
PROFITS . . .

and the Profit Motive

IN recent years a tremendous barrage of criticism has been hurled against the profit-motive. This criticism, a large part of which is the product of emotion rather than reason, has had the inevitable effect of increasing public suspicion and disfavour of profit-seeking and of dangerously weakening the fortifications of enterprise in all its forms—private, public and personal. The results of this are to be seen in the facts of the post-war situation—in the fact that public companies on the average have to be content with little more than half the “real” profit* they enjoyed before the war, in the disinclination of the worker to work overtime because the extra earnings after taxation are regarded as hardly sufficient to compensate for the extra effort, in the reluctance of many professional men to undertake more than a limited volume of work, and in the growing practice among younger men to seek in their careers security rather than risk and adventure.

There are few subjects about which there is greater misconception than profit and the profit-motive. There is probably no subject in which ignorance can do greater economic and industrial harm and on which unprejudiced and unclouded thinking is, therefore, more necessary.

Distinction Between Profits and the Profit-Motive.

In the first place in a great number of minds the profit-motive and business profits, particularly the profits of public com-

*Profit in terms of the goods and services it will purchase.

panies, seem to be regarded as identical. In fact, business profits are one aspect only, and a comparatively minor aspect, of the profit-motive. Except for a very small minority, all men—and not merely those who live by business profits and no matter whether they dwell in Australia, the United States or Soviet Russia—are actuated to a greater or lesser degree by the profit-motive. All men, with few exceptions, work for personal gain, and all men, with few exceptions, desire to increase the rewards they receive for the work they perform. This applies as much to the unskilled labourer as to the top business executive, as much to the tram-conductor as to the head of the tramways board, to the chef as to the cafe proprietor. In fact—and there is irony in this—there is probably no organisation more strongly founded on, and inspired by, the profit-motive than the trade union movement itself. At least the profit-motive is just as powerfully at work in the ranks of trade unionism as in those of employer organisations.

Profit-Motive Not Immoral.

Nor is this to be condemned on moral grounds. That a man should strive to increase his income in order to provide himself with the means of a fuller material and cultural existence, is altogether natural and wholly to be commended. In fact this urge to self improvement has been the driving force behind a great deal of the material and technological progress of mankind. There are of course some people, but their numbers are compara-

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tively small, who seek money and riches for their own sake or for ignoble ends—for the satisfaction of gross material pleasures, for the sheer joy of flaunting their riches in the face of the less fortunate, or for personal aggrandisement and the power money gives them over their fellow men. But for every human being of this kind, there are probably a thousand who desire money for nobler purposes—for the security and comfort of their wives and children, the improvement and beautification of their domestic surroundings, the opportunities it provides for better education, for the realisation of philanthropic and social ideals.

The profit-motive, the desire for personal gain and material betterment, is one of the elemental instincts of man. Kept within reasonable bounds it is not immoral, it is not against the interests of society, and it will continue to be active no matter what the form of the political and economic organisation. In a society in which all industry was owned and run by the State, there would still be wage-earners desirous of increasing their wages, managers and executives of raising their salaries, and engineers and musicians, and yes, even politicians, of obtaining greater rewards. The problem of securing economic and social justice does not consist in the elimination of the profit-motive—an aim which, being opposed to the fundamental nature of man, is entirely impracticable—but in distributing the product of human effort on a just basis in proportion to hard work, skill, enterprise, risk and social need and significance.

The profit-motive is not, however, the only motive animating men in their economic pursuits. There are at least two

others. One is the desire to give service; another is the desire for power. Both are present, in greater or lesser degree, in most men and both like the profit-motive can be—but need not necessarily be—a powerful influence for social and economic improvement.

The Motive of Service.

The motive of service is not the exclusive possession of a few saints. It is widely spread throughout the community. When a crisis such as a major war hits a nation, the motive of service becomes paramount, and hundreds of thousands of people can be found who are ready to sacrifice their own personal interests and even their lives for the good of the State. There is, in fact, present in most people a great latent capacity for selfless service. This capacity is not necessarily destroyed or submerged by the profit-motive. The two motives are not mutually exclusive. The urge to achieve a more comfortable livelihood and fuller life for oneself is not necessarily incompatible with the wish that other people should also have the opportunity and means of a better existence. The business leader in his ambition to build a great business enterprise is not seldom motivated by the ideal of service at least as much as by the pursuit of profit. Nor is the wage-earner clamouring for higher wages necessarily without a sincere desire, and often a great capacity, to serve his fellow men. A man is not black or white according to whether he happens to be a director of a big business or a dustman, a capitalist or a socialist. The idea that employers as a class are self-seekers, untouched by any finer ideals than that of personal profit, and that wage-earners as a class are selfless,

disinterested idealists untainted with the desire for personal gain, is utterly false, but it seems to exert a tremendous influence over present-day economic and political policy. The proportion of bad to good wage-earners is probably identical with the proportion of bad to good employers. The sooner we begin to think of men as individuals instead of men in the mass, the sooner we will commence to find real solutions for economic and social problems.

