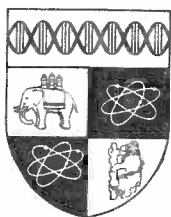


CLASS CONFLICT AND BARGAINING UNDER  
MONOPOLY CAPITALISM : THE IMPACT OF  
MASS UNEMPLOYMENT AND SOME EVIDENCE  
FROM THE UK

Steve Dowrick

NUMBER 261

**WARWICK ECONOMIC RESEARCH PAPERS**



DEPARTMENT OF ECONOMICS

UNIVERSITY OF WARWICK  
COVENTRY

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I am grateful for discussions with Keith Cowling, Ben Knight and Christos Pitelis and for comments from participants in the Warwick Industrial Economics Workshop and in the Cambridge Political Economy Seminar.

This paper is circulated for discussion purposes only and its contents should be considered preliminary.

1. INTRODUCTION

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Baran and Sweezy (1968, p.85) argue that "the working class as a whole is (not) in a position to encroach on surplus ... under monopoly capitalism employers can and do pass on higher labour costs in the form of higher prices". In Section 2 I examine this claim that employers' power in product markets can transcend conflict over the process and pay of labour, discussing the implications for conflict between groups of workers as well as conflict between workers and employers. Despite ample evidence of employers' monopoly pricing power, there is also evidence that profit margins do change in response to workers' strength - an observation which, I argue, is not adequately explained by theories based on the threat of foreign competition or by theories of oligopolistic uncertainty. Section 4 explores the hypothesis that employers and workers bargain over jobs as well as wages, a hypothesis which could explain workers' potential to erode profit margins.

The Marxist theory of a reserve army of labour acting as a brake on labour's strength might appear not to be relevant under monopoly capitalism, for if employers maintain stable profit margins, class conflict is transformed in aggregate into price inflation without affecting aggregate real profitability. In which case, capitalists would make the highest real profits by running the economy at full capacity. However, if workers' strength can erode profit margins, it opens up the possibility that employers would choose to maintain a pool of unemployed in order to protect profits by weakening workers' bargaining

power. I discuss this in Section 5 along with some empirical evidence that the recent rise in UK profitability is due in part to a fall in workers' strength.

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## 2. THE IMPLICATIONS OF A FIXED MONOPOLY MARK-UP

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Studies of the UK do confirm that monopoly margins over variable costs are fairly stable, particularly in relation to demand changes. Evidence on industrial pricing from Coutts et al (1978) and from Sawyer (1983) is that, in the words of Sawyer (p.98),

"we find considerable support for the view that price changes relative to cost changes are not strongly influenced by short-run variations in demand ... if we look at the actual price-cost margins, then we find considerable stability. Over the period 1970 to 1978 for British manufacturing as a whole, the ratio of gross profits to sales fluctuated between 0.194 and 0.217".<sup>1/</sup>

Glyn and Sutcliffe (1972) argue that international competition squeezes the share of profits. But their analysis does not adequately confront the thesis that margins over variable costs may be stable, and that it is the existence of quasi-fixed overhead costs (e.g. of salaried staff) which cause profit share to be reduced when capacity utilisation declines. Indeed, Coutts, Godley and Nordhaus (1978, pp.129-132) specifically conclude that neither import prices nor import penetration have a significant effect on UK domestic price-cost ratios. Murfin and Cowling (1981) also conclude that price changes are not significantly affected by import penetration.

Kalecki (1971, p.161) makes the point that, if margins are stable, "a general increase in money wages in a closed economy

does not change the distribution of national income"; a point which is confirmed by Rowthorn's (1981) formalisation of Kalecki's arguments in a model where the real wage is determined solely by the mark-up and by labour productivity.

If the variable labour input per unit of output is  $\ell$ , the wage is  $w$ , and the price-cost ratio ( $p/c$ ) is  $k$ , then:

$$\begin{aligned} \text{the real wage} &= \text{productivity/the price-cost ratio} \\ w/p &= \left(\frac{1}{\ell}\right) / k \end{aligned}$$

and wage share is simply the inverse of the price-cost ratio:

$$w\ell/p = \frac{1}{k}$$

If, however, raw materials are imported, then nominal wage changes may be converted into changes in the distribution of income, despite fixed profit margins, as long as the terms of trade can be turned against foreign producers. This point is made by Cowling (1982, p.98, fn.2). For if a stable mark-up is applied to total variable costs and if the foreign import part of the costs becomes relatively cheaper<sup>2/</sup> then the share of wages in value added will rise.

These Kaleckian analyses do suggest that, apart from gains made at the expense of the foreign sector, workers who are faced with a fixed monopoly mark-up are not able to change the distribution of income or win real wage rises in aggregate above the rate of increase of productivity. As Cowling (1982, p.99)

points out, this does not mean that there is no conflict between individual employers and their workers. If an individual firm or industry can impose relative pay cuts, or increase work effort, their profits will rise - and vice versa. It is only in aggregate that monopoly power appears to neutralise conflict over wages and production.<sup>3/</sup>

The effect of disaggregating conflict under monopoly capitalism is illustrated in diagram 1, an adaptation of Rowthorn's (1981) presentation of Baran and Sweezy's (1966) profitability schedule. The diagram represents the profitability of the "typical" employer (firm or industry) which mirrors the whole corporate economy. Simplifying to a closed economy where labour is the only variable input, there are constant returns to labour below full capacity, and the price-cost margin is fixed, we can write:

the margin  $(p-c)/p = m$

the value of the capital stock =  $pK$

the full capacity output is  $Y'$

actual output is  $Y$

the (normalised) level of employment  $L = Y/Y'$

the full capacity capital output ratio  $K/Y' = a$

the ratio of fixed real operating costs  $F$  to the  
the capital stock is  $F/K = f$

