Libertarian Alliance

THE MARXIAN THEORY OF EXPLOITATION: A CRITIQUE

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Richard Garner was a libertarian philosopher and a frequent contributor to the Libertarian Alliance and the Society for Individual Freedom until his premature death in 2011 at the age of 33. This pamphlet is an edited version of one that appeared on his personal blog on the 6th March 2008 and which first appeared in hardcopy in the September 2013 issue of *The Individual*, the journal of the SIF.

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Marxian "exploitation" versus reality

Socialists have railed against the market economy as inherently exploitative. One of the most well known and influential examples of this is in the writings of Karl Marx. This theory was developed most completely in his massive three-volume economics treatise *Capital,* but is neatly summarised by Arthur P. Mendel:

> *The entire argument in Capital rests on the labor theory of value. As was the case with virtually all the parts that Marx fused into his system, this concept was borrowed from earlier writers, in this case from the 'classical' economists such as Adam Smith and, especially, David Ricardo. It is primarily a price theory, according to which 'commodities' should exchange on the basis of the 'socially necessary' labor time devoted to their production. In other words, the amount of time a laborer works to produce a particular item determines its "exchange value": two products of equal labor value would thus be exchanged for one another.*
>
> *Having incorporated the labor theory of value, Marx derived from it a second step in his demonstration: the theory of 'surplus' labor value. According to this theory, the worker does not receive in wages an amount equal to the value of the goods he produces. We must keep in mind that the influence of the "pessimistic economists" still prevailed, as did the conditions promoting their pessimism. Drawing their conclusions from their own observations and from official government reports on working-class conditions in England during the industrial revolution, economists like Malthus and Ricardo argued that an "iron law of wages" existed that would keep wages down to a minimum necessary to meet the workers' basic needs. Marx accepted this and drew the conclusions he desired: on the one hand, the labor theory of value argued that labor created all the value of the goods sold by the capitalist; on the other hand, an 'iron law of wages' kept the laborer's income down to a subsistence minimum consequently, it must follow that the workers were not receiving the full value of their labor, that there was a 'surplus' kept by the capitalist owner of the means of production.*[1]

Our first response to this argument is to look at the "Iron Law of Wages." This theory is clearly false, for numerous reasons. The theory is, basically, that if wages rise for a time above enough to pay for mere subsistence then population will increase, resulting in increased competition for jobs amongst workers, resulting in lower wages. If, on the other hand, wages are lower than subsistence, fewer children are born, malnutrition kills off a certain percentage of the population, so competition for wages falls, and wages rise. Thus, it is argued, wages will always tend to a mere subsistence level.

It was in the nineteenth century that Malthus, Ricardo and Marx held to the theory of the Iron Law of Wages. However, in that century wages doubled and population increased over two and a half times. Rising real wages after 1850 did not lead to a rise in the birth rate, but the exact opposite: the birth rate fell from 35 per thousand in 1850 to 28.7 per thousand in 1900.[2] So empirical evidence doesn't back up the Malthusian argument.

Secondly, the Iron Law of Wages only approaches the question of what determines the price of labour from the perspective of supply and not demand (and then only crudely, for it doesn't recognise that the worker is buying a wage at the same time as selling their time, and thus take in the relative value they place on their uses of it). For instance, it is likely that a rise in population will result in a rise in demand for labour, so if population were to rise as a result of higher wages (as the Iron Law says it would), there is not necessarily a reason to expect a fall in wages as a result, because of an increase in demand for labour. This is, in fact, why an increased population as a result of free immigration or an absence of state control of reproduction will actually be likely to increase wages in the long term: increased population means more mouths to feed, means more demand for workers to feed them, means higher wages. Indeed, the Iron Law of Wages doesn't even take account of how productive a worker is. Surely, an employer would offer more to a skilled and dedicated worker than a talentless layabout, because the former will get more work done than the latter. If so, then, at least to that degree, wages will reflect productivity.

