

**SUBSTANTIATING PRICES BASED ON ECONOMIC PRINCIPLES UNDER THE CURRENT COMPETITIVE CONDITIONS**

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***Abstract***

*It is a legitimate and objective necessity of human progress, in general, that based on labor productivity growth, that lower production costs (per product unit), to proceed to the formation (determination) of lower product prices, with a positive effect on sales volumes.*

***Keywords:*** *labor productivity, product value, product price, practical work, abstract work, indices of economic activities.*

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A fundamental problem of Economics that many researchers were and still are concerned about, is the question of the relationship “productivity - value - price”, the connection and objective interdependence between labor productivity, the value and the price of the manufactured product within the general economic exchange mechanism. This relationship, pertaining to the process of forming the value of goods, is reflected in the end in the level and evolution of prices, ensuring their substantiation based on economic principles.

An important requirement of competitive economy is that the goods are bought and sold at their value, determined by the objective action of demand and supply.

Therefore, the effort to obtain a product changes with labor productivity. Of course, the higher labor productivity is, the lower the amount of work spent to obtain a product is. In the reverse situation, in certain cases

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where labor productivity is reduced, the workload for that unit of product will increase. Therefore, without neglecting the objectivity of supply and demand of a product on the market, the formation of the price size is directly proportional to the amount of working time spent and inversely proportional to labor productivity. Thus labor productivity growth can be considered as an inexorable law of human progress, and the prices and amount of use per product unit, should necessarily have a relatively downward trend.

Economic history has shown us that there were phenomena when there were significant increases in prices, worldwide, while the labor productivity increased (see period between 1980 and 1990). Faced with an exceptional situation, some economists are wondering directly or indirectly, whether the thesis on price size decrease with the increase in labor productivity is still valid.

Labor productivity growth, in general, contributes to human progress and economic entities are determined to switch to reducing production costs (per product unit) and to the formation of lower prices, with a positive impact on their turnover.

The validity of the thesis, in such situations, according to which with the increase in labor productivity there is a decrease in value and prices, is being questioned. We are tempted to believe that there is a total contradiction between the theoretical thesis on the decrease of value, as a result of labor productivity increase and based on the a reduction in prices level, on the one hand and the above reality presented, on the other hand. Such problems do not have a scientific, real substantiation, but rather a lack of analysis of the influence factors that lead to such assessments.

As an objective necessity of human progress, the legitimacy according to which labor productivity growth in industrial activity reduces production costs (per product unit), requires, in its turn, a reduction in the prices of products or service charges. As a requirement of the law of value, the above relation arises from the regularities of economic development.

The necessity of imposing the force of law in real activities of the productivity - value - price relationship cannot be questioned, regardless of the nature and complexity of the conditions in place. Therefore, the respective relationship expresses the fundamental relationships in the restructuring of manufacturing processes, in improving product quality and reducing production costs, in the redistribution of powers and optimizing material and information flows.

For the correct expression of the role of the productivity - value - price relationship, we must first very well define **value**, the value of product use. In the current globalized competitive market, there is a variety of definitions of value, but we select the one given by Jean Michel – president of AFAV (Association Française pour Analyse de la Valeur – The French Association for Value Analysis): “Value is the ensemble of the multiple benefits brought to and ranked (according to a system of values or preferences) by an “actor” or group of “actors” in a decision-making situation, under a specific context, for a unit of effort (cost, time) invested in a project (product, action) comparable with data from other projects”<sup>1</sup>. To create value and optimize value it is necessary to differentiate the benefits per unit of investment or effort. In this context, **value** represents the analysis performed on the product, given the expectations and motivations of the user, which is expressed by a size that grows or remains at least equal when product costs decrease and user needs increase.

Value as a result of the relationship between meeting the needs of the user and product costs is, on the one hand, an objective resultant given to the product through its *value of use* and, on the other hand, a subjective one, attributed to the product, through its *estimation value*, as a result of the anticipated evolution of the product. In this context, it is recommended that between the two components of value there permanently be a balance. In order to clarify the issues under analysis we consider it necessary to pay *increased attention* to the *productivity - value - price relationship at the level of a product or a service*. As is well known, labor productivity is related to practical work, not to abstract work and shows how many products are effectively manufactured in a unit of time or how long it takes to obtain a particular product. As a result of technical progress and application of advanced technologies, more products are manufactured in a company in the same unit of time, which means that labor productivity has increased, and each product should require a smaller amount of work, thus a lower absolute value in the formation of the product price. In this case the price obtained and subject to negotiation should be lower. It is possible that the product price does not decrease, meaning that the expression of value is separated from its objective, namely from the consumption of work necessary to obtain it.

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<sup>1</sup> Florin Chichernea – “ Value Management ”, AGIR Bulletin no.1/2010, pg. 11.

There are times when the amount of labor per product unit, even in the conditions of technical progress and labor productivity growth, does not decrease, but be maintained or even increase, but the manufactured product be of higher quality, have a higher use value. In this case, the actual price should be a result of the intersection of supply and demand, so to remain at the same level or to be increased. If this is the case we cannot discuss about an increase in price since the product is of superior quality, a higher use value rate on product unit in terms of determining a lower price. Or this is the very *essence of judiciously forming and correlating prices based on economic principles*. This applies only to new products.

