proves* that this supposed overall tendency will dominate in the long run, though he *argues* that it will.

And there is actually some rather good empirical evidence that during boom periods, at least, profits do go way up. This is not what the theory of the tendency of the rate of profit to fall would predict.

Of course, when a financial crisis looms and breaks out, and leads to a general overproduction crisis, profits do in fact fall tremendously. But the question is: Is this cause or effect? I think it is just an effect; that is, a result of the overproduction of capital and the supersaturation of all markets for commodities, which leads to falling sales, expenses in shutting down factories, and so forth.

In my view, the overproduction of capital is the basic explanation of overproduction crises (and, indeed, why they are properly *called* overproduction crises in the first place). There is some limited secondary validity to the anarchy theory, but the falling rate of profit theory is just plain wrong. But, as I say, many other Marxists who have investigated political economy go with one of the other 3 theories, or even yet more theories.

That's why Marxist crisis theory is such an overall mess even to this day!

Scott