Thirdly, the phrase "subsistence level" is so ambiguous as to be almost useless. Cave men subsisted on a lot less than the average UK worker – or even the least paid UK worker – so why haven't UK wages fallen to the level needed to provide subsistence to a cave man? Workers in today's Britain live a lifestyle many would have thought luxurious by the standards of one a hundred years ago.

Therefore, the "Iron Law of Wages" doesn't hold water. Given this, Marx's presumption that wages will always tend to be less than the true value of the labour spent producing becomes untenable, and, if this is the case, his claim that capitalism is exploitative looks shaky too.

The value of labour

However, we may go further. Having disposed of the theory about what determines how much value a capitalist gives a worker, let's turn to the theory about how much value a worker gives to the capitalist. This theory, as stated above, is "… primarily a price theory, according to which 'commodities' should exchange on the basis of the 'socially necessary' labor time devoted to their production. In other words, the amount of time a laborer works to produce a particular item determines its 'exchange value': two products of equal labor value would thus be exchanged for one another." In short, the exchange rate, or price, of one hour of socially necessary labour time, in a free market economy, would be another hour of socially necessary labour time: an hour of work from a farmer will buy an hour of work from the builder. Hence the belief, also iterated above, that "labor created all the value of the goods sold by the capitalist."

However, it is obvious that labour doesn't create all the value of the goods (remember that the argument isn't that only labour creates goods, but that only labour creates the value of those goods, or, in other words, only labour gives those goods value). Surely if a group of identical workers spent an identical amount of time building an identical house next to a landfill site or sewage works as they did building one next to a site of great natural beauty, the latter would fetch a higher price than the former. Isn't this obvious? If so, then it must also be obvious that the exchange value, the price, of each house is not solely determined by the labour put into producing it but also by the geographical position and by the attractiveness of that position to those who would live in the house. Hence it is the utility, the preference satisfaction derived from owning that house, which determines its price.

An old complaint against the traditional labour theory of value (as stated by Adam Smith and David Ricardo) was that it implied that useless labour would fetch an equal price as useful labour. For example, an hour's worth of delicate and life saving brain surgery would buy an hour's worth of digging holes and filling them in again. This is obviously not the case, so the price of a good cannot be determined by the amount of time spent working on it.

However, this was not Marx's claim. As Robert Nozick points out,

> *Marxist theory does not hold that the value of an object is proportional to the number of simple undifferentiated labour hours that went into its production; rather, the theory holds that the value of an object is proportional to the number of simple undifferentiated socially necessary labour hours that went into its production.*[3]

This claim is backed by reference to Marx's own words in the first volume of *Capital*.[4] The point is that Marx qualifies the traditional labour theory of value by also requiring that labour hours be socially necessary, and this, he believes, saves him from the above argument.

Marx writes that, "Nothing can have value without being an object of utility. If a thing is useless so is the labour embodied in it; the labour does not count as labour, and therefore creates no value."[5] However, even accepting the condition that an object has to be of some utility, there still remain some problems. For instance, what if a worker works for 893 hours on something that is of only very slight utility. This satisfies the condition that it must be of some utility. So, should we now believe that here on in only the time spent making it matters, that only the amount of labour matters, so that now that it is of some utility it will buy 893 products that are of incredible utility but only took an hour to make? No, because, as Marx says, "…the labour spent on them (commodities) counts effectively only in so far as it is spent in a form that is useful to others."[6] In other words, the 893 hours of labour are only valuable insofar as they are of utility to those that consume them, as is the hour of the other goods mentioned, which implies that the value of a good depends on its degree of utility to its consumer, that the labour embodied in it is only as valuable as it is of utility to its consumer.

Marx even claims that "Whether that labour is useful for others, and its product consequently capable of satisfying the wants of others, can be proved only by the act of exchange."[7] In other words, the only way to tell if a commodity is valuable or not, or even if it has value, is by observing the action of the market process – the act of exchange. This is a hell of a concession! But what becomes clear is that, by tacking on the qualifying condition that labour need be socially necessary in order to have value, Marx has in fact ended up with something very different from a labour theory of value. He has claimed, in effect, that the value of a product is determined in so far as it is useful in satisfying the preferences of the consumer and not by the amount of labour time spent producing it at all!

