

Will Marx Be Proved Right?

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A centrepiece of Marx's analysis of capitalism was that there would be a declining share for labour in national income. He argued that labour saving capital investment would systematically hold back the growth of the demand for labour, whilst the erosion of small-scale and precapitalist producers, in agriculture for example, would swell the labour supply. The result was a permanent "reserve army of labour" which, though fluctuating with the economic cycle, would be sufficient to prevent real wages growing as fast as labour productivity. Workers would thus spend an increasing proportion of working time producing surplus for capitalists and landlords rather than their own means of subsistence – a rising rate of exploitation in Marx's terminology. Leaving aside the political implications, such a rising rate of exploitation threatened stagnation unless capitalists were prepared to invest an increasing share of national income.

Labour's Share -The story thus far

Striking calculations by Bob Allen² have recently suggested that labour's share was indeed declining in the UK in the decades prior to the publication of Volume I of *Capital*. For a century or so thereafter labour's rose somewhat in the UK according to Feinstein's calculations, reflecting the growth of trades unions, political democracy and relatively high employment³. Of course there are a host of issues concerning how it should be measured, especially now that the welfare state collects taxes, redistributes them and provides services. Nevertheless the pre-tax wage share is still important as an indicator of how the immediate proceeds from production are distributed.

The notorious "profits squeeze" in many OECD countries in the later 1960s and 1970s symbolised an ebbing of the power of private ownership and management on a broad front. The subsequent quarter century has seen labour's incursions beaten back through macroeconomic stabilisation, the reassertion of "shareholder value", and privatisation⁴. Labour's share has receded markedly throughout much of Europe, as Figure 1 illustrates for the case of the UK where Mrs Thatcher pursued the new policies so forcefully. Unemployment has played a prominent role in this process by facilitating the weakening of organised labour. Even so labour's share in Germany, France and Italy as well as the UK has only declined towards the "normal" level of the 1950s; nothing yet which could yet be interpreted as the systematic downward trend predicted by Marx. The case of the USA shown in figure 1 is particularly striking as there has been no obvious shift back to capital at all thus far⁵. But could this be about to change?

¹ This is a slightly edited version of a paper published in *Oxonomics* Vol 1 Issue 1 (2006).
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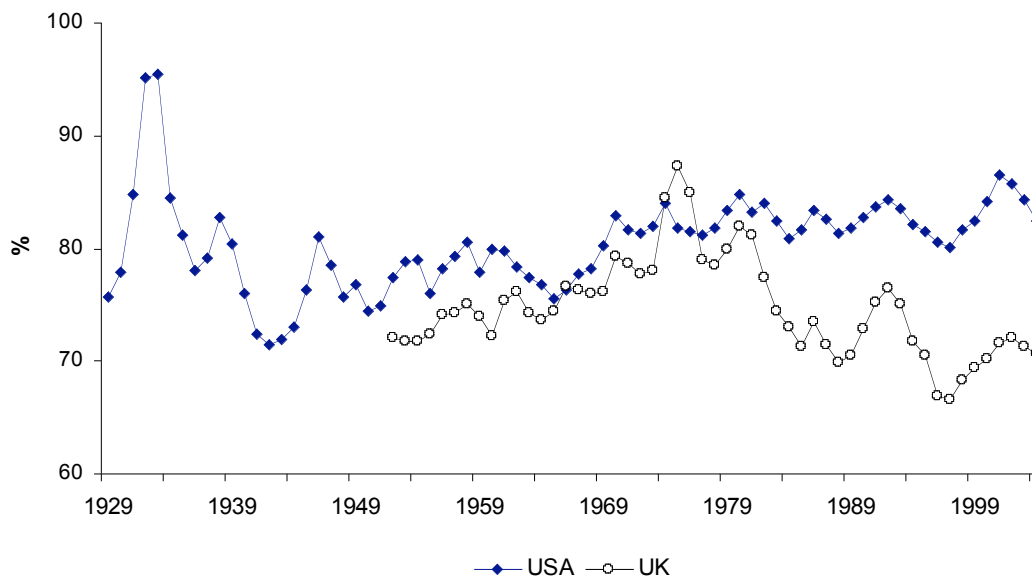
² R.Allen (2005) "Capital Accumulation, Technological Change and the Distribution of Income in the British Industrial Revolution" Oxford University Dept of Economics Working Paper No 239

³ R.Matthews, C Feinstein & J.Odling Smee *British Economic Growth 1856-1973*, Stanford (1982) chapter 6.

⁴ This process is recounted in A. Glyn *Capitalism Unleashed* OUP (2006).

