

## BOOK REVIEWS

**Kornai, János**

***Gondolatok a kapitalizmusról (Négy tanulmány)***

*(Reflections on Capitalism (Four Essays))*

*Budapest: Akadémiai Kiadó, 2011, 248 pp.*

### I.

The recently published essays<sup>1</sup> of Professor János Kornai are easy to read and comprehend: the clear and well-structured prose is complemented by the author's ambition to reach beyond the circle of fellow professionals in the science of macroeconomics. In the introduction to the essays, the author makes it very clear that his target audience is broader than usual, and that he hopes to address sociologists, political scientists, historians and even the average, general-interest reader. The easy-to-understand language, the strictly logical and transparent structure of the writings serve the author's purposes well.

Likewise, it is easy to accept the author's views emerging from the thorough discussion of the issues under consideration: the powerful reasoning, the vast array of facts marshalled to support a specific point of view, the multitude of notes and references taken from the literature of macroeconomics and beyond are very convincing indeed. In particular, I was and continue to be impressed by the very clear line drawn by the author between what he calls the *positive* and *normative* method of investigation, maintaining at the same time that both are needed for the

<sup>1</sup> Three of the four essays are already available in English (see notes 5–7). They are all directly downloadable from Kornai's own website: <http://www.kornai-janos.hu/online%20pub%20English.html>

course of the cognitive process to be complete. By the first, he means the neutral, “purely scientific” approach entailing an accurate description of the phenomenon and the full understanding of the causal relationship between its various components. In the course of the second, the given phenomenon is further investigated from the perspective of higher, e.g. moral values, meaning an examination of whether the phenomenon thus uncovered is to be considered good or bad from the point of view of moral justice. In order to achieve this, Kornai notes that it is equally important “to lay down *the set of values* by which the good can be discerned from the bad” (p. 17). The sequence of the two should not be reversed: first, we have to familiarize ourselves with the facts, uncover the essential relations between them, while the judgemental phase can follow only once the first phase has been completed.

This, incidentally, also explains why it is difficult to disagree with Professor Kornai or to challenge one or the other of his statements.

When reading the essays, I harboured all three of these sentiments: first of all the joy, an almost aesthetic pleasure, to be able to comprehend some of the most difficult issues of macroeconomics under the guidance offered by the author.

Secondly, and most importantly, the essential agreement with Kornai’s fundamental point, which he sums up as follows: “A case for capitalism – with critical eyes”. With due respect, though, I would slightly alter this to better describe my own position, which could be summed up as “A case for capitalism – without illusions”. The difference between the two is hardly huge, perhaps no more than a matter of imprecise perception. What I mean to say is that following Kornai’s line of reasoning, especially in the essay dealing with innovation and dynamism in capitalist society, in addition to or perhaps even beyond the rational train of thought presented there, one cannot help detecting something of an emotional nature. Were the essay not a strictly scientific piece of writing, I would even go as far as calling it a hymn to capitalism. For my part, I feel less enthusiastic and more inclined to simply accept the realities: the complexity of human nature, the overall performance of capitalism as a social formation, including its apparent ability for rejuvenation and self-correction, the failure of the only competing and tested alternative – socialism – make me believe that in the foreseeable future, capitalism will remain the only viable alternative for mankind, or at least for Western civilization to organize human society and its economy.

Kornai’s point is quite concise: “Make no mistake about it, while I am for capitalism ... I am not a bigot ... I do not think it is a ‘great society’, on the contrary, for more than one reason, I believe it is a ‘bad one’, but ... I think it is the least bad of all the options which are readily available”. Likewise, the following is important: “I am convinced that capitalism too has incurable vices ... which, although they can be allayed by means of appropriate policy measures, cannot be totally

remedied” (p. 22). Kornai makes another important statement here, pointing out that political democracy presupposes the existence of a market economy – i.e. capitalism. He is certainly right, even though unfortunately the opposite of this statement does not hold; the existence of capitalism or a market economy is no guarantee for the proper functioning of democracy; as a matter of fact, capitalism is capable of producing quite extreme, occasionally even terrible things, depending on a given country’s political, cultural, and other conditions.

