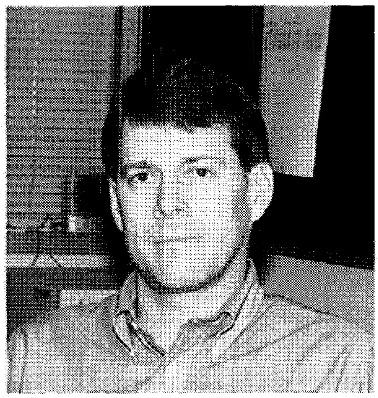
Rethinking the Profit Motive

Roger Terry



Roger Terry is the editor of Exchange, *the award-winning alumni magazine of the Marriott School of Management at Brigham Young University. He was a faculty member at the Marriott School for nine years. He is cofounder and president of* the funcompany, *a business that designs and markets unorthodox day planners, produces books, and offers various editorial services to businesses and individuals. His most recent book is* Economic Insanity: How Growth-Driven Capitalism Is Devouring the American Dream *(Berrett-Koehler, San Francisco, 1995).*

The most fundamental assumption of capitalism is endless economic growth. Growth is not only the prescribed cure for all our economic woes, it is the driving force, the engine, that makes capitalism work. On the surface, the theory goes like this: As the individual parts and pieces of the capitalist economy generate profit and reinvest a portion of it to increase productive capacity, they grow, and so does the overall system.

This reinvested profit is called capital, and without it, there is no capitalism. Capitalism, we might say, is a *growth system.* If it does not grow, it dies. The economy may shrink during recessionary cycles, but the ensuing rebound always more than compensates for any backtracking that has occurred.

Capitalism is, by definition, a system in constant pursuit of profit. Profit is capitalism's food, the air it breathes. But where, we might ask, does profit come from? This question is not as simple as it appears. To varying degrees, even the great worldly philosophers were perplexed by it and, curiously, only three reasonable answers were ever put forward: one by Karl Marx, another by Joseph Schumpeter, and a third by Thorstein Veblen. Even the venerable Adam Smith wavered on this question between two possible answers.

For a more detailed examination of the three theories, I recommend Robert Heilbroner's classic, *The Worldly Philosophers*,[1] but for the purposes of this article let me try to fit these three explanations into a very small nutshell. Marx said, basically, that profit doesn't occur naturally in the capitalist system. Market forces drive profit from the system whenever it rears its ugly head, so the only way capitalists can extract a profit from their operations is to steal it from the laborers. This they do by paying workers less than their actual value.

To Joseph Schumpeter, by contrast, profit is not stolen into existence; rather, it comes honestly, from innovation. Whenever someone invents a new machine or new product, devises a production process, or improves quality, this allows the innovator to extract money from the flow of production and consumption—either because quality has increased and people are willing to pay slightly more, or because production has become more efficient and the capitalist's per-unit expenses have declined, yet can temporarily charge the traditional price for a product. Profit, to Schumpeter, is a temporary glitch in the flow of production and consumption. Before long, everyone's quality will increase or their costs will decline as they learn the new method or purchase the new machinery. Then profit is squeezed out of the system. So, constant, repeated innovation is necessary to produce continuous profit.

Thorstein Veblen offers yet another perspective. He saw the economic process "as being basically mechanical in character,... the machinelike meshing of society as it turned out goods." [2] If this is so, then where does the businessman fit in? The businessman, Veblen concluded, was basically a saboteur of the system who extracted a profit by disrupting it.

The system saw no other end except making *goods*. The businessman, however, was interested in making *money*. How did he do this? By causing "breakdowns in the regular flow of output so that values would fluctuate and he could capitalize on the confusion to reap a profit."[3] And how did the businessman cause these breakdowns? By creating the never-never-land of corporate finance. On top of the machinelike production apparatus, explains Heilbroner, "the businessman built a superstructure of credit, loans, and make-believe capitalizations. Below, society turned over in its mechanical routine; above, the structure of finance swayed and shifted. And as the financial counterpart to the real world teetered, opportunities for profit constantly appeared, disappeared, and reappeared."[4]

Each of these theories explains to a degree where profit comes from in the capitalist system. Each of these sources of profit, however, has social and economic effects that are destructive, perhaps even fatal, in the long term.