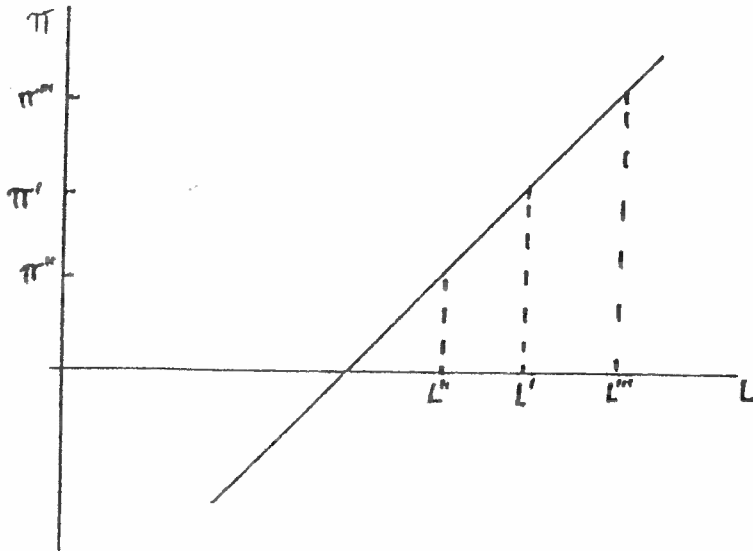
nominal profits =  $P$

The rate of profit is  $P/pK = \Pi = (m/a).L - f$

The rate of profit is a linear function of the level

DIAGRAM 1THE PROFITS CURVE

The rate of profit is:  $\pi = (m/a).L - f$





of employment (capacity utilisation). If the economy is kept (by the government) at a given level of real aggregate demand, giving employment  $L'$ , then average profitability in the economy is  $\Pi'$ . If workers force one employer to concede higher real wages, that employer raises price (given the assumption of a fixed margin) and demand for that product falls so that the employer reduces the number of jobs to, say,  $L''$ . But the price rise reduces the real wage and relative prices in other sectors, where employment rises to  $L'''$  and profit to  $\Pi'''$ .

We can see here that if monopolistic employers maintain fixed margins, workers can win a rise in real wages in one sector only by winning a higher than average pay rise. But it is not just employers' profits in that sector which suffer. For monopoly power allows an employer to pass part of the costs they are forced to concede on to consumers through higher prices. Here lie the seeds of division amongst workers under monopoly capitalism. Under competitive capitalism a wage rise specific to one firm would reduce the employer's profits, and might lead to bankruptcy, but would not be passed on to consumers. But monopoly pricing power cushions profits and passes on some of the cost. We can see the origins (but not the justification) of the recent success of conservative ideology in persuading workers to identify as consumers and to blame trades unions for price inflation.

The ability of monopoly capitalism to maintain aggregate profitability in the face of worker pressure rests crucially on industries maintaining a stable mark-up. If each industry faced with militant workers were to reduce its margins, perhaps

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in an attempt to maximise their (conjectured) profits, then the whole economy would move to a lower profits curve. The maintenance of price-cost margins is a collective good for capitalists.

Given a stable monopoly mark-up it would be in capital's interest to run the economy at full capacity. There may be a trade-off between unemployment and inflation, but it will not affect the average level of real profit. Nor would curbs on trade union strength affect real wages or profits in aggregate. But it is hard to believe that recent attacks by pro-capitalist governments in the UK and the USA on trade union organisation, and their failure to boost aggregate real demand in the face of mass unemployment is merely an attempt to reduce the rate of price inflation. We need to investigate the hypothesis that workers' strength may be able to erode profit margins.

### 3. CAN WORKERS' STRENGTH ERODE MONOPOLY MARGINS?

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Although the evidence of UK pricing previously cited does indicate that profit margins over unit costs are fairly stable in the face of both demand changes and foreign competition, there is a significant and surprising difference between the mark-up on labour and that on non-labour cost reported in the study by Sawyer (1983). It is important to note that for the UK economy as a whole labour costs account for most of unit variable costs, but at plant level Sawyer (1983, p.73) reports that direct labour accounts for only 20% of variable costs. This indicates a high level of vertical disintegration whereby the majority of inputs are raw materials, energy, intermediate goods and services, rather than direct labour (although the disintegration will be somewhat less at firm rather than plant level). Sawyer's surprising result is that although non-labour costs are fully marked-up, changes in wages do not have a significant effect on pricing. The implication is that wage pressure can cut into margins.

Related evidence comes from Henley (1984) who shows that the extent and pattern of union-employer bargaining across UK industries in the 1970s did have significant explanatory power, in regressions on wage share. In particular, the existence of extensive industry-level union-employer bargaining supplemented by plant-level bargaining appears to increase the share of wages in value-added - an indication that margins are reduced by union pressure.<sup>4/</sup>

Levinson's (1954) study of US income shares 1929-52 indicates that the union sector did manage to raise the share of labour in value added (although Levinson argues that

labour's share increased at the expense of interest and rent, rather than at the expense of profits, it is clearly a gain for labour at the expense of property income taken as a whole). Weisskopf's (1979) study of US profit rates 1949-75 does also indicate that wage-share, adjusted to take account of overhead labour, does change significantly both within and between business cycles - a phenomenon which he relates to the strength of labour without specifying a precise mechanism by which labour strength acts on profit margins. Freeman (1983) studied a cross-section of 139 US industries 1958-76 and reports that

"unionism has a statistically significant quantitatively important depressant impact upon the relevant profit indicators ... limited to the more concentrated industries"

- the profit indicators being both the price-cost margin and the rate of return on assets.

Most of the studies cited above measure workers' strength only by the degree of unionisation. Of course other factors such as labour legislation, union morale and resources, and the level of unemployment will probably be significant too. Nevertheless, the evidence does strongly suggest that workers' strength does erode profit margins.

But why should employers allow their profit margins to be squeezed? One possible explanation is that individual firms might conjecture a kinked demand curve: if they raise price in response to wage pressure they expect they will lose sales heavily

as they did not expect their rivals in the industry to raise price too. This explanation might be plausible in a loose-knit, uncoordinated industry where employers imagine that wage rises are specific to their firm while other cost rises are general; but it does not make sense in the context of concentrated collusive oligopolies, particularly where wage-bargaining is conducted at the industry level. The evidence on UK pricing which I have cited earlier discounts the alternative explanation that it might be the threat of foreign competition which squeezes margins. Moreover, flexible exchange rates make it possible for international competitiveness to be maintained (in aggregate) despite domestic price rises. Another explanation for the observed vulnerability of margins might be that there are time delays between cost and price rises. This would mean that changes in the rate of cost inflation would erode margins, but it does not necessarily mean that in the longer run margins are affected by the level of workers' strength.

I suggest here another explanation for the observed vulnerability of profit margins to workers' strength: the hypothesis that unions and employers bargain over jobs as well as over wages. In the next section I argue that this hypothesis implies that changes in wages and in profit margins are a direct reflection of shifts in bargaining strength between unions and employers.