Regardless of the above, the reconfirmation of the validity of Kornai’s point is more topical than ever; during times of social distress – wars, economic crises, social transitions – one hears a lot of lamentations proclaiming the end of the world: the public is worried about social vices, wants to see the perpetrators punished, and awaits new prophets. The present global crisis is no exception in this respect. Some people cherish hopes that the virtues of capitalism can be preserved while at the same time weeding out its vices. Let’s correct the mistakes, they say, by increasing state intervention, regulation and centralization. Others do not want to correct capitalism, but instead propose some vaguely defined “third road”, which would be an amalgam of the advantages of both socialism and capitalism without their ugly features. This line of thought is patently present in today’s Hungary. The shock of the social transition, the controversial features of the process as a result of which the capitalist market economy has been rolled out – including privatization, corruption, the extreme (actual or perceived) income differences among various segments of the population, the anomalous functioning of many social institutions – have led to the emergence of something which might perhaps be called “naive anti-capitalism” in the society, including its upper strata. The global crisis starting in 2008, whose end is nowhere to be seen yet, and whose potential impact on the world as a whole, and on vulnerable countries such as Hungary in particular, is likewise unclear, has given a boost to these feelings. At this point, it is appropriate to refer to the celebrated book *Animal Spirits* by Nobel Prize winner Akerlof and his equally illustrious co-author Shiller.<sup>2</sup> (Kornai also cites them more than once.) According to the American authors, the fluctuations of the economy cannot be properly understood without taking into account the changes in emotional factors, such as confidence, fairness, corruption and bad faith. One may say that broken confidence and the hurt feelings of unfair treatment, as well as indignation over cases of corruption and bad faith are all present in contemporary Hungary and the Hungarian economy. Recognizing this could help to understand the reasons for the not insignificant underperformance of Hungary relative to its potential, as well as to the performance of most of its neighbours.

<sup>2</sup> G. A. Akerlof – R. J. Schiller (2009): *Animal Spirits: How Human Psychology Drives the Economy, and Why it Matters for Global Capitalism*. Princeton University Press.

And the third factor: while reading the essays, I occasionally felt the urge to argue, to challenge one or another point made by Kornai. Sometimes I simply felt that some aspect – important to me – is not mentioned or developed properly. As pointed out earlier, I find myself in a delicate situation: it is not easy even for a peer to contradict Kornai, a scientist with a huge knowledge and experience. I am not an economist, let alone a scientist to enter such a dispute light-heartedly. I will therefore make my objections, as they say, with due respect and reserving the right to be mistaken and stand corrected.

## II.

The four essays differ quite substantially in terms of the issues they address, as well as the depth of elaboration. It seems to me that from a scientific point of view, the second essay (*Shortage Economics, Surplus Economics – on the Theory of Markets*) can be regarded as the most ambitious. It is also the longest.<sup>3</sup> Here, the author addresses the concept of “surplus”, proposing that it is an immanent feature of capitalist economy.

Kornai’s insight about shortage, as an immanent feature of socialist economy, has by now become an integral part of modern macroeconomic theory.<sup>4</sup> The author now sets himself the goal to attempt the same in respect of surplus being an integral part of the capitalist economy.

Needless to say, Kornai is perfectly aware of the fact that at every moment and stage there is surplus of every component (capacity, stocks, labour force) of economic activity. This, however, is deemed more or less technical by the mainstream macroeconomic theory. There is, as the author explains, “fluctuation around equilibrium, but none the less, the long term trend is called equilibrium” (p. 75). Kornai, however, posits that the difference is not simply one of terminology, e.g. the phenomenon in question is considered as equilibrium by some, while others might call it surplus economics. Kornai argues that surplus is an integral part of capitalist economy and if this is the case, “new light is thrown on many features of capitalism”, enabling a better understanding of the nature of this social formation.

To support his point, the author builds up his case meticulously, setting out first the definitions he will operate with, followed by the structure of reasoning and the practical examples (the US telephone and passenger car industries) which support his case. He deals with the concept of surplus separately in respect of the perhaps most important economic resource – the labour force. He introduces the reader to

<sup>3</sup> This essay has not been published yet in English.

<sup>4</sup> J. Kornai (1980): *Economics of Shortage*. Amsterdam: North Holland.

the most important “mainstream” theories in this context; the theory of the natural rate of unemployment and efficiency wages.

It is revealing about Kornai’s way of thinking as he compares the “equilibrium” oriented thinking of mainstream economists who might take inspiration from Newtonian physics with others who apparently find better analogies in Charles Darwin’s evolutionary theories. In the case of the latter, mere chance plays a more substantial role; things “work out well most of the time, but not always: sometimes good things get wiped out, although they sometimes survive, even though there may already exist better alternatives to take their place” (p. 131).

Kornai is fully aware that his concept and the reasoning shown in the essay lacks the full explanatory power and is not complete. No statistical observations are available to accurately discern the “normal” surplus capacities (needed in a microeconomic sense) across the economy. He is ready to admit that his line of reasoning is “verbal”, i.e. neither supported, nor proven by mathematical models. Nonetheless, he is convinced that these constraints should not stop him from raising questions when “the author, in his attempt to find answers to his questions, uses only verbal means ... being perfectly aware that the answer is temporary, incomplete and inexact, but it takes us closer to understanding the phenomenon under discussion” (p. 162).

