PROFITS and PRICES*

IT HAS recently been argued that increasing industrial costs arising from the 40-hour week and from mounting wage levels can be paid for out of profits; in other words, can be absorbed by industry without being passed on to the consumer in higher prices. This argument is, of course, rendered absurd by the simple logic of arithmetic. **If all the costs accruing from the 40-hour week, recent increases in wages, and from other causes, were to be met from company profits, there would soon be no profits at all, but losses throughout the length and breadth of industry.**

Moreover, this kind of argument plainly springs from a fundamental misconception of the contribution made by profits to the industrial virility and progress of the nation.

Private enterprise, which comprises probably about 80% of all economic activity in Australia, is undertaken for the purpose of profit. Whilst it is true that that is not its sole, nor even its main, purpose, it is true also that without the incentive of profit there would be no private enterprise at all. As wages are the reward for work, profits are the reward for risk and enterprise. When profits are high there is a much greater inducement for people to undergo risks and to participate in enterprise than when profits are low. Out of the productive activity which springs from those who serve the community by maintaining and launching new industrial enterprise, wages are paid. **It is completely false to think that wages and profits are mutually antagonistic; that if profits are high, wages must be low and conversely, that if wages are high, profits must be low.** The truth is just the opposite. **Good profits are the complement of high wages and high wages of good profits.**

The United States' economy at the present time provides a unique demonstration of this truth. Wages and profits are both at record levels, because, and only because, economic activity and production are at record levels.

Good profits are, of course, not the same thing as profiteering, which should be fought with every weapon that the State can command. Nor are profits identical with the incomes of rich men. Whilst many rich men derive part of their income from profits, multitudes of people, including many in retirement, who by no stretch of imagination could be regarded as wealthy, also draw income from profit.

When people speak of profits they think usually of those earned by industrial companies. Now, all the recognised statistics published by authorities such as the Commonwealth Statistician, and the Commonwealth Bank, prove three things:—

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First, that company profits are today taking a much smaller share of the total national income than before the war, while wages and salaries together are taking a much larger share; second, that if it were practicable without destroying initiative and enterprise (and of course it is not) to divide up among the community the income from company profits, the position of the individual would be little improved; and third, that the level of real profits is today much lower than before the war.

The first contention is proved by the following table:—

PER CENT. OF NATIONAL INCOME

	Company Income After Tax.	Undistributed Profits (Residents in Australia).	Dividends before Tax on Shareholders (Residents in Australia).	Wages and Salaries before Tax.
1938-9	9.1	3.0	4.2	54.3
1946-7	6.9	2.8	3.1	59.8

The suggestion, therefore, that increasing costs should be met without any rise of prices involves, in effect, a still smaller share of the national cake for profits and a still larger share for wages.

In any case, it is a mathematical impossibility for industry as a whole to pay these costs without increasing prices. **It has been authoritatively estimated that the cost of the 40-hour week will approximate to £50m. a year and recent basic wage increases to about £30m. But the National Income statistics published by the Commonwealth Treasurer show that total net profits of companies, after taxation has been paid, to be about £80m.**

Of the £40m. distributed in dividends to shareholders about one third is paid away in taxation, leaving, say, a net £30m. Spread equally over the whole population this sum would provide an extra 1/6 a week for every man, woman and child; spread over all workers about an extra 4/- or 5/- a week.

The remaining profit (£40m.), put aside to reserves and used for plant modernisation and development, could, of course, not be distributed **under any system** without catastrophic effects on the standard of living. These profits eventually add to the capacity of industry to pay high wages by improving productive efficiency. The industrial predominance of the United States is in large part due to the exceptionally large savings out of profits applied to purposes of capital development. These profits or any large part of them could only be distributed among consumers, either directly or in the form of lower prices, at the cost of industrial progress and future standards of living.

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The latest report of the Income Tax Commissioner shows profits earned by all companies engaged in manufacturing to be as follows:—

Taxable Income	£62m.
Less Company Taxation	£20m.
Net Company Income	£42m.

Assuming, as the National Income statistics suggest, that half these profits are ploughed back into industry, £21m. remains for distribution to shareholders. But the Income Tax Commissioner only allows them on average to retain about two-thirds of this; therefore, a net £14m. is paid to shareholders in manufacturing companies. Distributed among the 760,000 people employed in secondary industries, this sum would increase their pay by 7/- a week, but wages would eventually be drastically reduced because of the destruction of enterprise over a large part of the economy. In the light of these facts, is there anything in the glib statements by soap-box orators and extremist agitators of the mythical millions robbed from the workers in profits.

The comparatively minor proportion profits comprise of the total costs of industry may be gauged from the following figures showing the actual distribution of each £1 of company turnover for three large companies.

Company.	Wages.	Materials.	Other Expenses.	Taxation.	Divs.	Reserves.
Holeproof Ltd.	6/11½	10/-	1/8	9d.	4d.	3½d.
Felt & Textiles Ltd.	3/7	13/2	2/3	5½d.	6½d.	
E. T. Brown Ltd.	7/-	7/3½	3/7	11d.	6d.	8½d.

Similar figures published by the Commonwealth Statistician for secondary industry show the following break up of each £1 of turnover.

	Wages.	Fuel and Materials.	All Other Items.
1938-9	4/3	11/10	3/11
1945-46	4/9	11/10	3/5

The margin for all other items includes allowances for depreciation, all overhead expenses such as insurance, advertising, and interest, and profits and taxation. It will be observed that for every £1 of sales, wages have increased their share from 4/3 to 4/9 since 1939 at the expense of the third item.

The amounts of the individual cost actors which go to make up the sum of his third item cannot be exactly assessed. n examination of company accounts sug-ests, however, that net profits and taxa-ion absorb about 50% of this sum, while epreciation and overhead account for the emaining 50%. The split up of every £1 f turnover of secondary industry in 945-6 would therefore be something like his:—

Wages	4/9
Materials, etc.	11/10
Other expenses	1/9
Taxation	8d.
Dividends	6d.
Reserves	6d.

It is clear that if wages were increased vithout any increase in prices, some other tem would have to be reduced—that is, ssuming productivity remains the same s at present. If the cost of fuel and naterials were reduced owing to more fficient production, wages could be in-reased without raising prices. Similarly f taxation were cut down wages could be ncreased without any rise in prices. But if taxation and the cost of materials are not reduced, then any increase in wages could only be paid for out of profits. And as the reserve section of profits could not be seriously disturbed without affecting industrial productivity and progress, dividends would have to bear the brunt of the wage increase. A rise in wages of 10% would be sufficient to wipe out completely the shareholders' return. Since taxation on average takes about one-third of shareholders' dividends, there is really little, if any, scope for increasing wages by this method, without destroying the whole foundations of enterprise in this country.

There is one way, and one way only, that a really worthwhile increase in wages can be achieved without higher prices, and that is by increased productivity.

Statistics compiled by the Commonwealth Bank which show that the percentage rate of company profits on shareholders' funds—after provision for income tax—has declined from an average of 7% for the three years 1937-39 to 6% for the three years 1944-46. Allowing for the fall in purchasing power of the £1 since the pre-war year, this represents a reduction in the real rate of profits of over 40%.

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