

## ***PROFIT - AS AN INDICATOR OF EFFICIENCY IN PERFECT COMPETITION***

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### **Abstract**

*The article is devoted to demonstrating the role of profit in economic processes from the point of view of various theories that have taken place in the history of economic doctrines. Special attention is paid to the role of the profit indicator in measuring economic efficiency in the context of the theory of general equilibrium. And also the conclusion is formulated that it is impossible to identify the state of equilibrium with the economic optimum.*

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Profit is an influential economic phenomenon, both in state life and in the life of every economic entity. Profit as an economic category has always been the subject of discussion, comprehension, interpretation and scientific analysis from a variety of points of view (in particular, social, economic, financial, legal, etc.). Scientists who have devoted their scientific potential specifically to scientific thinking about profit have accumulated many hypotheses, concepts, statements, judgments about profit, which led to the formation of scientific doctrines called the “profit theory” [2].

The conceptual hypothesis<sup>1</sup> about profit as an indicator of economic efficiency receives theoretical development in the system of general equilibrium theory. Let us recall that in the context of globalization, the definitions of both economic efficiency and profit have developed. General equilibrium theorists refuse to study the dynamic factors of growth of social wealth and focus their analysis on formulating the conditions for the optimal distribution of resources between consumers. At the same time, the development of the theory of profit brings many economists close to formulating the thesis of zero profitability. Already “Walras' law” postulates equality between the value of a product and the costs of its production; the concept of zero profitability receives a mathematical description in the theory of the firm [5].

The perfect competition assumed by the equilibrium model is driven by the profit incentive, and profit maximization [1] both by the entire system and by individual firms maximizes the total economic effect. However, profit began to act as a general form of income on capital, and as functional income in general. It is considered as the difference between gross income and the sum of income for all factors of production; it is this difference that is reduced to zero in a state of equilibrium.

<sup>1</sup> A hypothetical version of an economic organization, extremely far from reality - this is the model of competitive equilibrium.

The role of profit as an indicator of efficiency in the classical model of perfect free competition is significantly limited by two circumstances: the distinction between market and natural prices and emphasizing the dynamic aspects of the growth of a good. The general equilibrium model does not have these restrictions. Fluctuations in market prices, and with them the rate of profit, here coincide with fluctuations in the economic efficiency of business entities, since the latter is understood as an approach to an equilibrium state. Within the framework of general equilibrium, the dynamics of economic efficiency and profitability are not studied. Because the economic system reaches a state of equilibrium as a result of the action of the competition mechanism, subject to the following conditions: a) competition is perfect; b) consumers maximize the utility they receive, and producers maximize profits. The general equilibrium model formulates conditions not only for production efficiency, but also for meeting the needs of exchange participants. Because every competitive equilibrium is a Pareto optimum [3], and vice versa.

The indicated generality and logical harmony of the competitive equilibrium model are explained, firstly, by its attractiveness; secondly, the optimizing possibilities of profit as an economic category; thirdly, they give rise to the idea of adequacy or coincidence of the concepts of economic efficiency and profitability indicator. The substantiation of the thesis about profit as a criterion of efficiency is the proof of the agreement of the maximum profit with the state of competitive equilibrium. But does the latter generate actual market conditions for economic optimality? Such a question certainly requires its own formulation.

Despite the complexity of the task of formulating the concept of market economic optimality, it is apparently possible to name some obvious requirements for it. It should include: firstly, the optimum in the sphere of production - the best use of production resources; secondly, the optimal distribution of produced goods and, thirdly, the optimal functioning of the economic system in dynamics - the stability of economic growth. Competitive equilibrium does not satisfy any of these requirements.

The very concept of economic optimum claims to formulate the conditions for the maximum possible level of satisfaction of the needs of society - it acts as a criterion for the effectiveness of the economic system. But does the state of equilibrium, understood in the sense of the equilibrium of market demand and supply, on the one hand, and the technically most efficient methods of production, on the other, truly ensure the maximum level of satisfaction of the needs of society?

No, it doesn't. Firstly, with this formulation of the problem, dynamic factors for increasing economic well-being are excluded from consideration: the general equilibrium model postulates the conditions for the optimal allocation of limited resources in a given period of time. It does not address the crucial problem of accumulation, and from this point of view it represents a step backward compared to the classical model of a market economy. But, if the problem of the relationship between consumption and accumulation is not solved, then the optimal conditions formulated in the static equilibrium model are not sufficient, and there is no reason to believe that they really express the maximum satisfaction of the needs of society.