#### 4. BARGAINING OVER JOBS AND WAGES

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When employers and unions bargain over wages it is useful to consider the minimum and maximum feasible outcomes. There will generally be a floor to the wage which the employer must offer, related to what workers could expect to earn elsewhere, the likelihood of unemployment, the level of unemployment pay, etc. This floor or reservation wage is the minimum wage which employers would have to pay to get workers if the union had no bargaining power at all. There is also a maximum wage which would force employers' profits (net of the opportunity cost of capital) to zero. Above that wage, the employer would be bankrupted or would choose to move capital elsewhere. The reservation wage and the opportunity cost of capital can be thought of as the earnings of capital and labour in the competitive markets of neo-classical theory and classical Marxism. The distinctive feature of modern capitalism is that oligopolistic control over product markets gives employers a potential surplus over "normal" profits. An individual union's potential to win pay rises above the reservation wage depends on the existence of such a surplus; for without a surplus, the union would be forced to accept the competitive wage or lose their jobs. Of course the existence of monopoly surplus does not necessarily mean that unions will win higher wages, only that the potential to do so is there.

There is empirical support from both the UK and the USA for the proposition that unions bargain over the surplus created by product market monopoly. Freeman's (1983) study of US industries shows that profits in concentrated industries

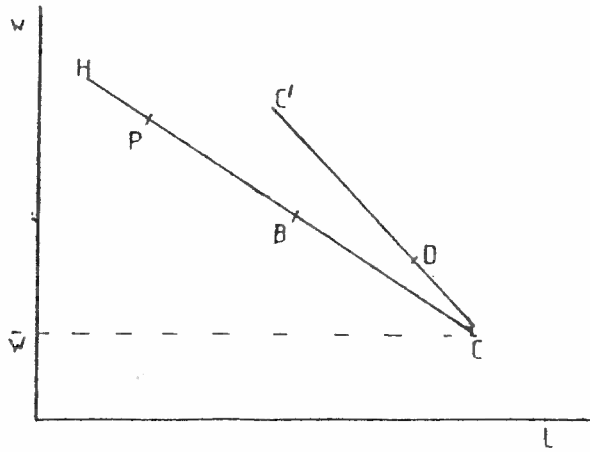
are reduced by union organisation. Adams and Brock's (1984) study of four major US industries found that wages and wage growth were higher in non-competitive than in competitive industries. de Menil (1971) found significant support for a bargaining hypothesis in six out of eight US industries over the period 1947-69. Nolan and Brown (1983) found in a study of the variance of wage increases of occupational groups in twenty-five UK engineering factories, 1971-80, that firm-specific effects dominated occupation effects - a result which can be interpreted as support for the surplus bargaining hypothesis. Geroski, Hamlin and Knight (1982) confirm that UK wages in 1968 were positively correlated with profit margins over 73 manufacturing industries. Tylecote (1975) found that UK wages rose faster during 1954-78 in the more concentrated (and perhaps more monopolistic industries). In an Australian study, Brown, Hayles, Hughes and Rowe (1984) found that wages are positively correlated with measures of market power. All these studies support the hypothesis that the larger the monopoly surplus, the larger is the premium that workers are able to win on their wages. But these studies do not tell us how much of the surplus workers are able to win, nor how they bargain for it.

Evidence on the extent of bargaining over jobs is mixed. US studies by Svejnar (1984), MaCurdy and Pencavel (1983) and Clark (1984) provide indirect evidence that bargaining does cover jobs - though both Svejnar and MaCurdy and Pencavel have to assume particular forms of firm's production functions to derive their results. On the other

hand, Oswald (1984) surveys actual union-employer deals in the UK and US and finds that explicit bargaining over jobs is conspicuously absent - but he does not deal with the possibility that job bargaining is implicit, nor with the possibility that job bargaining may be more prevalent in periods when workers are strong. It does appear that the implications of whether or not workers and employers do bargain over jobs is worthy of investigation.

When a union and employer are bargaining over wages, the employer must have some conjecture about demand for the product. An employer who conjectures a down-sloping marginal revenue curve and faces constant returns to labour employed will find it profitable to reduce employment the higher is the wage; so we might expect a monopolistic employer to present the union with a down-sloping labour demand curve (HC in diagram 2). In the diagram any point  $(w,L)$  represents a possible wage-job outcome which will result in an (expected) profit for the employer and an (expected) utility for the union. At point H the employer makes zero monopoly profit. At point C the workers are paid the reservation wage and the employer earns the full surplus. There is some point P which the union would choose if it could, beyond which point the benefits of a higher wage would be outweighed in the union's view by the ensuing job losses. The actual outcome of wage-bargaining can be represented by some point B. The stronger the employer's bargaining position, the lower down the labour demand curve will be the outcome B.



DIAGRAM 2BARGAINING FOR AN INDIVIDUAL EMPLOYER

any point  $(w, L)$  represents  
a possible wage/job  
outcome  
 $HC$  = labour demand curve  
 $C'C$  = contract curve  
 $P$  = union's preferred  
wage-only bargain  
 $B$  = actual wage-only  
bargain  
 $D$  = actual wage-job bargain  
 $\bar{w}$  = reservation wage

~~If the union is at all concerned with jobs, any wage-~~  
 only bargain B will be pareto inefficient, i.e. there will be some other bargain D which will be preferred by the union and will at the same time give the employer higher profits. The set of efficient bargains is shown in the diagram as the line C'C - the contract curve. In effect, the employer may be able to negotiate a lower wage deal by guaranteeing workers a minimum level of employment - whether the guarantee is in the form of an explicit no-redundancy agreement or an implicit contract.

There is one case which is particularly simple to analyse. Assume the following: a) the bargaining outcome is efficient; b) the employer aims to maximise profits; c) the union aims to maximise its members' income net of the reservation wage. In this case the contract curve is vertical and the level of employment is that which would obtain if the union had no bargaining strength and workers were paid just the reservation wage.<sup>5/</sup> The strength of the union's bargaining position is reflected solely in the wage, while the number of jobs is independent of relative bargaining strengths (though the number of jobs will fluctuate according to demand conditions and movements in the reservation wage).

