The Capital-Labor Relation:

Contemporary Character and Prospects for Change

By David M. Kotz

Department of Economics

and Political Economy Research Institute

University of Massachusetts Amherst

Amherst, MA 01003, U.S.A.

July, 2007

Email Address: dmkotz@econs.umass.edu

This paper was written for the Second Forum of the World Association for Political Economy (WAPE), on "The Political Economy of the Contemporary Relationship between Labor and Capital in the World," the University of Shimane, Japan, October 27-28, 2007
1. Introduction

In Marxist political economy, capitalism is understood as a mode of production based upon the wage labor relation. That is, the relation between the capitalist class, which owns the means of production, and the working class, which sells its labor-power to capital, is the defining feature of that mode of production.1

The capital-labor relation contains a contradiction. Frederick Engels wrote in Socialism: Utopian and Scientific that the contradiction between socialized production by labor on the one hand and the private appropriation of the product by capital on the other hand contains "the germ of the whole of the social antagonisms of today" (Engels, 1978, p. 704 -- italics in original). He went on to note that "The contradiction between socialised production and capitalistic appropriation manifested itself as the antagonism of proletariat and bourgeoisie" (p. 705 -- italics in original). That is, the relation between labor and capital, and the class conflict between the two, constitute the fundamental contradiction of capitalism. While the form of capitalism has changed in various ways during the 130 years since those word were first written, Engel's claim remains true for contemporary capitalism.

Marx introduced a theory of value and surplus value to analyze the fundamental relation of capitalism. Based on that theory, he showed how capitalist profit originates as surplus value produced by labor but appropriated by capital. In some presentations of Marxist theory, the appropriation of surplus value appears to be a kind of mechanical, or automatic, process. That is, the correct statement, that the capitalist employs labor-power to create a value greater than the value of that labor-power, is interpreted as an explanation of the emergence and appropriation of surplus value. However, that statement is not an explanation of the underlying relations behind the origin of surplus value but rather is a statement of the result of those underlying relations.

Surplus value is created as a result of the relation among three underlying variables: 1) the
length of the workday (or other suitably defined work period); 2) the living standard of the working class, on which is based the value of labor-power; 3) the productivity of labor, which determines how many hours are required to produce the set of goods that makes up the worker's living standard, and which is therefore also, along with workers' living standard, a determinant of the value of labor-power. One can explain the existence of surplus value in any one of three ways: 1) the workday is long, given the value of labor-power; 2) the living standard of the working class is low, given the productivity of labor and the length of the workday; 3) the productivity of labor is high, given the living standard of the working class and the length of the workday. The rate of exploitation (and the rate of surplus value) also is determined by the relation among the above three factors.²

The reason for reviewing the above basic elements of Marxist economic theory is to point out the central role in capitalism of the particular features of the capital-labor relation and the capital-labor struggle. At any time and place, the particular features of the capital-labor relation and the state of class struggle are key determinants of the rate of surplus value and the rate of profit. Marx devoted chapter 10 of volume I of *Capital* to an account of the long class struggle over the length of the workday in England, as an illustration of the central role of class struggle in determining the amount and rate of surplus value (Marx, 1887). However, class struggle affects the rate of surplus value not only through its effect on the length of the workday. Class struggle also affects the average living standard of workers -- often referred to as the real wage -- which is not a fixed and unchanging magnitude.³ While various social and technical factors affect the real wage at any time and place, class struggle is a major determinant of it. Class struggle also affects the third variable, the productivity of labor.⁴

The character of the capital-labor relation forms a basic aspect of each institutional form of capitalism. Historically capitalism has taken different forms at different times and in different locations. That is, while still remaining capitalism, the capitalist mode of production has been
associated with a significant variety of specific institutional structures. This has been expressed in the Marxist literature in various ways. In the early literature, this institutional variation was presented as a theory of stages of capitalism. In chapters 13-15 of *Capital*, Marx analyzes the successive stages of the capitalist production process, from simple cooperation to manufacturing and finally to modern industry. In *Imperialism: The Highest Stage of Capitalism*, Lenin extended the stages interpretation of institutional change in capitalism to include a new stage of imperialism (Lenin, 1939). In recent times the social structure of accumulation theory has analyzed the changing forms of capitalism based on the ways in which a set of institutions affects the process of capital accumulation, through its effect on both the rate of profit and the stability and predictability of profits (Gordon *et al.*, 1982; Kotz *et al.*, 1994).

