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ON THE AVERAGE RATE OF PROFIT IN BULGARIA

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ON THE AVERAGE RATE OF PROFIT IN BULGARIA

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Abstract: A study was conducted regarding the factors and effects of the average rate of profit in Bulgaria. The main variables on which this paper focuses are introduced in the beginning – those being the average rate of profit, the average organic composition of capital, the average rate of surplus value, the growth rate of the labour force, and the growth rate of the GDP. The proposed hypotheses' validity was analysed. The average rate of profit was found to have an upward trend, while a significant linear negative relationship was found between the average rate of profit and the average organic composition of capital; a statistically insignificant positive linear relationship was found between the growth rate of labour and the average rate of profit; a stronger yet not significant enough correlation exists between the labour force growth rate at a time $t + 1$ and the average rate of profit at time t; there is a significant positive linear relationship between the average rate of profit and the GDP growth rate; and a significant correlation was found between the average rate of profit and the average rate of surplus value.

Keywords: average rate of profit; average organic composition of capital; labour growth rate; GDP growth rate; average rate of surplus value

JEL codes: B51; C22; C12; E11

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Introduction

Rate of profit and its hypothesized tendencies

The rate of profit is one of the major economic statistics dealt with in the Marxian school of thought, as it has an important role in the economic growth cycle. First presented by Marx (Marx, 1953), the rate of profit was defined as the ratio between the surplus value and total capital depreciated in the process of production over a given work period. Using the rate of profit, Marx was able to develop his theory that

the rate of profit tends to fall. Since capitalist competition drives technological change, he claims that this decrease occurs as less and less surplus value is being extracted per unit of capital in the production process due to the fact that fewer workers are being used – workers (more specifically their labour) being the source of all value, including surplus value, which is the expansion of capital. This is, of course, based on the assumption that technological change happens in the positive direction, with constant capital (machines, raw materials, etc.) slowly replacing variable capital (the sum of all wages), which might not always be the case.

Factors in rate of profit

Constant capital slowly replacing variable capital can be expressed as the ratio between constant and variable capital, which we Marxists call the organic composition of capital. Knowing this, we can formalise Marx's theory in more mathematical terms by saying: There exists a negative linear relationship between the rate of profit and the organic composition of capital.

Modern studies of the rate ofprofit (Cockshott, 2013) suggest that other factors affect it, as well. Paul Cockshott outlines this in one of his papers, claiming that the rate of profit has an attractor, which depends on the growth rate of the labour force, the rate of cheapening of constant capital, and the portion of surplus being unproductively consumed. Unfortunately, data on the latter two couldn't be found for the case study of Bulgaria, so only the growth rate of the labour force has been included. To clarify why the labour force growth rate affects the rate of profit, it is because the labour force has to grow at the same pace as capital stock in order for wages to remain constant or drop lower. Otherwise, wages will increase as the proportion between demanded and supplied workers shifts in the positive direction, thus lowering the rate of profit as variable capital increases.

Effects of rate of profit

The rate of profit can also be called the growth rate of capital, as r can be multiplied by the used-up capital in a given work period to reach the expansion of capital, also known as profit. As the rate of profit decreases, assuming the organic composition of capital increases, the growth rate of capital decreases – alongside all the other things determined by it, such as the aggregate output growth rate expressed by GDP growth. It is believed that the rate of profit must reach some local minimum, which also means a minimum in the GDP growth rate after which it starts to increase again. This happens as the bourgeoisie destroys the achieved technological progress expressed in the organic composition of capital: that is, they decrease the organic composition of capital as a means to increase the rate of profit. It is believed to be a repeating event, with the growth rate having a cyclical pattern.

Rate of surplus value

Another statistic associated with the rate of profit is the rate of surplus value, also known as the rate of exploitation. It is defined as the ratio between the surplus value and variable capital used in the process of production. I will assume that the rate of exploitation is positively correlated in a linear fashion with the rate of profit, as one would naturally associate a higher surplus value per variable unit of capital with a potentially higher rate of profit, even though the rate of profit is not entirely dependent on the variable capital component.

General objective of the paper

This paper will describe a study conducted with the purpose of calculating the average rate of profit in Bulgaria for the time span 2008–2019, alongside the factors that affect it, those being the organic composition of capital and the growth rate of the labour force. Additionally considered are the values affected by the rate of profit in the country – primarily the GDP growth rate and the rate of surplus value – even though it is possible for the latter to be both a dependent and an independent variable, depending on how the change in its value was induced.