Kornai is certainly not alone with his dilemma. Another great economist, the Nobel prize winner American Paul Samuelson, is said to have fumbled in connection with a scientific point he had raised, saying that he was unable to make up his mind whether it was a stroke of genius or a simple commonplace. Only time can tell, he said, which is probably true for Kornai’s insight as well.

The title of the first essay, “*Innovation and Dynamism: Interaction between Systems and Technical Progress*”<sup>5</sup> more or less fully explains its contents; it compares the socialist and capitalist economies in respect of these two aspects.

Kornai’s “hero” is Joseph Schumpeter, the Austrian-American economist. Kornai uses this latter’s definition to describe the entrepreneur who plays a crucial role in the process of innovation pointing out that “in addition to borrowing his definition, my views are thoroughly influenced by Schumpeter’s theories on development and the nature of capitalism” (p. 38).

Citing a multitude of examples, Kornai sets out to convince his reader that it is the process of innovation which energizes economic activity by boosting competition. Competition has a beneficial influence on the process of innovation which as a result becomes – using the author’s expression – a system-specific feature of

<sup>5</sup> Paper presented at the UNU-Wider Conference, “Reflections on Transition: Twenty Years after the Fall of the Berlin Wall”, held on 18–19 September, 2009 in Helsinki. For the published version, see *Economics of Transition*, 2010, 18(4): 629–670.

capitalism itself. The variety of examples helps us to understand that innovation is “the air capitalism breathes”. There are fewer, but more saddening examples from our proximity showing that almost everything which was system-specific in the socialist economy served to prevent or slow down the advancement of innovation.

Investigating the case of the post-communist countries, Hungary among them, Kornai has exciting things to say about the link between the political transition and the idea of “creative destruction”. He states that following the political changes, “it took several years to get over the worst phase of the destructive side of the Schumpeterian process” (p. 55). After enjoying no more than a few years of prosperity, these countries suffered a new shock, this time the effect of a global recession. According to Kornai – and I fully share his point here – at this stage it is too early to say whether the ongoing recession will have a cleansing effect in the Schumpeterian sense, in other words, “does the destruction clear the way for more construction” (p. 56).

Confronted with so much “confusion and suffering”, it is a bit surprising to learn about Kornai’s resentment, or, better said, his anger and frustration that “The large majority of citizens in the post-socialist region do not understand the basic causal relationship between capitalism and technological progress ... most people enjoy the advantages ... [but] they do not attribute this great change to capitalism. On the contrary. A large part of the population has moderate or even vehement anti-capitalist feelings” (p. 55).

In some other places, however, it is the author himself who states that as a reaction to the damaging consequences of such destruction it is quite understandable that nowadays the word “capitalism” does not resonate nicely in the ears of the citizens of post-socialist countries.

While this is perfectly correct, I would go even further: as human beings, we have a rather asymmetric attitude towards the things of life, in general. We quickly become accustomed to good things, taking them for granted, whereas the bad things are difficult to accept, and they continue to haunt us for a long time. Let me use an analogy from my past experience as a corporate executive to throw some light on my point: it is quite well known that salary increases and other benefits are – as HR consultants prefer to term them – of “hygienic nature”. This is supposed to mean that a disregard for adequately providing one’s staff with these benefits can have a very negative influence on the work morale, while these benefits in themselves are certainly not sufficient to secure sustainable motivation. For that, you need to have other means as well (independent work conditions, trust, praise, promotion opportunities, etc.).

As already noted, Kornai strongly agrees with Schumpeter’s emphasis on the benefits of innovation and creative destruction. The author naturally does not dispute, but rather underscores the fact that innovation and technical progress can be

abused (wars, terrorism, sexual crimes, drugs, etc.). In spite of this, he maintains – correctly in my opinion – that “the direction of technical changes should indeed be considered as progress because it brings about many more benefits than drawbacks or dangers” (p. 47). While I basically agree with this statement, following Kornai’s line of argumentation, I cannot help thinking that something is missing here. Innovation in Kornai’s discussion strikes me as an almost harmonious, benevolent process. Kornai seems to disregard the fact that not every technical change is useful for society, quite to the contrary. In the process of capitalist innovation, it is not altogether important that the output should serve some useful end. The primary purpose of innovation is to yield profit to its owner and the two ideally coincide, but sometimes, however, they do not – and I would not venture to make even an educated guess as to how often and to the proportion of the first to the second.

In their book referred to earlier, Akerlof and Shiller formulate this point in the following way: “The bounty of capitalism has at least one downside. It does not automatically produce what people really need; it produces what they think they need and are willing to pay for. If they are willing to pay for medicine, it will produce real medicine. But if they are also willing to pay for snake oil, it will produce snake oil” (p. 26). The current crisis, for instance, had its roots in financial innovations which are of rather questionable social usefulness. (Consider that those who concocted and sold innovative securities had difficulty fully understanding them, let alone those who bought them.)