In this paper, it is argued that the two major institutional forms of capitalism which have predominated during the past sixty years of capitalist history can be understood as alternative ways of structuring the capital-labor relationship and the class struggle. The analysis will mainly draw on the history of institutional change in the U.S. during this period, although reference will also be made to other industrialized capitalist countries. Following this introductory section, section 2 examines the "regulationist" institutional structure that predominated in capitalism for about 25 years following World War II. Section 3 considers the neoliberal institutional structure since around 1980. Section 4 concerns prospects for the future.

Before proceeding, it should be noted that the conception of the capital-labor relation found in Marxist political economy differs sharply from that of neoclassical economics. In the latter theory, labor receives income reflecting its (marginal) contribution to production as well as also providing compensation for labor's (marginal) sacrifice in production. Similarly, capital receives income from production, in the form of interest and/or profit, that reflects capital's (marginal) contribution to production as well as also providing compensation for capital's (marginal) "sacrifice" in production.
That is, capital income arises from the marginal productivity of capital, from time preference, and from risk aversion. The income of capital and labor are entirely parallel in this theory, and there is no surplus and no exploitation. In a sense capital and labor have no relation in this theory, except for "participating" side by side in production. There is no basis for class struggle, since the income of each reflects both the respective contribution and sacrifice of each.

The only way that workers' struggle for higher wages can be understood within neoclassical theory is as an effort by sellers of labor-power to extract "monopoly rents," resulting in an inefficient allocation of resources. In the quite different analysis of Marxist political economy, there is no objective, market-determined, competitive wage rate. In Marxist theory the wage is a product of class struggle over the share of the value that workers produce that goes to workers versus the share that capital is able to appropriate for itself.

2. Capital-Labor Compromise, 1948-73

A specific institutional structure of capitalism emerged after World War II in the industrialized capitalist countries, with related international institutions as well. This institutional structure, or social structure of accumulation (SSA), has been described in detail in a number of works, including Gordon, Edwards, and Reich (1982, ch. 5) and Kotz, McDonough, and Reich (1994, p. 68). The postwar SSA included institutions affecting not only capital-labor relations but also state-economy relations, capital-capital relations (affecting the form of competition), and a new dominant ideology. In all of the major industrialized capitalist countries during that period, the state actively regulated the economy in various ways, competition among capitalists tended to be co-respective rather than unrestrained and cut-throat, and the dominant ideology endorsed capital-labor cooperation, an active state, and "civilized" competition. However, the central feature of that SSA was the relatively restrained and carefully regulated form of class struggle between labor and capital.

In the U.S. case, labor had become very strong during the depression years of the 1930s and
the war years in the first half of the 1940s. The trade union movement grew very rapidly during that period, as millions of industrial workers joined trade unions for the first time. The Roosevelt Administration and the U.S. Congress were largely sympathetic to the trade union movement, passing laws that facilitated union organization. During World War II full employment emerged, further strengthening the labor movement. Once the war ended, and with it labor's wartime no-strike pledge, a wave of militant strikes and other labor protests broke out. Communists and Socialists occupied many leadership positions in the new trade unions, and there was serious talk in the labor movement about forming a new labor party.

During the 1930s big business had fiercely resisted the rising strength of the trade union movement, often with violent methods. When militant labor activity began again after World War II, big business and its allies were able bring about a shift to the right in U.S. politics. Stoking fears of the newly strengthened Soviet Union, along with fear of the advancing Communist forces in China, the right wing succeeded in shifting the public mood against militant trade unionism. Congress passed new labor legislation which limited the trade unions' power (overturning President Truman's veto) and forced the expulsion of many left-wing leaders from the trade union movement.

From this situation there developed a capital-labor compromise, between the more moderate wing of the trade union leadership and the more far-seeing big business officials. With labor's more radical and militant wing having been marginalized, most of big capital informally agreed to engage in collective bargaining with the trade unions. On their side, the unions agreed to limit bargaining to issues of wages and working conditions. They also accepted the responsibility to prevent strikes during what became the standard 3-year labor contract. This capital-labor compromise meant regular wage increases for labor, while for capital it assured continued control of the production process as well as a measure of stability and predictability regarding labor costs.