For instance, a capitalist might artificially raise the rate of exploitation by pressuring their workers, thus making the rate of surplus value the independent variable. However, technological change could also cause a change in the rate of exploitation by making fewer workers work on more machines while producing the same or increased surplus value. This would make the rate of exploitation a dependent variable, dependent on the organic composition of capital.

The factors affecting the average rate of profit stated above have been strictly chosen based on studies of Marxian scholars because the rate of profit itself is a statistic defined in the Marxian school of thought as a way to explain economic crises within capitalism that isn't used by scholars from other economic schools of thought. Other schools of thought don't use it since they have no interest in concluding that capitalism's own contradictions will bring about its destruction, which can indeed be concluded via the rate of profit, if analysed further.

Research hypotheses

With an initial assumption that Bulgaria is exhibiting positive technological change, i.e., an increase in the organic composition of capital with respect to time, the following hypotheses were taken into account before this study was conducted:

- $\boldsymbol{H_1}$**:** The average rate of profit exhibits a downward trend.
- $\boldsymbol{H_2}$**:** There exists a negative linear relationship between the average rate of profit and the average organic composition of capital.

- $\boldsymbol{H_3}$**:** There exists a positive linear relationship between the average rate of profit and the growth rate of the labour force.
- $\boldsymbol{H_4}$**:** There exists a positive linear relationship between the GDP growth rate and the average rate of profit.
- $\boldsymbol{H_5}$: There exists a positive linear relationship between the average rate of surplus value and the average rate of profit.

Methodology

Variables

The five economic statistics which require our own calculations are the average rate of profit, the average organic composition of capital, the average rate of surplus value, the labour force growth rate, and the GDP growth rate.

The rate of profit has been defined by Marx in his Capital, Vol. 3 as:

$$r = \frac{S}{K} \quad (1)$$

in which S is the surplus value created in the process of production and K is the total capital depreciated in the production process.

The organic composition of capital (Marx, 1950) is defined as:

$$c = \frac{C}{V} \quad (2)$$

in which C is constant capital (the means of production) and V is variable capital (the sum of all wages).

$The\ rate\ of\ sur$plus value is defined as:

$$s = \frac{S}{V} \quad (3)$$

The growth $rate$ of the labour force is defined as:

$$g(t) = \frac{L(t) - L(t-1)}{L(t-1)} \quad (4)$$

in which $L(t)$ is the labour force at some time, t, and g is the growth rate of the labour force.

Finally, the GDP growth rate is defined as:

$$GDP_g(t) = \frac{GDP(t) - GDP(t-1)}{GDP(t-1)} \quad (5)$$

in which $GDP(t)$ is the GDP at some time, t.

Sample contents

The above are definitions of the rate of profit, composition of capital, and rate of exploitation for a specific industry, not of their averages. The average for each statistic will be calculated through the parameters obtained for more than one industry. However, the second problem of this study is selecting which industries should be included in the calculation of the three statistics.

Clearly, the first thing worth noting is that non-capitalist enterprises should not be included in the calculation because they do not generate any surplus value. Non-capitalist enterprises are those which do not rely on wage-labour, as wage-labour is the source of surplus value that is created by workers in the production process minus the reproduced value of their labour power, which is expressed in their wages.

These include (but are not limited to):

- government-funded public services (healthcare, transportation, education, etc.);
- government-funded administrative services;
- research and educational organisations created with no intent to create profit;
- other non-profit services/organisations.

Secondly, financial and commercial enterprises, such as banks and insurance companies, won't be included in the calculation as they do not create any new value in the economy but merely redistribute wealth[1]. A numerical argument about the latter companies' single role of wealth redistribution can be found in the footnotes.