With bargaining on a vertical contract curve the level of output and price is independent of the workers' bargaining strength. So a wage rise brought about by a rise in workers' strength eats directly into the profit margin. Such wage rises are not passed on into higher prices. Let the employers'

employers' maximum price-cost margin (at point C in diagram 2) be  $m''$ ; and the minimum price-cost margin (at point C') be  $m'$ .<sup>6/</sup> Then, if the workers' bargaining strength relative to the employers' is  $b : (1-b)$ , the actual mark-up is given by:

$$m = b.m' + (1-b).m''$$

Of course bargaining over jobs does not in general mean either that the contract curve will be vertical or that the outcome must lie on the contract curve. In practice, both employment and the wage will be sensitive to changes in bargaining strength. But the example of the vertical contract curve does indicate that a likely result of bargaining over jobs is that workers' strength is reflected inversely in the profit margin (and in wage share in value added) whereas I argued earlier that wage-only bargaining does not necessarily affect profit margins in a monopolistic industry. So we have here a possible explanation for the observations cited previously that workers' strength can erode profit margins.

It is important to note that job bargaining in itself does not represent any erosion of capitalist control or power, at least not at the level of the individual employer. For maintenance of margins and profit share is not a useful measure of capitalist power. Employers are concerned not with margins but with levels of profit. If bargaining is over wages alone, workers' strength may enable them to win wage rises which drive down the profit levels of individual employers, even if the

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employer maintains a stable price-cost margin. Bargaining over jobs is to the advantage of the individual employer who may be able to persuade the union to settle for a lower wage in return for job guarantees. Nor does job bargaining impinge on struggle for control of the work process, for employers' power to hire and fire individual workers is not threatened by an agreement which merely stipulates a minimum level of employment.

There is, however, a paradox between motives at a microeconomic level and their resolution in the macroeconomy. If individual employers bargain over wages only, they may each expect their profits to be reduced by workers' strength: but stable monopoly mark-ups ensure that workers' pressure on wages is converted into inflation, and aggregate real profits are unaffected. On the other hand, if employers bargain over jobs as well as wages, doing so in order to protect their individual profit levels, and in the process allowing their profit margins to fall, the macroeconomic outcome is that they may actually lose real profits as a result of abandoning the capitalist collective good of inflation.

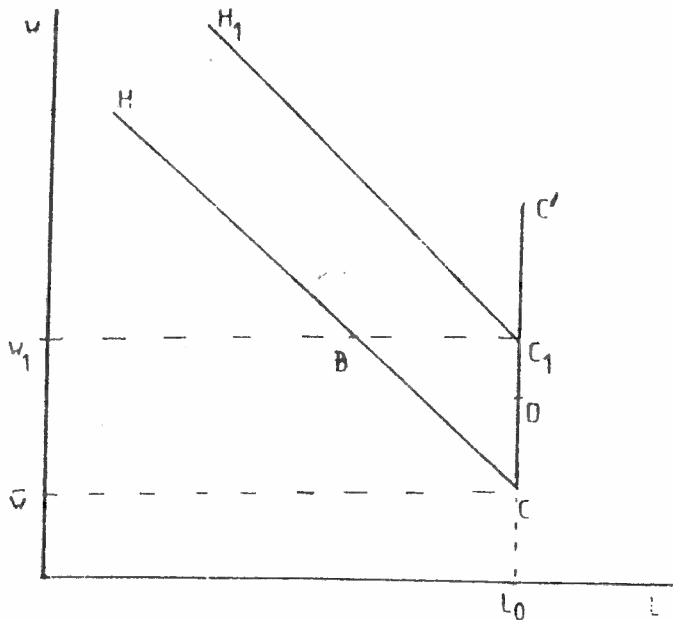
On the other hand, it is possible that at the micro-level an individual employer who bargains over jobs may make lower profits than if they bargained over the wage alone. For although there are potential wage-job bargains which are better for both parties, the expectation of job guarantees may have the effect of increasing workers' bargaining strength by removing the threat of job losses, so leaving employers

worse off. If this is so, then employers' individual and collective interests coincide - to resist workers' attempts to bargain over jobs. But whatever the micro-level position, at the macro-level it is clear that it is in the interests of capital as a class not to allow profit margins to be eroded - therefore not to bargain over employment.

This argument can be illustrated by considering the wage, job and profit outcomes of a "typical" employer bargaining with a union. The employer could be either a firm or an industry. The employer is typical in the sense that its decisions are mirrored in the economy as a whole; but the individual employer conjectures that the actions of the rest of the economy are independent of its own actions. Let us look first at wage-only bargaining. The employer's expectations of product demand result in a conjectured labour demand curve,  $HC$  in diagram 3. Suppose that we start from a position where the union has no bargaining power, so the wage is  $\bar{w}$ ; furthermore, suppose that the economy is in equilibrium such that the actual price level turns out as expected and the level of real aggregate demand does indeed generate the conjectured demand curve for the employer who does indeed employ the expected number of workers  $L_0$ . So the outcome is at point  $C$  in diagram 3, and the real profit rate is  $\Pi_0$  corresponding to point  $C$  in diagram 4 on the profits curve  $PC_0$ .

DIAGRAM 3

COMPARISON OF EX-ANTE BARGAIN AND OUTCOME FOR A TYPICAL EMPLOYER



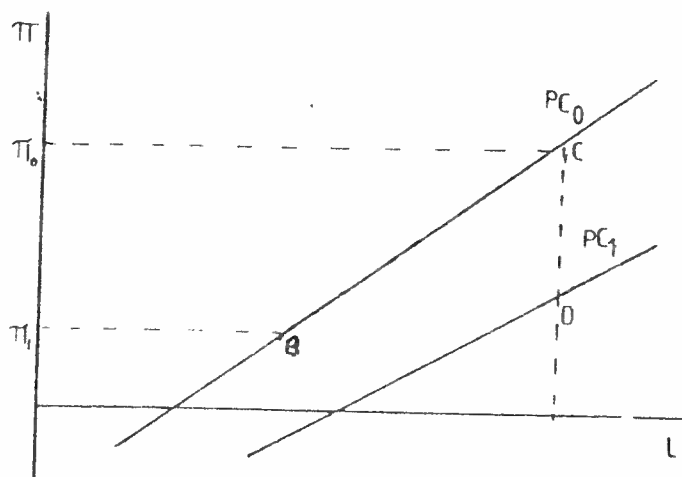
HC = conjectured labour demand  
 $H_1C_1$  = ex post labour demand  
 $C_1C''$  = conjectured contract curve  
 $\bar{w}$  = ex ante reservation wage  
 $w_1$  = nominal wage bargain