The class struggle did not disappear. However, it was channeled by the new institutions into
forms that were relatively nondisruptive for capital. Capital had to pay wages that rose over time and make some improvements in working conditions demanded by the unions, but capital received a critically important benefit in return, namely stability and predictability. Capital also hoped its concessions would stave off the threat of radical social change, which had appeared to be looming in the previous period.

The new capital-labor relation, based on compromise between the two classes, was the centerpiece of the postwar SSA. This took different forms in different countries. In some European countries, the trade unions and labor parties played a larger role than in the U.S., constructing a social democratic form of capitalism. However, there were many similarities among the different national versions of the post-war SSA, all based on capital-labor compromise. A key component of the post-war SSA was the rise of a "welfare state," that is, a set of state social programs that benefitted the working class. While this was more developed in European social democracies than in the US, it also arose in the US case. Such programs can be viewed as providing a "social wage," which supplements the wage received directly from the employer. The social wage in that period included such benefits as free or subsidized housing, health care, and education, as well as various types of social insurance covering unemployment, disability, and retirement.

As a result of the institutions that made up this capital-labor compromise, the pattern of capital accumulation that characterized this period included relatively rapid growth in real wages. In the US, the real hourly wage of production workers rose at 2.2% per year during 1948-73, while labor productivity rose only slightly faster, at 2.4% per year. This implies that labor was sharing more-or-less equally with capital in the increases in productivity that occurred during this period.

One might expect that the relative strength of the working class during that period, compared to the earlier period of capitalism, would be problematic for capitalism. However, the quarter-century following World War II is often called the "Golden Age" of capitalism, because it produced,
by many measures, the best economic performance of any period for which data are available. For example, in the USA the growth rate of GDP during 1948-73 was 3.94% per year, the fastest of any long period for which data are available (U.S. Bureau of Economic Analysis, 2007). The growth rate of labor productivity cited above is also relatively high by historical comparison.

High and rapidly rising real wages can have, under certain conditions, a tendency to promote rapid economic progress. Low and stagnating wages discourage the introduction of new labor-saving technologies, while high and rapidly growing wages encourage such innovation. In the late 19th century the US, initially less developed than the Western European economies, rapidly caught up and surpassed them. One factor that promoted the rapid technological progress in the US economy during that period was that the US faced higher real wages than its European rivals, with the gap even larger for unskilled labor. This promoted labor-saving innovation.

3. Capitalist Dominance, 1979 to Today

The postwar SSA began to weaken during 1967-73, and the period 1973-79 was one of transition to a new SSA. Around 1979 a neoliberal SSA emerged, initially in the UK and USA. During the succeeding years the neoliberal SSA spread to many other countries. The U.S. Government was able to shift the main global economic institutions toward neoliberalism in the 1980s, although a neoliberal SSA did not take hold domestically in all of the industrialized capitalist countries. Some of the European social democracies have moved only a small distance toward the neoliberal model, with some weakening of the trade union movement and some cutbacks in social programs, but without entirely adopting a neoliberal SSA.

The neoliberal SSA has involved a new set of institutions affecting all four relations mentioned above: capital-labor relations, state-economy relations, capital-capital relations, and the dominant ideology. The state significantly pulled back from regulation of the economy. Competition among capitalists shifted from co-respective behavior to unrestrained rivalry. A free-market, anti-
state ideology replaced the previous dominant ideology.

However, the central change has been in the capital-labor relation, which was transformed from one of compromise to full capitalist domination of labor. Changes in the other three relations can be understood as means to attain capitalist dominance over labor. Privatization and deregulation greatly weakened the bargaining power of the working class, as did the elimination of, and cutbacks in, social programs. Unrestrained competition led employers to not just resist improvements for workers but to seek to drive down wages and extend work hours. In the UK and the US, the start of the neoliberal era was marked by a state-led attack on a trade union, the miners' union in the UK and the air traffic controllers' union in the USA. In the US, most of big capital abandoned its previous acceptance of trade unions and used every available means to weaken unions and abolish them where possible. Neoliberal ideology insisted that the weakening of trade unions (referred to as the creation of "flexible" labor markets) and the elimination of (supposedly "bloated") social programs were necessary for economic progress.