Real-estate rent will also be excluded because it has the same role as that of financial and commercial enterprises, wealth redistribution. That is because we are assuming that the given individual or company that has purchased a piece of real estate for the purpose of renting it to other people hasn't actually funded the process of production of the given structures (house, apartment, etc.) within the land they own, and therefore they couldn't have extracted any surplus value. The surplus extraction was done by the construction company instead. The rental company is merely buying the given land for the value of the structures on it and then engages in an unequal exchange where the buyer acquires something of less value in material form than what they have paid in monetary form. The latter case is simple wealth

[1] "A may be clever enough to get the advantage of B or C without their being able to retaliate. A sells wine worth £40 to B, and obtains from him in exchange corn to the value of £50. A has converted his £40 into £50, has made more money out of less, and has converted his commodities into capital. Let us examine this a little more closely. Before the exchange we had £40 worth of wine in the hands of A, and £50 worth of corn in those of B, a total value of £90. After the exchange we have still the same total value of £90. The value in circulation has not increased by one iota, it is only distributed differently between A and B" (Marx, 1950, p. 134).

redistribution. Even if we assume that the land has no structures on it, the process of renting that land to others is still considered wealth redistribution. The rental company is basically giving the buyer a piece of land which has no value, as no labour has been put into the production/alteration of what is located there or the land itself, while the buyer is giving the company something of value, money.

Exclusion criteria

Based on the above discussion, an exclusion criterion of which sectors should be included has been constructed. The criteria are displayed in Table 1, with each industry having a value of 1 or 0 being appointed to it. A value of 1 means that the industry will be included in the calculation, while 0 indicates that it is not included. The industries included in the table will be those for which the National Statistical Institute of Bulgaria (NSI, 2008–2022) has provided data. The letter on the left of each industry is the category of that industry, as given by the NSI.

Table 1. Exclusion criteria by industry

Industry		Include (1) Exclude (0)
(A)	Agriculture, forestry, fisheries	1
(B)	Mining industry	1
(C)	Manufacturing industry	1
(D)	Production and distribution of electric and thermal energy, and of gaseous fuels	1
(E)	Water distribution, sewage services, waste management	1
(F)	Construction	1
(G)	Trade; Repair of automobiles and motorcycles	0
(H)	Transport, storage, and postal services	1
(I)	Hotels and restaurants	1
(J)	Production and distribution of information and creative products	1
(L)	Real estate	0
(M)	Professional work and research	0
(N)	Administrative services	0
(P)	Education	0
(Q)	Humane health activities, and social work	0
(R)	Culture, sport, entertainment	0
(S)	Other activities	0

Weaknesses and problems with criteria

Due to the NSI categorisation of industries, which is not in the author's control, the inclusion/exclusion criteria have their weaknesses. Some of the categories provided by the NSI include both non-profit and for-profit activities. Education (P) here might mean both public and private education. Thus, our calculations deviate from the actual statistics, but this was unavoidable considering the lack of more detailed data. In the case of education, it has been excluded because most educational services in Bulgaria are funded by the government. Another such industry would be professional work and research (M). This research and professional work may include both the private and public sectors. For example, no surplus value is extracted from a professor at a government-funded university, as the latter was created for non-profit purposes; on the other hand, a researcher at a pharmaceutical company will obviously have surplus value extracted from them since the company was created with a profit-generating intent. This industry has nevertheless been excluded – based on the assumption that most professional work and research in Bulgaria is associated with non-profit organisations.

There is also an issue with category J, production and distribution of information and creative products. This category includes both entities such as news outlets, which employ wage labourers in most cases, and also individual artists. Individual artists, as merely one example, are people who work for themselves. Therefore, no wage labour is being employed here, which creates no surplus value extraction. For-profit organisations and activities were assumed to prevail in this category, and that is the reason why it has been included in the calculation.

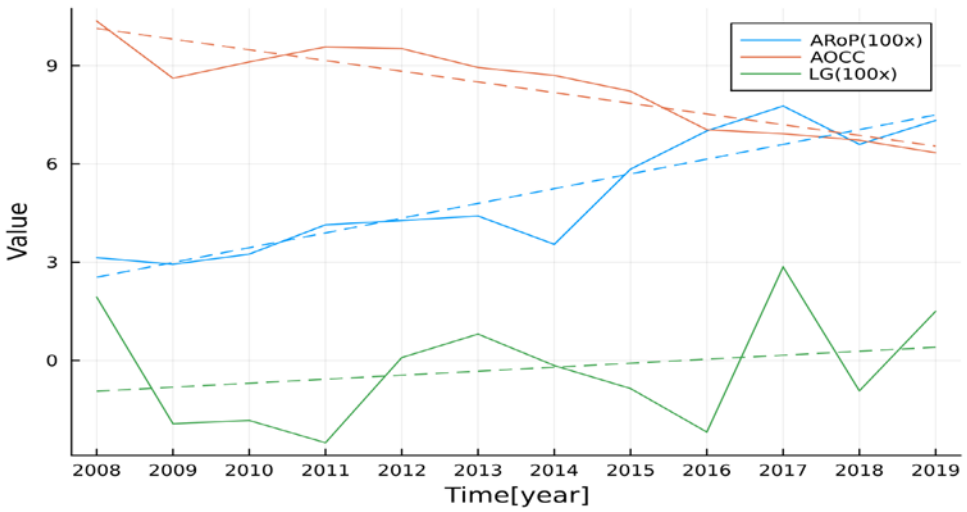
Another problem with the NSI categorisation is the presence of a category with different, unrelated activities: category (G), "Trade; Repair of automobiles and motorcycles". The former is an activity that merely redistributes wealth; the latter is one that actually involves some kind of production process where value is being created. If they had been separated, "Trade" would have been excluded and "Repair of automobiles and motorcycles" would have been included. As this is impossible, the entire category has been excluded because, even though vehicular repair might not be negligible, neither is trade. In fact, it's a big industry in Bulgaria, and trade cannot be included for reasons already outlined.