Debt-Driven Consumption

As Marx suggested, capitalists do indeed steal profits from employees by paying them less than they are worth, and this happens every day in the regular course of business. There are millions of underpaid individuals in organizational America—underpaid in the sense that they are unable to consume their share of overall production. And yet this must be so in the capitalist system. Why? For the simple reason that if businesses paid their employees enough so that they could purchase the exact amount of production they add to the economy, there would be, by definition, no profit, no excessive executive salaries and bonuses, and no dividends to stockholders. Let's examine this more closely.

Is it possible for one company—General Motors, for instance—to pay its employees enough so that they can buy all the cars GM produces in a given year? Of course not. If it did, then wages alone would *exceed* total revenue. (Remember, they must have enough *after-tax* income to buy the cars they produce.) GM has many expenses, and a good portion of these go to other businesses whose employees are, in a sense, GM employees, because they are dependent on General Motors' expenditures. So the question becomes: Can General Motors pay all these direct and indirect employees enough in annual wages so that they can purchase all the cars GM produces in a year? The answer is still no. And if we extend this analogy to include the entire economy, the answer remains no.

In an economy (the aggregate of all businesses in a nation or geographic region), the total annual income of workers, managers, and owners may be sufficient to purchase all the products generated by domestic businesses in a given year, but less than 100 percent of that income will be spent on consumption. A portion will be invested, either by corporations or by individual capitalists, back into the production process to increase productive capacity—to make the economy grow. In other words, we don't have enough disposable income in a given year to purchase all the products we have produced, and to make matters worse, next year there will be even more products that we can't afford.

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So, how do we buy all these products? And we do buy them, by the way. Indeed, for years now we have actually been purchasing more products than we produce, hence our repeated and increasing trade deficit. The answer to this paradox is really quite simple. The only way we can purchase more than we produce, when our wages represent a steadily decreasing portion of the system's total wealth, is to buy today's production with tomorrow's paycheck. Increasing consumer, trade, and national debt all contribute to our ability to consume well beyond our means. In essence, as the system grows, our ability to consume all that we produce is supported more and more by debt. And as we fall further and further behind in our ability to consume our production, the situation snowballs, because an ever-increasing portion of our income must go toward servicing our expanding debt. Such insanity cannot go on forever, of course.

"Clearly," writes Willis Harman, "to think of the many trillions of dollars of federal, municipal, corporate, and private debt in the United States alone ever being repaid is sheer fantasy. Since by far the greatest part of the money supply consists of currency or bank credit that has been borrowed into existence, it is impossible for people, in the aggregate, to get out of debt. To do so would require the repayment to primary lenders of more money than there ever is in existence."[5]

The Dilemma of the Postindustrial Society

In line with Joseph Schumpeter's view of profit, the new thinking regarding today's hypercompetitive global marketplace is that if we are to flourish or even survive, we need to achieve the impossible—somehow to come up with endless, brilliant, cheap innovation. If companies don't constantly reach new levels of innovation, they don't turn a profit, and they get left behind by competitors who *can* churn out innovation after innovation at an ever-accelerating pace.

One significant problem with accelerating technological innovation is the largely unspoken connection we've made between innovation-driven productivity growth and standard of living. We've been taught to assume that technological innovations and the economic growth they spur are constantly making our lives better. In fact, no such causal relationship exists. Although productivity has grown steadily over the past 25 years, primarily due to technological advances, our standard of living and real wages have actually stagnated or retreated.

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Our frantic push to increase productivity through new technological innovation is not improving our economic lot. Indeed, it may be argued that constant innovation is making us less and less able to purchase all the products we generate with our increased productivity.

The flaw in the productivity-or-bust doctrine is that new product and process technology tends to displace productive workers. Producing the items we need and want requires fewer and fewer workers with each passing year. Displaced workers are moved primarily onto welfare rolls or into the burgeoning service sector, where intense competition keeps wages at a much lower level than in the traditional manufacturing sector. Technology, then, has the effect of transferring wealth from the working class to the capitalist class, the only class that reaps a benefit from ever-advancing technology.

So what happens when we need only 5 or 10 percent of the population to manufacture the products we desire or realistically need? What do the rest of us do? Do we get up each morning, as William Abernathy once suggested, and press each other's pants? Or as Wayne Pullan puts it, "I'll cut your hair, and you'll cut my hair, and we'll both get rich." A nation of superfluous service workers is not an economically healthy nation, and never can be.