The effects of the neoliberal SSA can be seen clearly in data on the US labor market during the neoliberal era. From 1979-2000 (through the latest business cycle peak year), production workers' real hourly wage actually declined, by 4.4%. During that period labor productivity continued to rise, by 43% over the period (Economic Report of the President 2007, Tables B-47 and B-49). Thus, all of the benefit of rising productivity growth in the US during the neoliberal era has gone to capital.

The neoliberal SSA has been favorable for capital as measured by distributional change. Not only has capital been able to obtain a larger share of productivity increases (obtaining all of the gains in the US), other measures of inequality have increased rapidly in the neoliberal era. In the US in 2005 the average pay of the chief executive officer (CEO) of a large corporation (in the Standard and Poors 500) was 411 times that of the average worker, an almost ten-fold increase from 1982, when
CEO's were paid 42 times as much as the average worker (AFL-CIO, 2007).

The distribution of household income, which had become somewhat more equal during the preceding period, became rapidly more unequal during the neoliberal era. During 1948-73 the share of total family income received by the richest five per cent declined from 17.1% to 15.5% while that of the poorest 20% rose from 4.9% to 5.5%. Reversing that trend, from 1979-2004 the share of the top 5% rose from 15.3% to 20.9% while that of the poorest 20% fell from 5.5% to 4.0% (Economic Policy Institute 2007). Recent data show that the share of income going to the top 1% has reached its highest level since 1929.9

However, the neoliberal SSA has not produced the promised improvement in aggregate economic performance. GDP growth in the US during 1979-2000 was 3.10% per year, compared to 3.94% per year during the previous SSA (US Bureau of Economic Analysis, 2007).10 Labor productivity growth was 1.73% per year in 1979-2000; using comparable data, labor productivity growth averaged 2.77% per year during 1948-1973 (Economic Report of the President 2007, Table B-49).11

4. Prospects for the Future

According to the Marxist view, the contradictory nature of the capital-labor relation cannot be permanently overcome within the capitalist system. An SSA can effectively regulate the capital-labor relation in a particular way for a period of time, but eventually the contradictory character of that relation reasserts itself and the SSA ceases to operate effectively. That sets the stage for a transition in the institutional form of capitalism.

Thus, the post-World War II SSA, based on capital-labor compromise, may have produced relatively rapid economic progress for a period of time, but after some twenty-five years its contradictions sharpened, leading to its decline and, in many capitalist countries, its replacement by a neoliberal SSA. Most analysts believe the key contradiction of the postwar SSA was the relatively
strong position of the working class, which eventually produced problems for capital and led to a declining rate of profit and growing economic instability.\(^\text{12}\)

The neoliberal SSA also has contradictions, although they are different from those of the previous SSA. One can cite three important contradictions of the neoliberal SSA. First, the lack of bargaining power of the working class may be good for capital by bringing a high rate of surplus value, but it simultaneously creates a potential realization problem. That is, with profits rising rapidly while real wages stagnate or decline, a problem arises of how to sell the rising output during an economic expansion. The problem of overproduction always looms in a neoliberal SSA, and this tends to grow more severe over time (Kotz, 2008).

Second, the growing inequality in a neoliberal SSA, combined with the weak regulation of the financial sector, tends to set off speculative bubbles in various assets, such as securities and land. This can promote rapid economic expansion for a time, but it creates the possibility of a severe financial crisis.

Third, as Mao Zedong pointed out, "Where there is oppression, there is resistance." The high rate of exploitation of the working class in a neoliberal SSA tends eventually to provoke resistance in various forms. The threat of intensifying class conflict creates instability that can undermine the neoliberal SSA.

The neoliberal SSA has now been in existence for more than twenty-five years. A recent paper (Kotz, 2008) argues that, at least in the US, the contradictions of neoliberalism may be sharpening sufficiently that neoliberalism may not be able to survive much longer. While transition periods are difficult to foresee in advance, there are some signs that we may be entering such a period on a world scale. If that is the case, then there may be a prolonged period of crisis and instability, followed by the emergence of a new institutional form of capitalism that would replace the neoliberal SSA. If a new institutional form of capitalism does replace neoliberalism, the nature of
that new institutional form cannot be determined in advance but depends on the course of political struggles among various classes, class segments, and groups.