The last category (S) is ambiguous if judged by its name alone. "Other activities" might be anything, but it has been excluded because if those activities were negligible enough to not be included as separate industries in the NSI categorisation, they are negligible enough to be excluded from the present calculations.

Analysis of results

Factors affecting average rate of profit

With the help of the sources referenced at the bottom of this paper, the average rate of profit, average organic composition of capital, average rate of surplus value, and labour force growth rate have been calculated. The plot of labour growth (scaled by 100), the average rate of profit (scaled by 100), and the average organic composition of capital, with respect to time, can be seen in Figure 1. AOCC, ARoP, and LG in the legend respectively function as abbreviations for the "average organic composition of capital", "the average rate of profit", and the "labour force growth rate". The dashed lines represent the trend lines of the variables whose curves have the same colour.



Source: Author's own calculations based on NSI data – NSI Infostat (a); NSI Infostat (b), and the methodology outlined above.

Figure 1. Plot of the average r, c and labour force growth with respect to time

A few things can be said about the relationships observed in Figure 1. For starters, the ARoP (average rate of profit) and the LG (labour force growth rate) exhibit an upward trend over time, while the average organic composition of capital shows a downward trend – thus disproving the first proposed hypothesis. Looking at the average organic composition of capital and the ARoP, it can be seen that there is a negative linear relationship between the two. It is commonly expected for the AOOC (average organic composition of capital) to increase, since the further development of a capitalist society assumes further growth of labour productivity through technological

change, which is expressed as a change in the composition of capital over time. However, in the case of Bulgaria, we notice the opposite of what is expected. The labour component of capital here is on the rise, which is surprising. As a result, the rate of profit increases. On the other hand, the ARoP appears to have some positive relationship with the LG in some places, so it might be assumed to be linear.

Two linear regression analyses were afterwards conducted, assuming the following two linear relationships:

$$r(c,t) = \beta_0 + \beta_1 c(t) + \varepsilon \quad (6)$$

$$r(g,t) = \alpha_0 + \alpha_1 g(t) + \varepsilon \quad (7)$$

in which α and β are assumed to be some coefficients.

The results of the two linear regressions can be seen in Tables 2 and 3. The linear regression in Table 2 reveals what was already expected, that is, a negative relationship between the two variables, as the approximated negative value of β_1 proves. Further increases in the ARoP are expected if the average organic composition continues with this downward trend. The p-values for the two estimates of the parameters prove the regression is statistically significant, assuming a significance level of 0.05. On the other hand, the regression results provided in Table 3 show a positive correlation between $r(t)$ and $g(t)$, but the approximation of the slope α_1 is shown to be statistically insignificant, judging by the fact that the p-value is 0.34. Therefore, while the labour growth rate plays a role in the determination of the average rate of profit, it is not the most reliable tool to determine the latter – of course, this is only when following the linear model assumed above, which only looks at the given independent variables' effects individually in separate equations.

Table 2. Linear regression of the relationship between $r(t)$ and $c(t)$

	Parameter estimate	Standard Error	t-value	Pr >|t|
β_0	0.151006	0.0173729	8.69204	<1e-05
β_1	-0.0120932	0.00206088	-5.86796	0.0002

Source: Author's own calculations.