DIAGRAM 4

THE PROFIT CURVE FOR THE TYPICAL EMPLOYER : a) IF MARGINS ARE MAINTAINED ; b) IF MARGINS ARE SQUEEZED

$PC_0 : \pi = m_0 \cdot a/L - f$

$PC_1 : \pi = m_1 \cdot a/L - f$



Now consider that happens if workers' strength rises

so that they are able to win a nominal wage rise to  $w_1$ . The employer expects demand to be choked off by the price rise which follows the wage concession, and therefore expects employment to fall to point B and the profit rate to fall to  $\Pi_1$ . But all employers raise their prices above the expected rate of inflation. So, if real aggregate demand in the economy is maintained (e.g. by government or by banks) the actual demand curve facing the typical employer shifts so that the labour demand curve shifts to  $H_1C_1$ , employment stays at  $L_0$ , and real profits stay at  $\Pi_0$ . Employers expected to be forced down their profits curve from point C to B, but inflation bounces them back to point C. In this scenario, the rise in workers' strength has been turned into inflation by a combination of employers' power to raise prices (exercised in unplanned concert) and some mechanism which maintains a stable level of real aggregate demand. Real profits are protected by inflation.<sup>7/</sup>

Of course, in this story workers' real wage aspirations are denied and a further round of bargaining could lead to accelerated inflation. Inflation provides the resolution of a contradiction between: i) the level of the individual employer, where workers may have the strength to bid up nominal wages and reduce expected profits, and ii) the level of the economy where employers maintain aggregate real profitability as a result of maintaining their profit margins. This contradiction between micro-level nominal bargaining and the macro-level real outcome is the basis of the inflationary aspiration gap described by Rowthorn (1980, p.150-1).

In contrast, consider the implications of bargaining over jobs as well as wages. The initial bargain is again at point C in both diagrams 3 and 4. Now, as workers gain strength they negotiate a better nominal deal at point D (where individual employers make higher expected profits than at B). If we make the strong simplifying assumptions that neither employment nor the reservation wage are affected by this rise in workers' strength, then output and prices will be unchanged and the increase in union power is reflected in a narrowed profit margin, falling from  $m_0$  to  $m_1$  - i.e. the profits curve drops to pass through point D in diagram 4. Aggregate real profits are driven down by workers' strength because individual employers abandon the collective weapon of inflation.

I have described the polar extremes of a) wage-only bargaining, where employers' monopoly power may preserve profitability by transforming, in aggregate, wage pressure into inflation; and b) wage and job bargaining which can shift the profits curve in favour of wages or profits according to the balance of class strength. Reality is no doubt somewhere inbetween, with class struggle partly transformed into inflation, partly a straightforward conflict between profits and wages.



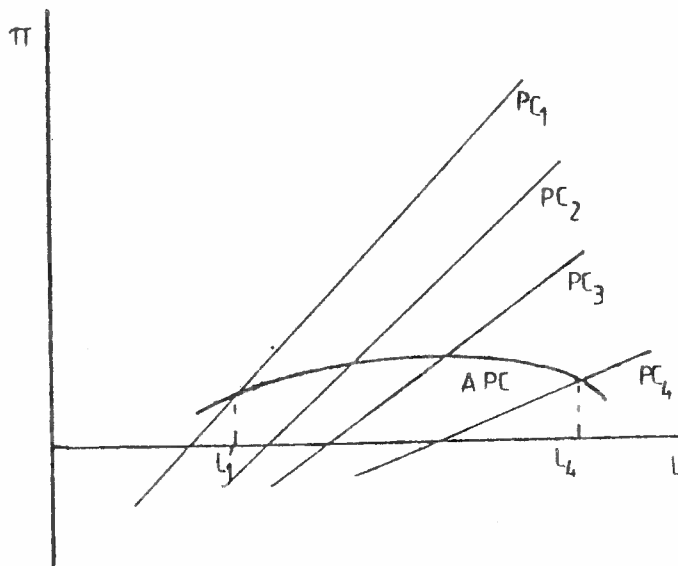
## DIAGRAM 5

THE ACTUAL PROFITS CURVE - WHEN RISING EMPLOYMENT SQUEEZES MARGINS

$PC_i$  = the notional profits curve  $\pi = m(L_i).a/L - f$

where the margin  $m$  is a function of employment :  $m = m(L)$

APC = the actual profits curve  $\pi = m(L).a/L - f$



5. THE RESERVE ARMY OF LABOUR - AND THE UK EXPERIENCE  
1979-84

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I have argued on both empirical and theoretical grounds that an increase in workers' strength has the effect of lowering the profits curve - shifting the distribution of income at any given level of output and employment in favour of wages. If unemployment weakens workers' bargaining position, it may be in the interests of capital to maintain a pool of unemployed - for although a recession which produces unemployment reduces the overall level of production, it may increase the share going to profits to such an extent that profitability is actually increased.

This argument is illustrated in diagram 5. At increasing employment levels ( $L_1$  to  $L_4$ ) the mark-up falls (from  $m_1$  to  $m_4$ ) so lowering (from  $PC_1$  to  $PC_4$ ) the appropriate notional profits curve which would hold if the mark-up was constant. We can trace out the actual profits curve (APC). If APC peaks below full employment, the reserve army hypothesis is validated. Of course it does not mean that increasing unemployment will always increase profitability, only that there will be, for capital as a whole, an optimal level of unemployment.<sup>8/</sup>

Weisskopf (1979, p.371) concludes in his study of the US economy that:

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"evidence on labour market conditions - both in a cyclical and in a longer-run context - was fully consistent with the argument that the strength of labour vis-a-vis capital increases when the reserve army of labour is relatively depleted".

The late stages of each of five successive cyclical expansions saw a fall in the rate of profit in the US non-financial corporate business sector. (The same is certainly true of the UK economy in 1979). But Weisskopf argues that his evidence also supports the reserve army hypothesis in the longer-run secular context. This too is confirmed by the recent experience of the UK economy.