A complete analysis of the evolution of prices of certain products should include an analysis of the changes in and the complexity of use values, of the technical - economic and functional parameters of the products concerned. In order to meet the needs for production and consumption, besides the price analysis and the economic analysis in general, the complexity of all values (use and estimation) should be taken into account. In this context some concrete issues must be presented, but for product safety reasons, the examples will not be nominated, but some arbitrary ones. The (negotiation) production, delivery price of product "A" is 30 % higher than that of product "A.1", but on technical parameter unit it is 10 % lower. Moreover, the price of a "B" is 3 times higher than the price of the "B.1" engine, but on technical parameter unit (horsepower), the price is 20 % lower. Examples may continue.

### **Conclusions:**

Following the development and modernization of production processes and manufacturing technologies in companies, the labor productivity growth and the reduction of work and material consumption as well as wages, it is possible to relatively decrease, namely on value unit of value use and the price for which the product is sold, respecting, in the end, the principle of the relationship under discussion. We believe that this is how the relationship between productivity - value - price concretely manifests itself. The condition to observe the correlation analyzed is strongly hit by the principle of competitive economy, of supply and demand of products in the market economy.

It should be emphasized that the practice has shown that there are cases in which the said relationship is not observed. The existence of such cases, under the influence of various factors (whether internal or external)

does not lead us to abandon the principle, on the contrary, as is known, the exception proves the rule. Under these conditions, it is recommended that the requirement for the productivity – value - price relationship be achieved not only on the ensemble of production and as a trend, but for each product and service executed, with the regularity required.

In an economy, the total amount or the value on a branch, the general price level (amount thereof), are matters that are to be addressed on a different level of analysis. Consequently, the total value is given by the volume and complexity of the work done in the respective period of time. If we assume that in a period of time of three years, 900 million work-hours (simple labor) shall be carried out, then the total value remains unchanged, and so does the sum of the prices which must correspond to the sum of the values. At the same time the mass of material goods and services may increase, increasing truly along with labor productivity. It should be noted that by increasing labor productivity, the price of each product or rather, per unit of use value is lower, obtaining, however, more products, there is an overall price amount equal to or greater. Hence the idea that, with the increase in productivity and reduction of production costs in an economy, the value of the total social product is not reduced and neither is the total amount of prices. In reality, if the amount of work increases, logically, the value and the total amount of prices increases as well.

Increase in the value and in the total amount of prices does not mean higher prices per product or per unit of use value. The price decrease (per products or per unit of use value) does not mean the decrease of value created in the economy, namely the sum of values and prices, but increasing at a higher rate the volume and quality of the products and services provided, labor productivity resulting in natural, physical, real expression.

In carrying out the productivity - value - price relationship, a highly complex one, there is no contradiction of meaning, on the contrary, through the contradictory process that takes place, like any process, the dialectical unity between the interdependent relationship factors referred to is determined. And therefore, in the law-like process of forming value and prices there is no objective inconsistency between the sum of the values and the amount of the prices. Moreover, this process joins them and permanently overlaps them, according to the regularities and relationships between the essential sides and the phenomenalist sides of economic processes, according to the law of unity between the essence and the phenomenon. Thus the

processes and regularities of value and prices formation are real and take place in an indestructible unity.

In the specialized literature we find authors who tend to complicate matters too much in what concerns prices formation and their relationship with value and labor productivity in the competitive global economy conditions. Thus, this complication results into a break of prices from their essence, measuring and expressing value, determined by the actual production costs (competitive) and ensuring a normal profit. The essence in pricing consists of the reflection of its real production costs and providing the producer with a normal income. Thus, prices should be formed as close to competitive prices, objectively expressed depending on supply and demand. Therefore competitive prices must be as close to the manufacturer, to the actual conditions of production, in order to stimulate the production of goods and reduce corresponding costs. It is recommended, in this regard, that the prices charged (delivery) fully reflect the actual production costs for the production of the goods, the quantity and quality of the use values units derived.

The price expresses, must express, the unbreakable unity between the value side and the material side of the product. The reflection in prices of objective requirements arises from the productivity - value - price relationship, ensuring their substantiation on real economic principles and their sustainability and stability contribute to the development of a lasting, real economy as a whole.

For example, at a general level, we will stop at major *indices* covering developments in industrial activity in Romania in the year 2014 and that are connected to the productivity - value - price relationship.

Thus, in the year 2014 compared to the year 2013, *the gross industrial production* increased by 6.1 %, due to the manufacturing industry (+7.5 %) and the mining and quarrying industry (+1.0 %). In the sector of production and supply of electricity, gas, steam and air conditioning production decreased by 4.7 %<sup>1</sup>.

In the year 2014 compared to the year 2013, *labor productivity in industry* increased by 4.7 %, due to the manufacturing industry (+5.4 %), the mining and quarrying industry (+2.1 %) and the sector of production and supply of electricity, gas, steam and air conditioning (+1,1 %).

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<sup>1</sup> [www.inse.ro](http://www.inse.ro), Industry Statistical Bulletin no. 12/2014, pg. 6.

*The value index of turnover in industry*, in the year 2014 compared to the year 2013, increased by 7.8 %, due to the manufacturing industry (+7.8 %) and the mining and quarrying industry (+7.5 %).

As far as the industrial production price indices are concerned, in the month of December 2014 versus November 2014, industrial producer prices fell by 1.1 %. In December 2014 versus December 2013, price increases were registered for water supply, sewerage, waste management and remediation activities (+3.5 %).

In connection with the *labor market* it should be emphasized that the number of employees in industry (in the units with 4 employees and over) was in the month of December 2014 of 1294.5 thousand people, 7.0 thousand people lower than in November 2014.

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