Table 3. Linear regression of the relationship between $r(t)$ and $g(t)$

	Parameter estimate	Standard Error	t-value	Pr > |t|
α_0	0.050996	0.00520969	9.78867	<1e-05
α_1	0.305281	0.306655	0.995517	0.3430

Source: Author's own calculations.

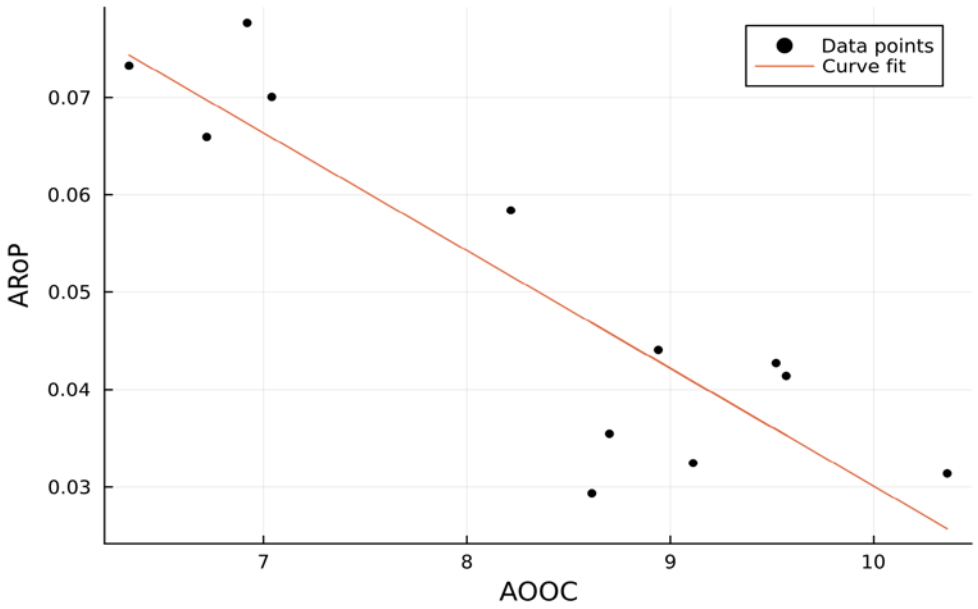
Despite the failure to find a statistically significant approximation of the assumed linear relationship between $r(t)$ and $g(t)$, further analysis reveals that there exists a much clearer relationship between $r(t)$ and $g(t+1)$. Another linear regression analysis has been conducted, revealing the results displayed in Table 4. While the p-value of the coefficient α_1 is still not enough to be counted as significant, it is relatively smaller and provides some support for the initial claims made in the beginning about the LG's effects on the ARoP. Therefore, H_3 cannot be accepted.

Table 4. Linear regression of the relationship between $g(t+1)$ and $r(t)$

	Parameter estimate	Standard Error	t-value	Pr > |t|
α_0	0.0505833	0.00479348	10.5525	<1e-05
α_1	0.534127	0.286055	1.86722	0.0947

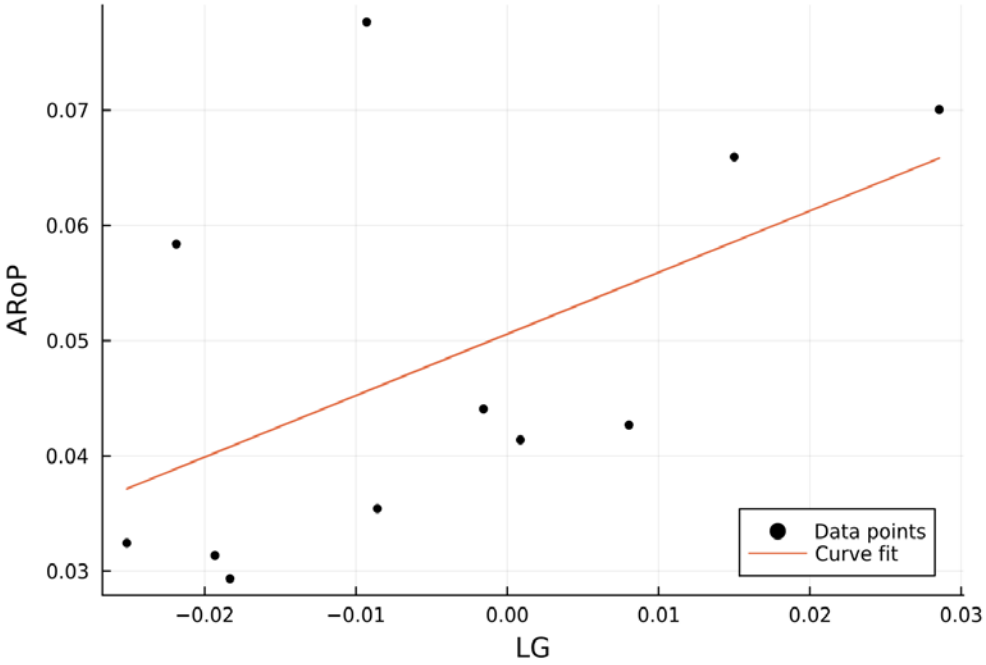
Source: Author's own calculations.