⁵ This conclusion requires serious qualification. The profits of financial companies have been excluded because it is very tricky to integrate them in this national accounting framework. These have been rising dramatically in the USA (see Glyn 2006 chapter 3). Moreover there have been spectacular increases in the very highest echelons of

Figure 1 Labour's Share 1929-2004
 (% of net value added of non-financial companies)



Source: Bureau of Economic Analysis NIPA Accounts, ONS Blue Book tables linked to Armstrong et al (1991). Note in these series labour's share is employee compensation as percentage of net value added; that is after deduction of capital consumption.

China and a Global Reserve Army of Labour

The *Communist Manifesto* proclaimed the spread of capitalism across the globe in the most unequivocal terms:

“The need of a constantly expanding market for its products chases the bourgeoisie over the entire surface of the globe. It must nestle everywhere, settle everywhere, establish connections everywhere. The bourgeoisie has, through its exploitation of the world market, given a cosmopolitan character to production and consumption in every country.”

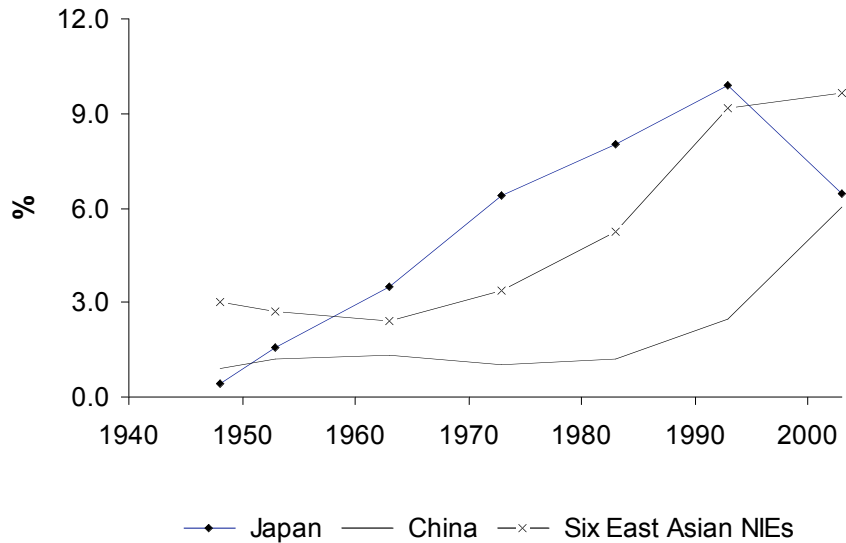
The headlong expansion of capitalism in China, with India joining the charge, seems to be finally bringing Marx and Engel's prediction to completion. What are the implications for workers in the rich countries?

At first glance the eruption of China into the world economy seems to be just the latest example of Asian countries “catching up” with the leading industrial powers (see Figure 2). China's

“labour incomes” (CEO compensation most notoriously) and these should really be included in profits rather than labour's share (see the data in R. Gordon 2005 “Where Did the Productivity Growth Go?” NBER Working Paper 11842).

export growth has been spectacular of course, but so was that of Japan and the Asian tigers in earlier decades.

Figure 2 Asian Shares of World Exports (%)

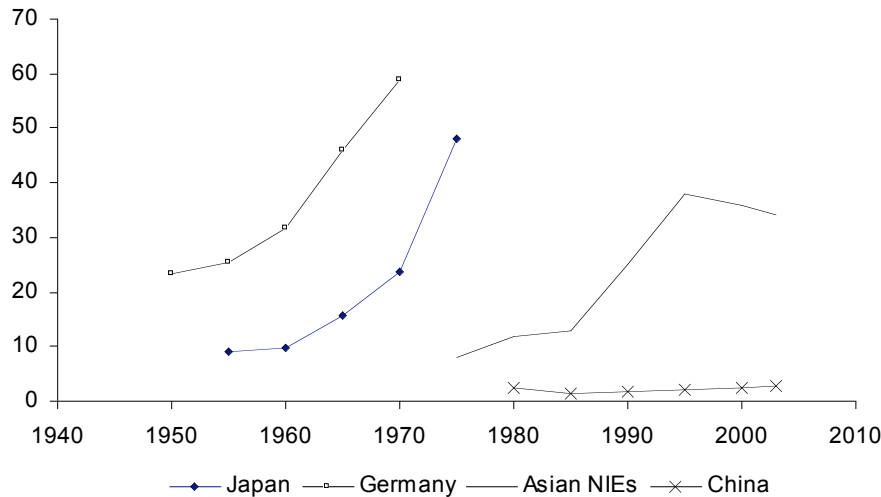


Source:WTO.

What makes China (and India) fundamentally different is the presence of vast reserves of labour previously isolated from the world economy by economic backwardness and autarky. Total employment in China is estimated at around 750 million, or about one and a half times that of the whole of the OECD and nearly ten times the combined employment of Japan and Korea. About one half of China's employment is still in agriculture. This represents an enormous potential labour supply. Estimates of the numbers who may be pulled out of agriculture, where their incomes are very low, into industrial and service jobs in the towns range as high as 150- 300 million depending on the time scale. These, together with tens of millions of urban underemployed, constitute a reserve army of labour of quite unprecedented magnitude.