The theory of general equilibrium does not at all address the question of the stability of this equilibrium within the framework of the problem of the business cycle. But, if such dynamic factors of economic growth as, for example, an increase in the volume of resources, are excluded from consideration on the basis that they relate to the technical segment of the enterprise's activities, then there is no point in talking about cyclical fluctuations. In full accordance with the theory of the cycle, the development of market relations aimed at making a profit can lead the economy not to a state of stable equilibrium, but to negative fluctuations. Such a judgment undermines the concept of optimum and equilibrium theory, and with it the thesis about the possibilities of optimizing profitability.

Secondly, perfect competition eliminates deviations from equilibrium prices. "Here the equilibrium price would not be the result of supply and demand; it would accompany the market in order to achieve

immediate stability. But facts remain facts; movements towards equilibrium and fluctuations around equilibrium reveal themselves in actual prices, which cannot be subject to revision, but, on the contrary, are final” [4]. As a result, the sales volume will exceed the volume corresponding to the equilibrium state, and the average price will exceed the theoretical price, and the latter, in a perfect market, has always been imperfect - moreover, precisely because of the prevailing desire of producers for maximum profit [1]. And this thought does not actually lead to a state of balance. It will be possible to discover permanent relationships in it.

Thirdly, the equilibrium theory was able to formulate evidence for the existence of an equilibrium state, but it does not contain evidence that such a state is achievable under competitive conditions. There is no reason to assert that the economic system, even if all the prerequisites assumed by the equilibrium model are present, will automatically arrive at the equilibrium point, and will not fluctuate endlessly around it. The external impulse that will direct the system to a state of equilibrium must be indicated. This is not even contained in equilibrium theory. Moreover, the assumption about the stabilizing task of speculative activity in a competitive market is not justified; on the contrary, there are sufficient grounds to consider it as a factor that increases fluctuations in market prices. Since price fluctuations cause their actual average level to increase above the level of the theoretical equilibrium price.

Fourthly, which seems especially important to us, the scientific value of the general equilibrium model is significantly reduced due to the fact that it formulates conditions only regarding economic equilibrium - for a given distribution of property and income. The latter is introduced into the model as a factor, and therefore the concept of economic optimum becomes even more conditional in it. Equilibrium under an appropriate price system that determines a particular distribution of income between participants in market exchange means the maximum possible total utility. Although the latter requires equality not of substitution rates, but of absolute marginal utilities for all participants in the exchange. Such equality is possible under the condition of equality of income and the absence of individual preferences. Such a premise makes it possible to formulate the conditions for an economic optimum, but at a high cost - due to the impoverishment of the very concept of optimum. As a result, it turns out to be only a “production” optimum, which does not take into account the possibility of increasing the efficiency of the economic system through the redistribution of income between various participants. In other words, there is no provision for a distribution system that is most favorable from the point of view of increasing the efficiency of production itself. Accordingly, the optimizing segments of the profit indicator are also limited.

Fifthly, the limitations of the equilibrium theory are that it operates only on a given list of economic goods and does not take into account the existing efficiency of the economic system based on the introduction of new types of goods and services into circulation. This limits the role of the profit indicator in reflecting the economic efficiency of production, since the influence on this indicator of new production, which definitely affects the overall level of efficiency of the economic system, is not considered.

All this once again proves the absence in the model under consideration of a number of elements, without which the description of the economic processes under study is incomplete. Therefore, conclusions based on this model cannot be shared without significant reservations. Taking into account these reservations, the competitive equilibrium model can claim to formulate the conditions of only a partial optimum - a certain static state of the economy in which an effective inter-sectoral distribution of limited resources is achieved. It would be wrong to completely deny the possibilities of economic analysis opened up by the general equilibrium model, but one cannot identify the state of equilibrium with the economic optimum. In addition, this model is not identifiable, and it is generally accepted that it is unsuitable for describing a real economy. After all, its main premise is about perfect competition. Its unrealistic nature lies in ignoring the existence of factors that limit the operation of the mechanism of free competition, but also in the absolute mobility of production factors it assumes and

comprehensive information from participants in market exchange regarding economic conditions - in the present and future. Therefore, the need for extreme caution when assessing the conclusions of the general equilibrium theory, including the role of the profit indicator in measuring economic efficiency, is obvious.

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