The visual representations of the linear regressions, whose results are shown in Tables 2 and 4, can be seen in Figures 2 and 3.



Source: The calculations from Figure 1 and the estimates from Table 2.

Figure 2. Average rate of profit with respect to average organic composition of capital



Source: The calculations from Figure 1 and the estimates from Table 4.

Figure 3. Average rate of profit with respect to future labour growth rate

A final linear regression model for r was then applied, assuming it to be a function of both $g(t+1)$ and $c(t)$ in a single equation, that is:

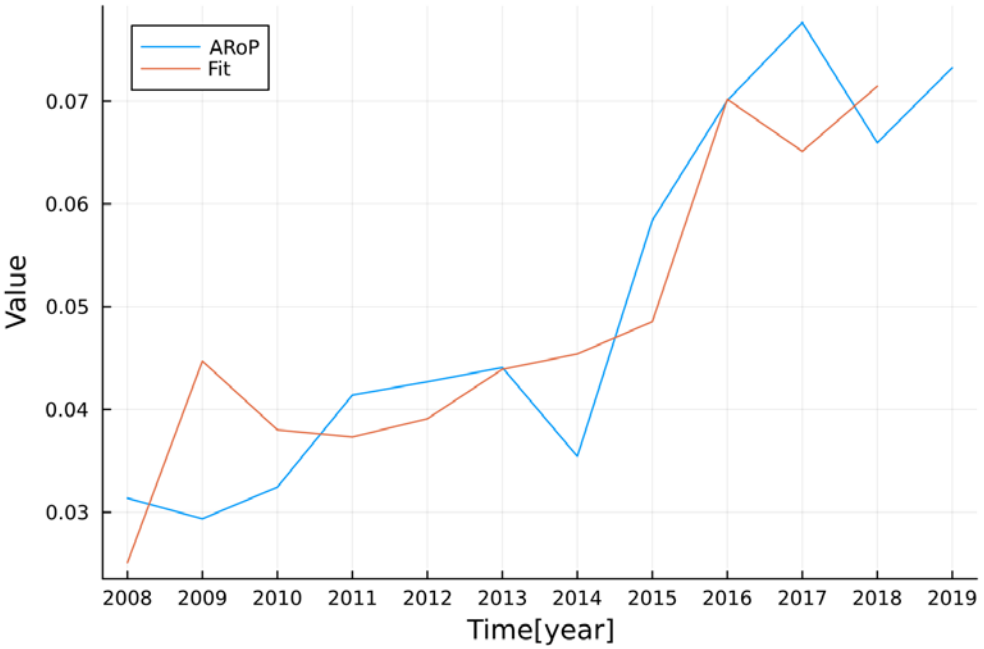
$$r(g,c,t) = \gamma_0 + \gamma_1 c(t) + \gamma_2 g(t+1) \tag{8}$$

The results of the linear regression analysis, assuming the latter model, are presented in Table 5. A visual representation of the approximated fit is shown in Figure 4, in which it is compared to the actual average rate of profit over time.

Table 5. Linear regression of the relationship between $r(t)$ and $g(t+1)$, and $c(t)$

	Parameter estimate	Standard Error	t-value	Pr > |t|
γ_0	0.143805	0.0240193	5.98708	0.0003
γ_1	-0.0111431	0.00284892	-3.91134	0.0045
γ_2	0.169354	0.200765	0.843545	0.4234

Source: Author's own calculations.



Source: The calculations from Figure 1 and the estimates from Table 5.

Figure 4. The ARoP and its approximation with respect to time

It appears that both c and g influence the ARoP in Table 5, but g's approximation is found to be statistically unsignificant. A larger role is once again played by c in the determination of r.