Capitalism's solution to the dilemma of a shrinking manufacturing workforce is to introduce new products—primarily services—at an accelerating pace (to perpetually create new jobs to replace the ones we have eliminated). To some degree this curbs unemployment, though not misemployment, and it keeps the wheels of capitalism spinning, but it also pressures us to consume more than ever before. The question, then, becomes: How long can we sustain this expanding spiral of debt-driven economic activity without seeing the whole system collapse? An economy built on an expanding foundation of superfluous products and expendable workers cannot endure forever. Technology-driven productivity improvement is fast creating a society in which the vast majority of us must find work in nonproductive activities, while those who control capital have little use for us, except as consumers.

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A second and equally dismal consequence of deriving profit from accelerating innovation is that this process speeds up product obsolescence. Thus, our economic health becomes dependent on continual innovation. We must perpetually make existing products obsolete by replacing them with newer versions; we must constantly improve quality, endlessly invent new products, and forever refine production processes so that we can make things less expensively. This constant obsolescence and the increase in available products, however, are filling our lives and our world with junk. I've been to the local landfill and have seen firsthand the mess created by our disposable society. But I also look around my house and can't believe all the *things* my family possesses, and how few of them we really need or use. And it's getting worse.

As the economy grows, the total innovation needed to sustain growth multiplies exponentially, as does the waste in the system. Sooner, rather than later, we will hit one of two inevitable limits—one economic, the other environmental. We will either make the planet incapable of sustaining our way of life (some argue that we have already accomplished this) or we will innovate ourselves into a two-tiered society composed of a small hyper-productive minority that creates wave after wave of new products for a huge, underpaid, nonproductive majority that is less and less capable of maintaining its customary living standard.

The Disconnected Financial System

Veblen tells us that profit is the result of financial manipulations by businesspeople who sabotage the system. The problem with this method of creating profit is that it divorces the financial system from the apparatus of production and consumption and makes profit an end in itself. In Veblen's world, most of the goods that clamor for our spare change (or remaining credit) are not an end in themselves, items that people actually need or that improve their lives. Most products sold in today's market are means to an end, and that end is profit. *They were created, not because we need them or even want them, but so that someone could extort a profit from the flow.* Production has become a tool of finance, not the reverse.

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"Twenty years ago," write Daly and Cobb, "the greatest power over the global economy may have been that of transnational corporations engaged in production. Today that power has shifted to institutions dealing with finance. Investment has come increasingly to mean the buying and selling of productive enterprises rather than their establishment or expansion."[6]

Financial markets, adds Paul Hawken, "reduce acts of commerce, which always have significant impact on human and natural life, to mere finance, to a decimal, to basis points, to net present value. We are turning over the financing of the world, if we haven't already, to money lenders whose interests and incentives revolve around minute increments gained in the sale of abstracted financial instruments."[7] Indeed, financial manipulation has grown so prevalent that we now have what has been called a *paper economy*, or "the direct conversion of money into more money without reference to commodities even as an intermediate step."[8]

Finance as an end in itself is a scary thing. When money becomes the most-sought-after product, something is terribly wrong, for money is no product at all. Money is a tool, a pure fiction we use to ease the exchange of real products. Said John Stuart Mill: "It is a machine for doing quickly and commodiously, what would be done, though less quickly and commodiously, without it; and like many other kinds of machinery, it only exerts a distinct and independent influence of its own when it gets out of order."[9]

Money in our day has indeed gotten out of order. It has become the most sought-after commodity of all, able to expand exponentially without any reference at all to real economic growth or contraction. And because of this, an increasingly speculative currency market has arisen. The financial superstructure in our economy has lost touch almost completely with the actual production and consumption of goods and services. Consequently, the world economy is becoming increasingly referred to as "one vast gambling casino." The ballooning derivatives market is the latest manifestation of speculation gone mad.

To illustrate how out of control money is, consider that annual world trade exceeds $3 trillion. World financial flows, on the other hand, reach nearly $100 trillion per year. What this means, according to Willis Harman, is that less than 5 percent of the "funds sloshing around the globe" have anything whatever to do with "goods and services that enhance human life."[10] To put it mildly, both the world economy and the American economy are growing more and more distant from the real world in which people eat, sleep, live, work, die, and consume. The mitotic propagation of money has totally overwhelmed the direct, beneficial type of transactions in which people buy and sell products to better their lives.

The System Is in Control

Profit is totally inadequate as the answer to our most fundamental economic questions. Aside from the problems just discussed that arise from the three methods of achieving enough profit to make the system grow, profit, by nature, creates a system in which power concentrates in the hands of those who seek their own and not necessarily society's good. A profit-driven system is basically a greed-driven system. It engenders within people a set of values that are in direct conflict with the health and well-being of human society.