However, the crisis period of an SSA does not necessarily lead to a new institutional form of capitalism. Since 1980 the neoliberal SSA has brought worsening conditions for the majority, which has tended to undermine support for capitalism itself. After a long historical period in which capitalism, despite its contradictions, brought a certain kind of progress, the neoliberal era contains indications that capitalism is now holding back human progress rather than promoting it. If neoliberal capitalism is now entering a period of crisis, the possibility exists that it will give way, not to another institutional form of capitalism, but to new efforts to go beyond capitalism and build a socialist system. Indeed, we have recently seen new attempts to build socialism in South America.

Marxist political economists should not limit their activities solely to the analysis of capitalism and how it evolves. If our analysis suggests that new possibilities may be opening up to challenge capitalism, we should act on that analysis. We should be involved in the struggle over the future direction of the global political economy, contributing toward the eventual replacement of capitalism by socialism, which is the only system capable of fully meeting human needs.
References


Notes

1. Other features of capitalism include that it is a system of commodity production and that the aim of production is profit. Neoclassical economics regards capitalism as simply a system of commodity production (a market economy) based on private ownership of the means of production.

2. The rate of profit is partly determined by those three factors, but it is also affected by other factors such as the organic composition of capital, the turnover time of capital, and the conditions for the realization of the value created in production.

3. In a simple model, the real wage is the same as the living standard of workers. However, the two are not identical if one takes account of goods and services that are necessary for the reproduction of the working class but which are not purchased from the wage. These include goods and services that are provided socially or via unpaid domestic labor. These relations can also affect the rate of surplus value.

4. Technological progress is of course a major determinant of the productivity of labor. However, class struggle affects technological progress. Furthermore, class struggle affects the intensity of labor, which in turn affects output per labor hour within any given technology.

5. A similar analysis of social structures of accumulation is found in Wolfson (2003).

6. The neoclassical theory of capital income has serious conceptual problems, which were explored in the famous "Cambridge Capital Controversy" which pitted Cambridge, UK (which criticized neoclassical capital theory) against Cambridge, Massachusetts (which defended it).

7. The two growth rates cited are from Economic Report of the President 1988, p. 298, 300. Below we cite a slightly different figure for labor productivity growth during that period, of 2.77% per year, when the object is to compare labor productivity growth during 1948-73 with the rate for 1979-2000. The higher rate for 1948-73 was due to a recent revision by the Bureau of Labor Statistics in the series for labor productivity growth. However, the earlier series for labor productivity growth is the appropriate one to use for comparison to the rate of wage growth during 1948-73.

8. The US had a labor shortage during that period, since, unlike in much of Europe, it did not have a large impoverished class of peasants that could be drawn into wage labor at low wages. Also, in the late 19th century it was still possible for workers to become farmers by moving to available land in US West. On both accounts, the relatively high living standard of small farmers in the US, compared to that of European peasants, tended to elevate the wage level in industry.

9. In 2000 and again in 2005 the richest hundredth of one percent (0.01%) of families in the U.S. received 5% of total income, a level that had been not been reached previously since 1929. During the 1950s and 1960s the share received by the top 0.01% was 1% to 1.5% of total income (Piketty and Saez, 2007).

10. From 1979 to 2006 the GDP growth rate was 2.97% per year.
11. For this comparison, the latest (revised) data series from the US Bureau of Labor Statistics was used, to get an appropriate comparison. In these data, labor productivity growth during 1948-73 was somewhat faster, at 2.77% per year, than in the earlier data cited, of 2.4% per year. For the entire neoliberal era to date, 1979-2006, labor productivity growth was 1.97% per year.

12. For example, see Bowles *et al.*, 1990. There were other contradictions of the previous SSA. For example, in the international arena, its international institutions depended on the unchallenged economic dominance of the U.S., which was a temporary result of World War II. The law of uneven development eventually brought several US competitors close to economic parity with the US, which caused the Bretton Woods monetary system to collapse in the early 1970s.