Effects of average rate of profit on GDP growth rate

The GDP growth rate (according to NSI data from 2008 to 2019) has been calculated via Equation 5 with the GDP value representing prices at a given time, t. A linear relationship between GDP_g and r is assumed, that is:

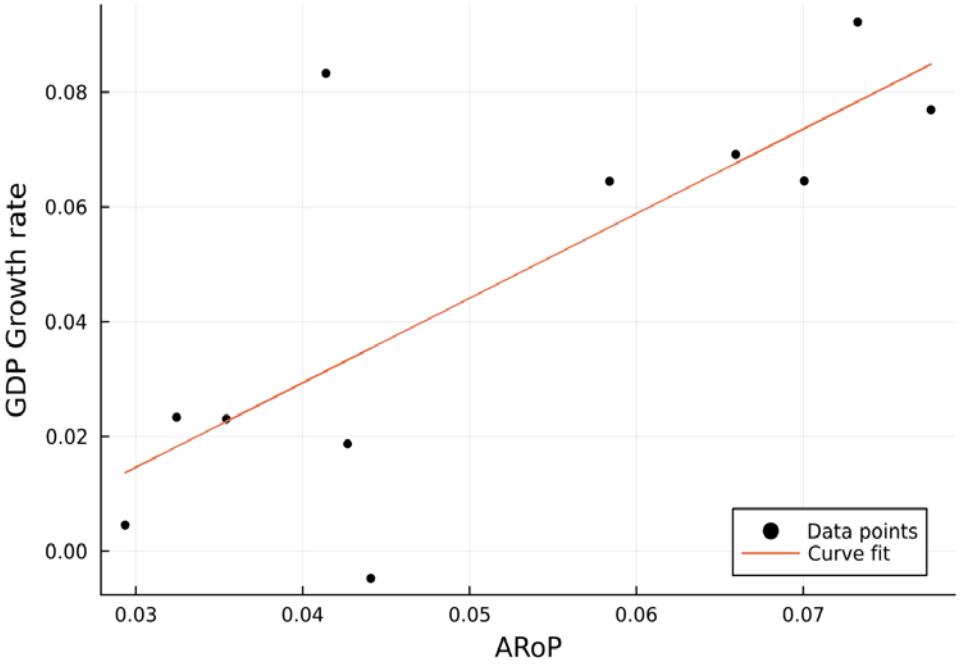
$$GDP_g(r,t) = \delta_0 + \delta_1 r(t) + \varepsilon \tag{9}$$

A linear regression analysis has been applied to it in Table 6. There, the statistical significance of the approximated intercept appears small. However, when looking at the approximation of the slope of the function $GDP_g(r,t)$, a positive linear relationship is visible between the two, with the p-value being 0.007 and indicating strong evidence for such a relationship. A visual representation of the regression is presented in Figure 5. It is expected that further growth in the rate of profit will increase the GDP growth rate.

Table 6. A linear regression analysis of the relationship between GDP_g and r

	Parameter estimate	Standard Error	t-value	Pr > |t|
δ_0	-0.029601	0.0231329	-1.2796	0.2327
δ_1	1.47368	0.424183	3.47417	0.0070

Source: Author's own calculations.

