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Profit Share in Income: An Analysis of Its Influence on Macroeconomic Performance

Authors : Alain Villemeur

Abstract : The relationships between the profit share in income on the one hand and the growth rates of output and employment on the other hand have been studied for 17 advanced economies since 1961. The vast majority (98%) of annual values for the profit share fall between 20% and 40%, with an average value of 33.9%. For the 17 advanced economies, Gross Domestic Product and productivity growth rates tend to fall as the profit share in income rises. For the employment growth rates, the relationships are complex; nevertheless, over long periods (1961-2000), it appears that the more job-creating economies are Australia, Canada, and the United States; they have experienced a profit share close to 1/3. This raises a number of questions, not least the value of 1/3 for the profit share and its role in macroeconomic fundamentals. To explain these facts, an endogenous growth model is developed. This growth and distribution model reconciles the great ideas of Kaldor (economic growth as a chain reaction), of Keynes (effective demand and marginal efficiency of capital) and of Ricardo (importance of the wage-profit distribution) in an economy facing creative destruction. A production function is obtained, depending mainly on the growth of employment, the rate of net investment and the profit share in income. In theory, we show the existence of incentives: an incentive for job creation when the profit share is less than 1/3 and another incentive for job destruction in the opposite case. Thus, increasing the profit share can boost the employment growth rate until it reaches the value of 1/3; otherwise lowers the employment growth rate. Three key findings can be drawn from these considerations. The first reveals that the best GDP and productivity growth rates are obtained with a profit share of less than 1/3. The second is that maximum job growth is associated with a 1/3 profit share, given the existence of incentives to create more jobs when the profit share is less than 1/3 or to destroy more jobs otherwise. The third is the decline in performance (GDP growth rate and productivity growth rate) when the profit share increases. In conclusion, increasing the profit share in income weakens GDP growth or productivity growth as a long-term trend, contrary to the trickle-down hypothesis. The employment growth rate is maximum for a profit share in income of 1/3. All these lessons suggest macroeconomic policies considering the profit share in income.

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