The Power Motive.

In impelling men on to greater efforts and achievement the attraction of power is possibly just as important as the lure of profits. And, like the profit-motive, the power-motive is not good or bad in itself. It becomes bad when the desire for power is so powerful that it submerges all other motives, and when power itself is applied to evil or ignoble purposes. There are few men who have attained to the topmost flights in industry that have not engrained deeply in them the love of power. But it is also true that the successful union leader at the head of a union whose membership may run to tens of thousands desires power and enjoys its exercise equally as much as the managing director of a business with capital resources amounting to millions of pounds. The real test of the value of power is whether it is wisely exercised.

Mixture of Motives.

The human being is a strange and complex mixture of many, and often contrasting, motives and instincts. In one man one motive will predominate, in other men it will be insignificant. These three motives, the desire for profit, the desire for power, the desire to serve, are present, and will remain present, in varying degrees in practically all men, no matter to

what section of the community they belong, no matter what the political form of the society in which they live and have their being.

Business Profits.

In the minds of most people the profit-motive is identified with the profits earned by business, particularly the profits of the larger public companies to which a great deal of publicity is given in the daily press. As we have seen, this idea is fallacious. It leads those who see no purpose in, or justification for, business profits to a sweeping condemnation of the profit-motive as such. One might as well pass sentence of guilt on man himself.

Business profits are one aspect only of the profit-motive.

Functions of Business Profits.

What useful functions do these profits perform?

1. **Incentive to Achievement:** First of all they provide an incentive to achievement. They encourage men to create and build, to show enterprise, to produce new and better products, improve methods of production, raise efficiency and reduce costs, expand markets, provide better service, invest and risk capital in new forms of production. This incentive function of profits is, however, probably less strong in the large public company than in the small private company, partnership, or one-man business. In the smaller business the connection between effort and enterprise on the one side and reward on the other is much more direct than in the large concern. Very often the driving force behind an ambitious programme of expansion undertaken by a large public company springs from one or two top executives who do not stand to benefit financially in anything like the degree to which

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their efforts would seem to entitle them. In the development activities of the large organisation, the motives of power, of national service, the sheer joy of adventure and satisfaction in achievement play a large part.

2. Test of Efficiency: This, however, should not be taken to mean that profit performs no function of value in such concerns. In these, as in smaller businesses, profit is a test of efficiency. The most efficient business, the one that provides the highest quality products at the lowest cost is in general the one that makes the most profit. This, of course, is not universally true. In a monopolistic business, or in an industry in which the firms have banded together to fix unfair minimum prices and eliminate competition, profit need not be, and very often is not, any indication of outstanding efficiency. Nevertheless, the business which makes the highest profits is not infrequently the one that gives the best service to the community. This is a fact very often overlooked.

3. Index of Demand. Thirdly, profit, actual and prospective, is one of the means by which the business man is informed of the changing desires and tastes of the consumer. When profits in a particular industry rise, other things being equal, it is often a broad indication that the public is prepared to consume more of the things that the industry produces. When profits decline, the business man knows that he must tread warily, and possibly reduce his production of the things on which losses are being incurred.

4. Attract Savings: Fourthly, profits are the means of attracting savings into industry—high profits are the means of enticing capital into new, risky, but often socially beneficial forms of production. Profits provide the fund out of which interest on their investment is paid to those

prepared to place their savings at the disposal of industry in the hope of obtaining a reward. It is these savings which make possible the expansion of capital equipment and the improvement of industrial efficiency. Experience confirms, and modern economic theory accepts, the proposition that the standard of life of a people depends very largely on the extent and quality of its productive capital equipment. The average level of profits should therefore be sufficient to ensure an adequate flow of savings into industry. It is no accident that the high-profit economy of the United States is also the one with the greatest amount of physical capital per head of the population, and the one able to pay the highest real wages to its workers. If we are to achieve a higher level of wages, there must be more capital. High profits and high real wages are not, as is commonly supposed, mutually exclusive. They are in fact two sides of the same coin—the coin of national prosperity. This is a truth that needs to be well absorbed by both capital and labour, as well as by governments.

5. Providing Reserves for Capital Development: The development of the capital resources of industry is financed not solely by the savings of tens of thousands of shareholders. A very substantial part is financed directly out of business profit itself. This is the fifth function of profit. All the profits earned by industry are not paid away as dividends to shareholders. A big proportion, in the larger public companies amounting on average to something like 15%, is retained in the business, and much of this is used for the purchase of additional plant and equipment. It is as much in the interest of the community as in that of business that this

should be done, for it provides a direct and simple method of financing the countless small improvements and additions to processes and equipment that are for obvious reasons unsuitable for financing by the issue of new shares or debentures.