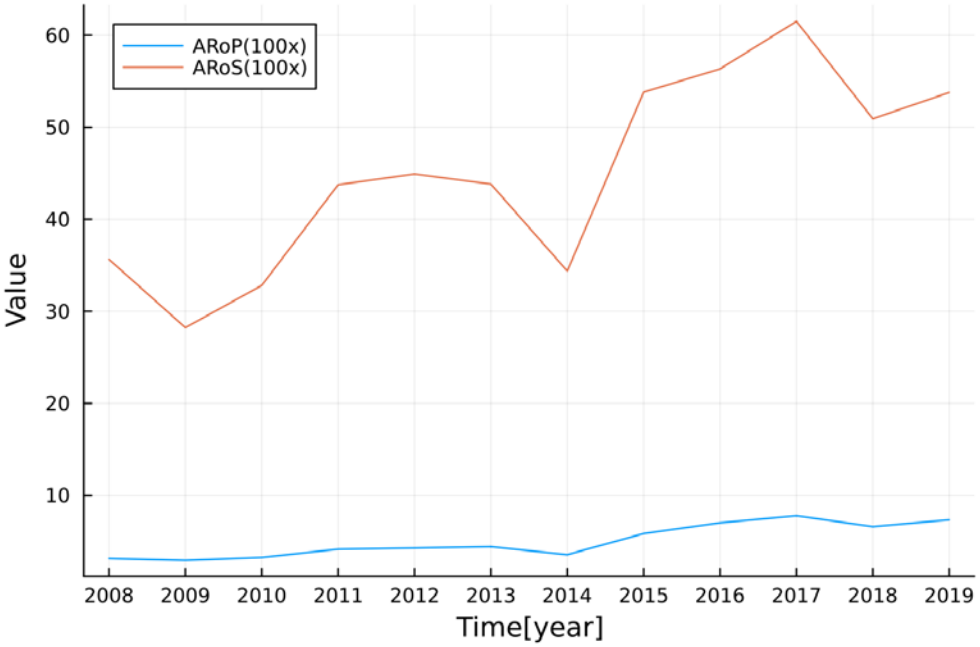


Source: Author's own calculations based on NSI data and estimates from Table 6.

Figure 5. GDP growth rate plotted against the average rate of profit

Average rate of surplus value

The average rate of surplus value has been left as the last thing that this paper deals with since it is uncertain whether its change is a result or a cause. Because of that, only the relationship between it and the rate of profit will be examined. The graphs of the two variables can be seen plotted out in Figure 6 with respect to time. The abbreviations ARoP and ARoS are respectively abbreviations of the "average rate of profit" and the "average rate of surplus value".



Source: Author's own calculations based on NSI data.

Figure 6. The average rate of profit and the average rate of surplus value with respect to time.

An upward trend in the average rate of surplus value can be observed in Figure 6. Its relationship with the average rate of profit appears to be a positive linear one, as hypothesised. To support our hypothesis further, a linear regression analysis test has been conducted (Table 7), while assuming the following linear relationship:

$$r(s,t) = \theta_0 + \theta_1 s(t) + \varepsilon \quad (10)$$

Table 7. Linear regression analysis of relationship between r and s

	Parameter estimate	Standard Error	t-value	Pr > |t|
θ_0	-0.0220104	0.00765267	-2.87617	0.0165
θ_1	0.16045	0.0165969	9.66745	<1e-05

Source: Author's own calculations.

The estimate θ_1 is indeed positive, with its p-value being incredibly small, thus proving its statistical significance. We can accept H_5.

Conclusion

While the exclusion criteria can be debated, as others might argue that a certain industry should/shouldn't be included in the calculation of the three statistics, the conducted study has successfully accepted or rejected all its stated hypotheses, presenting some interesting findings about Bulgaria's economic development.

For starters, in the beginning of the study, H_1 was rejected due to the average rate of profit's upward trend, which was unexpected. Following individual linear regression analyses, both of which have $r(t)$ as the predicted variable, it was concluded that there exists a strong negative linear correlation between $r(t)$ and $c(t)$, thus providing an explanation for the increasing average rate of profit. It refers to a decreasing average organic composition of capital, which appears to be counter-intuitive: a capitalist economy is usually expected to slowly replace human labour with machines. The opposite appears to be happening in Bulgaria. H_2 was accepted as a valid hypothesis.

On the other hand, the linear regression done with $r(t)$ being the predicted variable and $g(t)$ being the predictor showed a positive linear correlation between the two variables; yet it was found that the approximation of the slope of the function $r(g,t)$ is statistically insignificant due to its relatively high p-value. H_3 was disproved, but an alternative hypothesis of H_3 was introduced: a positive linear correlation exists between $r(t)$ and $g(t+1)$. A linear regression analysis showed this relationship to have far greater statistical significance, yet the hypothesis still failed to be accepted. A linear regression analysis with both variables $g(t+1)$ and $c(t)$ included as predictors of $r(t)$ was conducted, which showed the estimation of the rate of change of $r(t)$ with respect to $g(t+1)$ to be statistically insignificant, while the opposite was true for $c(t)$.

The effects of the average rate of profit on the GDP growth rate were studied. A linear regression analysis proved H_4, that the average rate of profit does significantly affect the growth rate of the GDP.

Finally, the correlation between $s(t)$ and $r(t)$ was studied. Linear regression analysis revealed a significant positive linear relationship between the two. It was also found that the rate of exploitation in Bulgaria was on the increase during the analysed period.

Conflicts of Interest

The author has no conflicts of interest to declare.

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