Marx the market enthusiast

However, we can approach this from a different direction. Imagine that things are being produced as efficiently as they can be, but that too many of them are produced to sell at a certain price. The price at which the market clears is lower than the apparent labour values of the products: a greater number of efficient hours went into producing them than people were willing to pay for. Does this show that the number of average hours spent making an item of sufficient utility doesn't determine its value? Marx's answer to this question is to say that if such overproduction occurs that the market won't clear at a certain price, then the labour devoted to making an object was inefficiently used – less of the thing should have been made – even though the labour itself was efficient. Thus, not all those efficient labour hours constituted socially necessary labour time. The product does not have less value than the number of socially necessary labour hours expended on it, because there were simply fewer socially necessary labour hours expended on it than meets the eye.

> *Suppose that every piece of linen in the market contains no more labour than is socially necessary. In spite of this, all the pieces taken as a whole may have had superfluous labour-time spent on them. If the market cannot stomach the whole quantity at the normal price of 2 shillings a yard, this proves too great a portion of the total labour of the community has been expended in the form of weaving. The effect is the same as if each weaver had expended more labour-time upon his particular product than is socially necessary.*[8]

Robert Nozick neatly sums up the consequences of this view:

> *Thus Marx holds that this labour isn't all socially necessary. What is socially necessary, and how much of it is, will be determined by what happens on the market! There is no longer any labour theory of value; the central notion of socially necessary labour time is itself defined in terms of the processes and exchange ratios of a competitive market.*[9]

So on one hand Marx concocts a theory about prices that actually tells us that prices are not determined by labour, and then on the other he tells us that workers are exploited because all the value of the product they create is determined by labour. This is simply intellectual dishonesty!

Utility and explaining value

The classic labour theory of value is clearly wrong because it cannot explain why a sawdust sandwich won't buy a cheese sandwich when they both take the same amount of time to make. In fact, the labour theory of value is not even useful in economics because it cannot explain what goes on in an economy. For instance, I can buy cola in one-litre-bottles, and I can also buy it in two-litre-bottles. However, the price of a two-litre-bottle is not twice that of the one-litre-bottle even though it holds twice the contents. Why is that? Modern economics, abandoning anything approaching a labour theory of value, can answer this, but the labour theory of value cannot.

In terms of modern economics, it is easy to explain. It is less important to me that I get a second litre of cola than it is that I get a first. Once I have one litre, I care less about getting the second; the marginal utility of a second litre is lower than the first. Thus, if the company wanted to sell me a second litre, they have to make it cost me less than the first, because it is less important to me than the first. This is why the two litres of cola in a two-litre bottle will not be the same price as the two litres in two one-litre bottles.

But the amount of labour time spent producing the second litre was exactly the same as that spent producing the first litre. Therefore, the labour theory of value cannot explain why two-litre bottles of cola are cheaper than two one-litre bottles. Marx's changes to the labour theory of value lead us further and further away from an account of exploitation, because he would have to say that the labour embodied in the second litre in the two-litre bottle was less "socially necessary" than that of the first, but can only do so on the grounds that the market for cola wouldn't clear if it was twice the price.