6. Reserves for Hard Times: Finally most prudent businesses set aside some of their profits to build up reserves that can be called upon in the event of hard times. These reserves can give long-run stability to a business, and, if properly used, can assist it to maintain its labour force at the maximum numbers when sales fall off and production has to be curtailed. In fact the contribution which business as a whole might make to alleviating the consequences of trade depression through the intelligent use of reserves built up in good times out of profits is a subject to which far too little attention has been paid in the past and to which a great deal of study might beneficially be devoted by businessmen themselves.

Excessive Profits.

One of the most widespread and tenaciously-held misconceptions about profits is that they are excessive and far greater than is necessary for the efficient conduct of industry. It would be idle to deny that there are many instances of unnecessarily high profits. The business man, like the vast majority of other men, is no paragon of virtue and if he sees the opportunity of increasing his profits, even though they may already be more than adequate, he will generally grasp it. But though there are cases of excessive profit-making, altogether they add up to no more than a very minor part of business as a whole. Over the whole field of industry, taking into account bad years as well as good, losses (which are by no means infrequent) as well as gains, the average level of business profits is astonishingly moderate. Statistics published by the Commonwealth Bank suggest that the average return on capital

invested in industry is something of the order of 5% to 6%.

The evil of excessive profit-making—of profiteering—remains, however, and must be unreservedly condemned. The best protection against profiteering is to be found in a lively vigorous competition. Where competition is impracticable or non-existent there is a case for some government oversight and control of the level of profits. But discrimination is needed. There is always a grave danger that a localised assault on profiteering will develop into a general large-scale attack on all profits with disastrous consequences for the economy.

The attempt by the Commonwealth Government in 1942 to eliminate profiteering during the war by imposing an overall ceiling on profit of 4% on capital employed is a case in point. When the proposal came to be examined in detail, the impracticability as well as the injustice of placing an arbitrary upper limit over all profits became apparent and the Government wisely decided to abandon the scheme. The main reason for abandonment put forward by the Prime Minister, the late Mr. John Curtin, was that the plan would have had the effect of imposing an impossible tax burden on the small shareholder. He pointed out that there were 300,000 shareholders in Australia with incomes below £250 a year and that insuperable difficulties had been encountered in providing for a just application of the profit limitation.

In this announcement the Prime Minister made the significant admission that he had yet to discover the correct definition of "excessive profits." It is in fact impossible to limit profits to an arbitrary standard rate without committing mani-

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fest absurdities and gross economic injustices. Is the new risky speculative business to be permitted no higher profit than that earned by the old well-established organisation? Is a highly competitive business to be placed on the same basis as a monopoly? Is the efficient business to be allowed no greater profit than the inefficient? Is the gold mining company to be restricted to the same rate of profit as the company supplying an essential service? Is the pioneer and inventor to get no special reward for years of sacrifice and arduous work? Excessive profit cannot be decided only by the rate of profit on capital employed in the business. It can be determined only by reference to all the economic circumstances surrounding the business. These circumstances vary widely between each industry and often between individual firms in the same industry.

Profit A Means Not an End.

Profit is not as is commonly thought the sole objective of business. Strictly speaking it is doubtful whether it is an objective at all. It is a means to an end, not an end in itself. It provides the businessman with a means of estimating the market for his product, of providing his employees with security and better conditions of employment, and of rewarding those people who are prepared to place their savings in his care. To quote a standard text book on management, "Profit can no more be the objective of a business than eating is the objective of living." But without eating there is no life and without profit there is no business—at least no business under the private enterprise system.

Business Man Partly to Blame.

For the suspicion and hostility surrounding business profits the businessman himself must bear a large share of the blame. He has never made an organised and well-considered attempt to explain the nature and composition of profits to the public. On the contrary he has tended to surround the whole subject of profits with a cloak of secrecy. He usually presents his financial reports in such a way that their real meaning is clear only to the skilled interpreter of accounts. He frames his profit statements mainly to meet the needs of the shareholders, not the requirements of his workers and the public. Only recently, and then only in rare cases, has he attempted to explain his profits more fully and simply to his employees and show the proportion they consume of the total revenue of his business. The ordinary citizen reading the headlines in the financial press since the end of the war can hardly be blamed if he is under the impression that company profits have seldom been higher. He would be surprised indeed if he were told the truth—that the post-war level of profits is probably less than two-thirds of the pre-war level.

There are few more urgent needs in industry than the need for franker and fuller information about profits. If private enterprise neglects to take the initiative in this, governments should consider exercising compulsion. For such compulsion would be in the interests of business itself and of more accurate and realistic economic and political thinking. As a leading journal* has excellently put it "The aim would be not to convict industry of sin, but to clear it of unfounded suspicion."

*"The Economist," 27/7/46.

