

with respect to the nature of profits as a cost. It is, nevertheless, a useful reminder that, in the long run, "normal" profits are a cost of production. Consistent with this treatment of profits, total cost will therefore equal the sum of the returns to factors of production, including capital consumption, plus taxes. Since the returns to the factors of production, including capital consumption allowances, are actually gross incomes, total cost will be equal to the sum of these gross incomes plus taxes. Thus total cost may be measured by summing gross incomes and taxes as well as by valuing output at market prices.

Within a given industry relations similar to those outlined above will hold. The gross product originating in the industry equals the value added in the industry and the value added is equal to the total costs originating in the industry.⁴ The total costs originating in the industry are in turn the sum of the gross incomes to factors of production used in the industry, including capital consumption allowances, and taxes. Thus total costs originating within an industry may be measured by the sum of gross incomes and taxes originating there.

The relationships described will hold generally. However, in order to be consistent with the Department of Commerce national income accounts, gross income and taxes must be defined as they are by Commerce. Therefore in this study the gross income of any factor will equal its income including direct taxes on that income. The remaining taxes which must then be added to the gross incomes to obtain total cost originating in an industry will be the indirect business taxes levied on the industry.

In accordance with the treatment described in the previous paragraph, the measure of total cost originating in an industry is the sum of gross returns to factors of production utilized in the industry, including the taxes thereon, plus indirect business taxes. The classification of factors of production may be as fine as the available data will permit. For this study only the two very broadly defined factors, labor and property, were used. A finer breakdown is technically possible, but the available data do not warrant a finer classification. The returns to these factors are shown as three separate items: compensation of employees, capital consumption allowances, and net business income. Thus the total cost originating in an industry would be the sum of these three items plus indirect business taxes. For certain purposes the sum of capital consumption allowances and net business income is a useful figure. This sum we have labeled gross business income.

An explanation of the calculation of the four cost items is given in appendix A. It should be noted, however, that net business income has been calculated by subtracting compensation from net income originating in each industry. It therefore is the net income to all factors except labor, and includes such diverse elements as corporate profits, interest, and income of unincorporated business.

The sum of the four items which equal total cost is also equal to gross product measured by value added. This sum will therefore be referred to as gross product originating or GPO in any given industry.

The estimation of GPO for an industry is only the first step in determining the behavior of unit costs in the industry. Without relating

⁴ While there are certain technical statistical differences between "value added," as employed in census data, and "gross product originating," conceptually the two terms may be treated as identical.