However, we can reject the Marxist theory of exploitation without even rejecting the labour theory of value. David Gauthier sums up the Marxist argument:

> *Marxism offers a direct challenge to our account of the Market which, if sustained, would refute the claim that market interaction is impartial. For the Marxist insists that private ownership of the means of production, a fundamental presupposition of the market, is necessarily exploitative. The argument is simple. Under private ownership, nothing can prevent the emergence of a situation in which some individuals (capitalists) own the means that others (workers) need if they are to engage in productive activity. These others are then compelled to sell their labour power to the owners of the material means that production requires. This sale is exploitative. For the essential and distinctive characteristic of labour is that it produces more than the cost of its own production; labour thus reproduces itself and in addition produces what in Marxist thought is called surplus value. Now labour power is bought and sold, as any other commodity, at a price sufficient to cover its cost of production. Hence the buyer of labour necessarily receives the surplus value, since he pays the worker a wage equal to the cost of producing the labour power sold, and receives a price equal to the value of what that labour power produces. The market systematically favours the buyer of labour power over the seller; hence its operation is in principle partial to the capitalist.*[10]

Gauthier begins studying this position from the claim that the market price of what labour produces is greater than the cost of its own production. Imagine that the price of labour power was equal to the cost of producing it. It is obvious that under these conditions there would be a demand for more labour, because buyers (capitalist employers) profit from the difference between the price they pay for labour power and what they receive in exchange for its product, which, under these conditions, would be nothing (because price equals cost). This demand for more labour power would continue until the marginal product of an additional unit of labour power is equal to the marginal cost of producing that additional unit. However, at this point the price of labour – the wage paid – is equal to the price that is received for its product. There can be no surplus value when the supply of labour is brought into equilibrium with the demand for it. "The worker receives a wage equal to the marginal difference her labour power adds to the total product" – workers are paid according to their marginal productivity.

Marxists attempt to escape from this conclusion by denying that supply and demand come into equilibrium. The claim is that the buyer of labour power is able to keep its price, the wage, below the price he receives for its product, because the supply of labour will always exceed demand for it because of what Engels called "The reserve army of the unemployed." However, we have just seen that if the wage is below the price received for the product of labour, then there will be an effective demand for more labour – demand will be greater than supply. So the Marxist is trapped in a contradiction: The buyer of labour power is able to derive surplus value from labour – to pay the worker less than he receives for the product of labour – only if labour exceeds demand. But if there is a surplus to extract then this creates amongst capitalists a demand for labour in excess of the existing supply. As Gauthier says,

> *Or, to put the matter another way, if the supply of labour exceeds the demand for it, this can only be because the cost of producing labour exceeds the price that can be received for its product. So there can only be surplus value if supply exceeds demand but if supply exceeds demand there can be no surplus value.*[11]

So, if, as Marxists suppose, labour power is a commodity, then the operation of a competitive market must bring the supply of labour into equilibrium with the demand for it. Thus, at equilibrium, there can't be any surplus value for the buyer of labour power to extract, and so there can be no exploitation of the seller of labour power – the worker. Thus, in a competitive market, there can be no exploitation of workers, at least in the Marxist sense.

Notes

(1) Editor's note: Unfortunately, Richard did not reference this passage in the original blogged version of the essay and I have been unable to source it. All that I can say is that the late Arthur P. Mendel was an American professor of history at the University of Michigan. He wrote widely but specialised in Russian intellectual history.

(2) John L. Hanson, *A Textbook of Economics,* Macdonald & Evans, 1966, p. 311. Editor's note: Again, I must apologise. This a guess on my part. Whilst he cited the author, book title and page number, Richard did not cite the edition of the book.

(3) Robert Nozick, 'Anarchy, State and Utopia', p. 118, in Kory Schaff (ed.), *Philosophy and the Problems of Work,* Lanham, MD, 2001, pp. 109-122.

(4) Karl Marx, *Capital,* Volume 1, 1887/2010, p. 45. The version referenced here can be found at the "libertarian communist" website: http://libcom.org/library/capital-karl-marx, retrieved 28th June 2013.

(5) Marx, *ibid.*, p. 28.

(6) Marx, *ibid.*, p. 49.

(7) Marx, *ibid.*, p. 50.

(8) Marx, *ibid.*, p. 80.

(9) Nozick, *op. cit.*, p. 120.

(10) David Gauthier, *Morals by Agreement* (new ed.), Clarendon Press, 1987, p. 110.

(11) Gauthier, *ibid*, p. 112.