The early 1980s have seen massive deflation and unemployment in the UK, but at the same time profitability has recovered from the trough of the mid 1970s to a ten-year record level, above the average level of the 1960s. At the beginning of 1984 GDP was about the same as in 1979 - but although the national cake had not increased in size since the Thatcher government took office, the division of the cake had altered radically. The dramatic slump and gradual recovery of the early 1980s have seen not only a major restructuring of the economy, but also a major redistribution from wages to profits. The share of gross profits in GDP has soared to a post-war record level of over 18% by the first quarter of 1985, while the share of wages and salaries has slumped to a record low (see Table 1). A truly dramatic change in the distribution of income, taking the share of profits well above the 1960-73 average of 12%. At the same time, the real net rate of return on capital rose

TABLE 1 - UK PROFITABILITY 1960-84

YEAR	SHARES IN GDP		SHARE IN NDP		REAL RATE OF RETURN							
	EARNINGS <sup>1</sup>	PROFITS <sup>2</sup>	PROFITS <sup>3</sup>		ALL COMPANIES	EXCLUDING PRE-TAX	NORTH SEA <sup>5</sup>	POST-TAX				
1960-73 (av)	67.3	%	13.4	%	12.1	%	9.2	%	9.2	%	6.5	%
1974-79 (av)	69.3		10.5		8.0		5.7		5.3		5.4	
1980-84 (av)	66.9		13.3		-		-		-		-	
1974	70.2		8.9		7.3		5.1		5.3		5.3	
1975	72.5		7.9		5.4		4.0		4.3		3.5	
1976	70.8		8.4		5.8		4.2		4.3		4.3	
1977	67.5		12.4		9.7		7.0		6.4		7.0	
1978	67.0		13.0		10.4		7.5		6.8		7.2	
1979	67.7		12.6		9.3		6.5		4.9		5.0	
1980	69.0		11.8		8.8		6.1		3.7		4.5	
1981	68.5		11.5		9.5		6.5		3.4		4.2	
1982	66.6		12.8		10.8		7.8		4.3		4.5	
1983	65.7		14.2		13.0		10.0		5.8 <sup>7</sup>		5.8 <sup>7</sup>	
1984	64.9		16.0						8.5 <sup>7</sup>		8.5 <sup>7</sup>	
1985 Q1	63.8		18.5									

Sources : Bank of England Quarterly Bulletin September 1984, 352-359.  
 British Business, 21 September 1984, 119-120.  
 Economic Trends April 1985, p.14, and Annual Supplement 1985, p.3.  
 National Income and Expenditure 1984, Tables 3.5 and 5.4

Notes : 1. Wages and salaries, forces' pay and employers' contributions.  
 2. Gross trading profits of companies, net of stock appreciation, including financial institutions.  
 3. Net trading profits and rent of industrial and commercial companies.  
 4. Net operating surplus on UK operations, before interest and tax, on net capital stock of fixed assets (excluding land) at current replacement cost plus book value of stocks.  
 5. Estimated from BEQB chart p.358, backward-looking measure.  
 7. Bank of England estimate, BEBQ p.353 for 1984 Q1.

from 6.5% in 1979 to 10% in 1983, and presumably well above 10% at the start of 1984 - compared with an average of 9.2% over the years 1960-73.

These record profitability figures are not an artefact of the profits slump in the mid-1970s. Nor are they purely a result of the restructuring of the economy towards north sea oil. By the beginning of 1984 the Bank of England's estimate of the real rate of return of non-north sea companies was at a ten-year record level and only just below the 1960-73 average. The post-tax non-north sea rate of return was well above the 1960s average. Including north sea activities, which now account for just over one third of UK company profits, raises the real rate of return much higher still.

The rise in the share of profits is explicable from table 2A where we see that although the hourly product wage for all workers in the UK rose by some 17% between 1979 and 1983, productivity rose even faster; so the product wage per unit of output (i.e. the share of wages and salaries) fell by 4%. Moreover, the cost of this massive redistribution towards profits has not been borne equally by all workers. The prime losers have of course been those thrown out of work or deprived of the chance to start work. For although UK output at the beginning of 1984 was the same as in 1979, it was produced by a million and a half fewer workers. For those still in work, earnings did not rise at the same rate as productivity, hence the redistribution towards profits. Furthermore, the rise in real post-tax earnings was restricted to non-manual workers,

TABLE 2A : UK Real Hourly Wages and Unemployment over the  
Recession 1979-83

Growth of adult hourly (1) real earnings and costs  
(% growth over whole period, then annual % growth on previous  
year)

ALL INDUSTRIES AND SERVICES

	1979-83	1980	1981	1982	1983
Unemployment (5)	+139%	+25	55	16	6
GDP	-1.1	-3.2	-1.9	1.6	2.5
product wage (3)	17.2	4.8	5.0	2.9	3.5
product wage per unit output (6)	-4	2	-1.4	-2.5	-2.1
<u>real post-tax wages (1,2)</u>					
all adults	12.2	6.4	0.6	-0.3	5.1
male manual	5.4	4.5	-2.9	-0.3	4.2
female manual	4.3	5.6	-4.4	-2.1	5.5
male non-manual	14.7	7.5	1.4	0.4	4.8
female non-manual	15.5	7.7	2.6	-0.9	5.5

TABLE 2B : Manufacturing IndustryMANUFACTURING

	1979-83	1980	1981	1982	1983
Output	-12.3	-8.5	-6.3	0.3	2.3
product wage (4)	17.7	7.3	4.3	2.3	2.8
product wage per unit output (6)	2.2	8.1	0.2	-2.4	-3.3
<u>real post-tax wages (1,2)</u>					
all adults	7.7	4.0	-1.0	0.3	4.3
male manual	3.0	2.5	-2.9	-0.3	4.2
female manual	1.6	2.5	-4.0	-1.6	4.9
male non-manual	10.5	5.5	-1.1	1.3	4.5
female non-manual	10.4	4.7	-0.9	1.2	5.1

Sources: Employment Gazette, February and August 1984,  
Blue Book 1984, Economic Trends No.371, September,  
1984.

Notes:

- (1) hourly earnings of full-time men, 21 years and over,  
and women, 18 years and over, all occupations,  
excluding those whose pay was affected by absence,  
excluding overtime pay and overtime hours.
- (2) deflated by Tax and Price Index
- (3) deflated by GDP deflator
- (4) deflated by Producer Prices Index
- (5) excluding school leavers
- (6) i.e. the share of wages and salaries in revenue

whose real pay rose at an average of 3.6% per annum over the period - about in line with the overall rise in productivity. But over the same period, manual workers' real hourly pay rose at an average of only 1.2% per annum. Male manual workers lost overtime hours, so their real weekly earnings did not rise at all between 1979 and 1983 - and their real weekly earnings actually fell in manufacturing industry (see Table 2B).