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There is no mechanism in the totally free capitalist market to discourage greed or to create the equality that we claim as an American ideal. In fact, the profit-driven market works at every level to reduce fair competition, eliminate free enterprise, concentrate power and wealth, and build authoritarian economic structures.

As a disturbing side note, the market itself has absolutely no interest in human beings or their needs. It is not interested in full or meaningful employment, as evidenced by the long-term practice of replacing workers (who, because of their inherent inefficiency, are seen as part of the problem) with more efficient machines. The market's sole interest is profit and the power of survival that profit imparts. It is a perfectly impersonal system that views people just as it views any other resource—as a cost that must be minimized. It may be argued that the market is now in control. It is certainly beyond our control. And that is a frightening prospect.

As David Korten explains in his new book *When Corporations Rule the World*, "We have become captives of a rogue system that is functioning beyond human direction. Driven by its own imperatives, that system has gained control over many of the most important aspects of our lives to demand that we give ourselves over to its purpose—the making of money. We now face an even more ominous prospect. Having found its own direction and gained control of the institutions that once served our needs, the system that now holds us captive is finding that it has little need for people."[11]

Systemic Change

It has become obvious that we must find an alternative to the soulless quest for profit that drives our market system. Workable alternatives to our current system, however, are not part of the political agenda of either major party in America. The conservative solution of setting the market free from government meddling only intensifies all the problems outlined above. Additionally, it intensifies the fragmenting of society into diverse economic classes and exacerbates our dependence on debt and welfare. The liberal solution of redistributing income, on the other hand, creates dependence and lack of initiative among the poor and breeds resentment and callousness among the wealthy.

Neither of these solutions has more than a tenuous connection to reality. The only realistic solution to our economic woes, as I argue at length in *Economic Insanity*, must create systemic rather than cosmetic change. Instead of redistributing income—a feeble and ineffective attempt at ameliorating the *effects* and not the *source* of the profit motive—we must consider instead redistributing capital, giving a fair share to those whose labors actually create the products we need and want. If we were to limit capital ownership so that a person could own only as much capital as he or she could make productive use of, we would automatically solve a host of problems.

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Such a system would abolish the widening gap between rich and poor. It would defuse the growth imperative, because incentives would run toward smaller, community-oriented businesses and away from immense, unaccountable, transnational corporations. It would also increase choice in the economy and enhance healthy competition (whereas the power of large corporations restricts choice and eliminates healthy competition). It would put economics back into the social, political, and moral context where it rightly belongs. And it would remove much of the incentive for downsizing workers into the nonproductive service sector by focusing our attention on personally productive and satisfying work instead of on turning a profit at any price. Most important, however, it would subject the market to human needs, putting people back in control of their lives and livelihoods.

For such deep structural changes to be fully effective, of course, we will need to restore certain moral principles that we've discarded along the path to corporate domination and endless economic growth. I will be exploring this topic in a book that is now on the drawing board, but let me merely add at this point that unless our economic endeavors are guided by the higher good of society and restrained by certain moral absolutes, we will achieve neither a healthy economy nor a sound society.

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1. Robert L. Heilbroner, *The Worldly Philosophers: The Lives, Times, and Ideas of the Great Economic Thinkers*. 6th ed. New York: Simon & Schuster. 1986.

2. Ibid, p. 235.

3. Ibid, p. 235-6.

4. Ibid, p. 236.

5. Willis Harman, "Whatever Happened to Usury?" *World Business Academy Perspectives*. Vol. 6, No. 2, 1992, p. 20.

6. Herman E. Daly and John B. Cobb, Jr., *For the Common Good: Redirecting the Economy toward Community, the Environment, and a Sustainable Future*. Boston: Beacon Press. [1989], 1994. p. 436.

7. Paul Hawken, *The Ecology of Commerce: A Declaration of Sustainability*. New York: HarperCollins. 1993. p. 94.

8. Daley and Cobb, p. 410.

9. John Stuart Mill, *The Principles of Political Economy*. 9th ed. London: Longmans, Green & Co. Vol. II (Book III, Chap. VII). [1848], 1886. p. 9.

10. Willis Harman, Letter to the author. March 3, 1995.

11. David Korten, *When Corporations Rule the World.* West Hartford, CT: Kumarian Press, and San Francisco: Berrett-Koehler. 1995. p. 226.