The contrast between China's trajectory and the earlier episodes of "catch-up" is shown most starkly by what is has been happening to wages. Figure 3 shows that China started its growth spurt with far lower manufacturing wages than were found in the earlier stars of post-1945 growth – Germany, Japan and the Asian tigers. Moreover China's wages have barely risen at all in dollar terms as compared to the US level, despite more than two decades of extremely rapid economic growth.

Figure 3 Manufacturing wages during catch-up, USA=100



Source: Bureau of Labor Statistics and author’s calculations

Although the millions of migrant workers in China’s export factories seem hardly to have benefitted, average real incomes have been growing in the towns. However in the 1980s and early 1990s the Chinese Yuan was successively devalued and this prevented wages rising much in dollar terms. In 2002 manufacturing wages were still estimated at less than 3% of the US level⁶. Now, however, there is now pressure for Yuan revaluation which would push up dollar wages, amplifying the effect of domestic cost increases. However starting from such a low base, even compound interest grinds exceedingly slowly. If dollar wages grew some 6% per year faster in China than in the USA over the next two decades, Chinese wages would still only be *one tenth* of the US level by 2025.

What is the implication for workers in the North of the integration into the world economy of vast labour reserves. Much attention has naturally been devoted to effects through international trade. What will Northern workers displaced by Southern imports do? What will the North be able to sell to pay for the ever rising tide of manufactures and services produced with much lower wages in the South? Sustained revaluation of Southern currencies will relieve competitive pressure on Northern producers, but by the same token consumers in the North will no longer be paying such low prices for imports.

Although such issues are serious enough there is another more ominous possibility. What if there was a major drain of real investment spending from the North to the South? Thus far the extraordinary burst of capital accumulation in China – capital stock growing at 10% per year, some four times as fast as in the North – has come almost entirely from domestic sources. China takes a large chunk of total Foreign Direct Investment in the South but it still represents only one tenth of Chinese domestic investment. The total FDI inflow to the South in 2004 (mostly from

⁶ J. Bannister “Manufacturing earnings and compensation in China”. *Monthly Labor Review* August 2005. 22-40.

the North) was only 3-4% of Northern domestic investment in that year. The feeble capital accumulation in the North of recent years cannot be blamed on an investment outflow to low wage countries. It is just not large enough.

But could the trickle of FDI from North to South turn into a flood? TV pictures of the machinery at Birmingham's huge Longbridge car plant being packed up for shipment to China may be an extreme case. However as Richard Freeman⁷ has argued China is producing large numbers of highly trained but still relatively cheap workers so that its production possibilities are not confined to low wage unskilled work. With very low wage costs in China, and cheap transport and communication, why should Northern producers continue investing to maintain their capital stock in the North, let alone extend it? If investment peters out where would Northern workers find jobs? When Longbridge closed a government minister was ill-advised to suggest that the car workers could seek jobs at Tesco's. Hardly a comforting response.

It is not too far fetched to imagine a long period of capital stock stagnation in the North, because investment in the "emerging markets" is much more profitable. This could bring intense pressure on the jobs and working conditions of Northern workers, with even the sectors where relocation is not possible (retailing, education, public administration for example) flooded with job seekers. The bargaining chips would be in the hands of capital to a degree not seen since the industrial revolution. The stylised fact of labour's share fluctuating in the 2/3 to 4/5 range could disappear too, with Marx's rising rate of exploitation emerging, a century and a half after he first predicted it.

At the macroeconomic level a declining share for labour poses nasty questions. As Malthus originally noted, who is to purchase the output which workers are unable to buy (in this case an increasing share of national output? If domestic investment is weak, as discussed above, demand could be maintained by some combination of:

- (a) a rising share of taxation from profits and other high incomes used to finance expansion of collectively provided services such as health, education and care for the elderly;
- (b) increased luxury consumption from those in receipt of rising profit incomes or rising wages at the top of the pay distribution.

The distributional implications of these alternative patterns are very different. In the first case an increasing proportion of society's resources would be devoted to providing for collective needs. In the second case an increasing share of the less qualified would be providing non-tradeable services for the wealthy elite⁸.

⁷ Freeman, R. (2005) "What Really Ails Europe (and America): The Doubling of the Global Workforce" The Globalist www.theglobalist.com June 3

⁸ Alan Manning has found that the job prospects of the less qualified in the USA depend on the number of better off consumers in their city. See "We Can Work it Out: The impact of Technological change on the demand for Low Skill Workers" CEP Discussion Paper No 640, June 2004.

The fundamental point is that the emerging trends in the world economy seem destined to return to centre stage the most important question for classical economists – how will the distribution of incomes evolve and what are the economic and political implications.