So not only was there a redistribution from earned income to profits, but also from wages to salaries. Male manual hourly earnings fell from 68% to 63% of male non-manual earnings. Non-manual women fell even further behind, from 70% to 69% of the hourly earnings of their male manual counterparts (or from 48% to 44% of the hourly pay of male non-manual workers), (see Table 3).

It is clear that the recent boom in profits has come at the expense of manual workers' real pay (in relation to productivity). Is this redistribution merely a result of the demise of unprofitable industries and a move towards high productivity and high profit activities? It appears to be much more than that. For, as we have seen in Section 4, high profit industries tend to pay higher wages - so if we were merely witnessing a restructuring of industrial activity we would expect to have seen a sharp rise in real manual pay, a rise due to the secular rise of wages in line with productivity compounded by a switch to high productivity, high wage activities. But Tables 2A and 2B show that in fact manual hourly earnings



TABLE 3 : Differentiale over the Recession : Manual/Non-  
Manual, and Female/Male Hourly Earnings (1)

	1979	1983
<u>women : men</u>		
manual	70.2%	69.6%
non-manual	61.0%	61.4%
<u>manual : non-manual</u>		
men	68.2%	63.4%
women	78.5%	71.8%

Source: Employment Gazette, February 1984, Table 5.6

Note:

- (1) adult full-time hourly earnings, excluding absentees and excluding overtime pay and overtime hours, all industries and services.

hardly rose at all in real terms, faring worst of all in the manufacturing sector which has borne the brunt of the restructuring. Moreover, a study of real rates of return between 1980 and 1983 for major non-oil UK-based companies (Bank of England Quarterly Bulletin, September 1984, p.362) breaks the results down into 23 major industrial groupings. 19 groups experienced a rise in profitability, with falls recorded only in office equipment and shipping and transport sectors. These figures do include the overseas activities of UK companies (whereas all figures quoted in the tables refer to the UK operations of both domestic and foreign-based capital). Nevertheless, they indicate that profitability has risen in almost all sectors. So I conclude that although restructuring has undoubtedly occurred, the rise of UK profitability to record levels is also due to a weakening of workers' bargaining strength, reflected most clearly in the holding back of manual workers' real wages.

The unique nature of the recent shift in strength towards capital is illustrated by the figures in Table 4 which show the recent period of decline in real manual wage rates (not earnings) in stark contrast with their steady upward growth (along with productivity) since 1963. Prior to 1980, real manual wage rates fell in only three years since 1963 : each time in a period of pay policy under a Labour government. The 1965 and 1969 cuts were made good by compensating pay rises within one or two years - viz. the success of "real wage resistance" econometric models for this period. But the 1976 cut in real manual wage rates had still not been made up by

TABLE 4 : UK Manual Real Wage Rates 1968-83

## Average annual rates of growth

	1963-68	1968-73	1973-79	1979-83
	% p.a.	% p.a.	% p.a.	% p.a.
<u>Real wage rates (1)</u>				
all industries and services	1.0	3.6	1.6	-0.6
manufacturing	1.2	2.4	1.6	-1.4

THE INCIDENCE OF FALLING REAL WAGE RATES 1968-83

years of falling real wage rates	1965	1969	1977	1980	1981	1982
<u>% real wage growth</u>						
all industries	-0.5	-0.1	-9.3	0	-1.7	-1.7
manufacturing	-1.1	0	-11.2	-0.9	-2.4	-2.7
official pay policy	yes	yes	yes	no	no	no
<u>unemployment (2)</u>						
level (millions)	0.3	0.6	1.4	1.6	2.4	2.8
% change on last year	-14	-1	+8	+25	+55	+16

Sources: Economic Trends Annual Supplement 1982;  
Employment Gazette, February 1984;  
Economic Trends, June 1984

Notes:

- (1) Nominal wages deflated by the General Index of Retail Prices.
- (2) Unemployed excluding school leavers, annual average.

the beginning of 1984. And this is exactly the period of the rise of mass unemployment in the UK from 0.8 million at the beginning of 1975 to over 3 million in 1984, and the rise of profitability to a ten-year record.

The reserve army hypothesis - that mass unemployment can boost profits by weakening workers - is clearly supported by the recent UK experience. Knight (1983) argues that the effectiveness of the reserve army has weakened as the unemployed lose (or never get the chance to acquire) the skills and motivation with which to threaten workers in employment. But his evidence of a rising product wage over the recession does not take account of the fact that the product wage has risen slower than productivity in the whole economy - i.e. the share of wages and salaries has fallen. Even in manufacturing, where the share of wages and salaries rose 1979-83, it is evident that this rise occurred entirely in 1979-81 when manufacturing output slumped by some 15% - and that wage and salary share has fallen sharply since then (see Table 2B). This is entirely compatible with the hypothesis that the bargaining power and income share of production workers in manufacturing has fallen throughout the recession, whilst the salaries of many non-manual workers represent fixed overhead costs which inevitably constitute a bigger share of income when output falls. Moreover, in terms of real post-tax pay, manual workers in manufacturing made only minimal gains in hourly earnings and suffered a cut in weekly earnings between 1979 and 1983. Set against the strong rise in productivity, it is evident that manual workers' position has weakened considerably over the recession.

Of course, real wages in the UK have also been affected by changes in the terms of trade; the rise in the value of sterling in 1980 and its subsequent decline has no doubt contributed to the rise and subsequent decline in real manual wages over the same period. But this does not explain the very marked shift in the distribution of income away from manual workers and towards both profits and non-manual earnings. If potential profitability has been boosted by the post-1980 decline in the value of sterling, why have workers not succeeded in bargaining for a share in these profits? The argument put forward here is that mass unemployment has played a key role in undermining workers' bargaining position. Evidence for this hypothesis comes from Layard and Nickell's (1985) econometric study of UK employment and wages 1954-83 which shows that unemployment has a marked depressive effect on real manual wages.

Nevertheless, it is not to evident that it is just the level of unemployment which weakens workers' position. Knight (1983) argues that it is the rate of increase of unemployment which strengthens capital. In particular, workers may be weakened by the threat of the sack which is directly related to the rate of loss of employment. If this is the case, workers may begin to restore their bargaining power and share of income as unemployment levels off. Indeed, the recent years of falling real manual wage rates in the UK do correspond to years of sharply rising unemployment.

## 6. CONCLUSIONS

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I have argued that a key feature of monopoly capitalism is employers' power to maintain price-cost margins in the face of workers' nominal wage demands. If employers do maintain their margins, and if the real terms of overseas trade are fixed, conflict over pay and productivity is transformed in aggregate into inflation. However, although aggregate real profits are impervious to workers' strength (at a given level of real output) if margins are maintained, the profits of individual employers are not so protected. There is ample evidence that in practice margins can be lowered by workers' pressure. I argue that one reason why employers might abandon the "collective good" of inflation is if it is seen to be in the interests of individual employers to bargain over jobs as well as wages; though I also note that that it may be that bargaining over jobs is a concession which workers have to wrest from employers. Whatever the reason, workers' potential ability to squeeze employers' profit margins means that conflict between capital and labour is partly transformed into inflation (thus appearing to set one group of workers against another), partly reflected in the division of income between profits and wages.

The evidence that wages tend to be higher in more monopolistic industries supports the thesis that workers win some share in monopoly surplus (defining surplus as the excess of revenue over opportunity costs, rather than in the Marxist sense). An implication is that workers' class interest in opposing monopoly capital is overlaid by a sectional short-

term interest in the maintenance and enhancement of monopoly power in their own particular industry. This sectional interest is not completely straightforward. Greater monopoly surplus may offer the prospect of higher wages; but if it gives the employers more bargaining power, and restricts employment, the result may be that the industry's workers are worse off.

The evidence that workers' strength can, in part, erode profit margins provides an obvious explanation of why, even under monopoly capitalism, employers in general want to weaken union organisation and bargaining strength. In particular, employers may find that although recession reduces the size of national income (relative to trend growth), their share may increase to such an extent, as a result of the effect of unemployment on workers' bargaining strength, that profits are actually increased by recession. This hypothesis is supported by the evidence that the rise of mass unemployment in the UK 1979-83 has seen a marked shift in the distribution of income : real manual wage rates have suffered their first sustained fall in 30 years; real manual earnings have fallen way behind the growth of productivity; only non-manual earnings have kept pace with productivity growth; the share and the rate of profit has risen to a ten-year record level, above the average level of 1960-73.

Nevertheless, it is not so evident whether workers' bargaining power has been weakened primarily by the level of unemployment or by the rate of change of employment. If the latter, capital's hope must be that recession and the creation

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of mass unemployment have sufficiently altered the organisational and legal position of trades unions to hold back workers' bargaining power when unemployment levels off.



Footnotes:

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- 1/ I interpret their results not as evidence that demand is unimportant in pricing, but rather in support of the hypothesis: a) that oligopolistic industries operate in general with excess capacity and fairly constant short-run marginal costs; b) that they act as profit maximisers; c) that the factors which determine the optimal mark-up of price over marginal cost are fairly stable over demand changes. These factors may be those analysed by Cowling (1981): industrial concentration, demand elasticity and collusion.

Given the assumption of constant returns to variable inputs and if the industry mark-up is stable, we can see that industry pricing will appear to depend on cost changes rather than on demand shifts. For example, an industry may experience a cost rise without knowing whether this is merely a nominal, inflationary rise (with inverse demand rising in proportion) or whether it is a rise in costs relative to demand. In either case, the best response of the monopolistic industry is to apply the optimum mark-up to costs. But it is misleading to claim that prices are based solely on costs, for the optimum mark-up is derived from (conjectured) demand.

- 2/ Strictly, this is true only if the elasticity of substitution between domestic labour and foreign imports is less than unity. Dowrick (1984) shows that if the mark-up is fixed, the elasticity of the wage share with respect to the wage:import-price ratio is given by  $v.(1-w)(1-\sigma)$  where  $b$  is the share of imports in variable costs,  $w$  is wage share, and  $\sigma$  is the elasticity of substitution between labour and imports.
- 3/ Employers have an interest both in reducing wages and in increasing workers' effort and productivity. As a convenient simplification I shall treat effort and productivity as given, and consider only conflict over wages and the level of employment. Alternatively, one can consider the level of employment to refer to the total effort/productive work performed by labour rather than just the number of worker-hours or weeks - so the wage  $w$  is the wage paid per unit of effort. Of course, productivity changes alter capital-output ratios and the real size of aggregate income for a given level of employment. Subsuming conflict over productivity under the notion of efficiency wages does leave the picture incomplete; but it allows a clearer presentation of conflict over distribution.

- 4/ One alternative explanation of Henley's results is that margins are not affected by union pressure, but that higher wages increase labour's share in variable costs (see footnote 2/). However, Cowling (1982, p.170) reports that the aggregate materials : wage-bill ratio for UK manufacturing plants has shown little variability.
- 5/ For exposition and discussion of bargaining models, and of this particular example, see McDonald and Solow (1981) and Svejnar (1982). The bargain can be modelled formally as the outcome of Nash bargaining with variable bargaining power. In the example given here, the level of employment is independent of each side's bargaining strength because each side wishes to maximise the surplus, the excess of revenue over opportunity costs. The conflict is purely over the division of the surplus, and an efficient outcome must have the surplus-maximising level of output and employment. The lowest point (C) on the contract curve represents the outcome if workers have no bargaining power: they receive just the reservation wage. The highest point (C') on the contract curve represents the highest wage the workers can win without driving the employer out of business (but see footnote 6/).
- 6/ I have taken the employers' minimum profit constraint to be the "opportunity cost of capital". However, if the employers' assets are rented or externally financed at a valuation which reflects full monopoly rents, then the economic surplus is removed from the bargaining arena by the threat of bankruptcy. If monopoly rents are fully capitalised the point C' in diagram 2 coincides with point C : workers can neither raise their wage nor erode the employers' margins.
- 7/ However, if either pricing or real aggregate demand is slow to respond to price changes, then wages will increase at the expense of profits, albeit temporarily. Both the studies by Coutts, Godley and Nordhaus (1978) and Sawyer (1983) do indicate that there is a lag in marking up prices, so changes in the rate of inflation might account for some of the variation in profit rates. Moreover, the more the economy is vertically disaggregated, the slower will output prices respond to wage changes.

- 8/ The shifts in the distribution of income which are implied in the bending of the profits curve will have some effect on aggregate demand in the economy and could lead to underconsumptionist arguments that, at high levels of unemployment the relatively high share of profits will reinforce recession due to a low propensity to consume out of profits.
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