In this sense, Kornai’s position endorsing the huge moral and financial benefits as rewards for innovation needs at least to be refined in my opinion.

Another concern is the relationship between technically useful innovations and the protection of environment. Let us take a very topical example: that is underwater oil production. There can be no doubt that the development and operation of floating oil rigs require extraordinary sophistication, technical know-how and development, in short, innovation, which of course yields substantial economic benefits to its sponsors. On the other hand, it is equally obvious that this engineering miracle causes – not potentially, but in actual reality – serious damage to the environment (a point in case is the accident involving the oil rig operated by BP in the Gulf of Mexico.)

The third essay,<sup>6</sup> “*Liberté, Égalité, Fraternité: Reflections on the Changes Following the Collapse of Communism*”, addresses the question of whether and to

<sup>6</sup> The essay is based on a presentation at the conference “*The Future of Social Changes. Visions and Perspectives after 20 Years of Transition*” held in Bucharest by the Erste Foundation and the Wiener Institute für Wirtschaftsvergleiche in June 2009. For the published version, see *European Review*, 2009, 18(3): 379–397.

what extent the grand ideas of the French Revolution have become a reality following the political changes in the region.

The picture is at best muted: we can be satisfied with the achievements in the field of freedom. In addition to political freedom, economic freedom – the right of free entrepreneurship, of free entry to the market and the security of private ownership – is more or less complete, too. It is with some sadness, though, that one has to note that a number of measures brought by the new Hungarian government which came to power in 2010 create uncertainties in this respect.

It is a cause for concern that the region's population, including the Hungarian people, does not fully understand, nor appreciate the importance of freedom as a higher value. Kornai cites statistics to demonstrate that most of the people in the region prefer order to freedom. To this I would add that other statistics imply that in contrast to Western countries, the people of the region and of Hungary prefer welfare to democracy (and freedom), too.

In respect of *Égalité*, Kornai draws our attention to the fact that on the average, Central European people give more support to an economic policy which aims at the reduction of inequalities than the world average. Kornai, however, again uses this opportunity to emphasize that inequality is a system-specific feature of capitalism. It is possible and sometimes necessary to reduce it, but to eliminate it or even attempt to do so is definitely counterproductive.

Speaking of *Fraternité*, the author substitutes this term with solidarity. Perhaps the most important insight in the essay is that "The policy concerning the Welfare State is in many respects inconsistent, because it seeks to satisfy two opposite, mutually exclusive, sets of values, and to please simultaneously two large constituencies having radically different preferences and disliking each other. ... policy-makers ... cannot evade the problem of consistency. If they try to do so, they have to pay a political price" (p. 204).

The performance of the Hungarian political elite in the past 20 years fully confirms the truth of the above conclusion.

The fourth and last essay, "*Marx – through the Eyes of an East European Intellectual*", was originally prepared as a keynote address for a conference in Japan.<sup>7</sup> The essay discusses the author's relation to Marx both on the personal-emotional level and on the academic level. Like so many other East European intellectuals, as a young man Kornai set out by enthusiastically joining the communist movement and after gradually losing his illusions, he ended up with completely breaking with communism or socialism, as it existed.

From the reader's point of view, it is much more intriguing how Kornai, the scientist sees his relation to Marx. What I particularly find exciting – and, at the

<sup>7</sup> The conference, which was entirely devoted to Marx, was held at Kaganawa University (Yokohama). For the published version, see *Social Research*, Fall 2009, 76(3): 965–986.

same time, most thought provoking – are Kornai's thoughts on the intellectual responsibility Marx bears for communism as it existed during the greater part of the 20<sup>th</sup> century. Kornai's position is very straightforward; Marx does bear such intellectual responsibility, the communist countries after all did implement his vision by attempting to eliminate private ownership and market coordination by substituting it with state ownership and bureaucratic state direction.

There is no doubt that Marx believed in a utopia, in a dream that the equality of mankind can be achieved. He was not alone; many visionaries before him – Jesus Christ, Sir Thomas More, the early French socialists – had the same dream. Regrettably, they had been wrong and so was Marx. Human nature is infinitely more complex for one value (equality) to be able to describe, to capture or to motivate it.

Proceeding in his line of thinking, Kornai holds Marx responsible in an intellectual sense for the dictatorship introduced in the communist countries and, indirectly therefore, for the horrible crimes committed during that period. At this point, it seems to me that Kornai's position may not be fully balanced or can be considered sort of a back projection.

What I have in mind is that Marx, the revolutionary, was confronted with the 19<sup>th</sup> century version of capitalism and “bourgeois” democracy, which as a matter of fact did not provide the overwhelming majority of the population with economic and other means necessary to lead a decent life. It did not guarantee basic human rights either. For instance, the institution of general voting rights did not exist for quite some time; there was racial and sexual discrimination, child labour, even slavery. Property rights were anything but balanced (for example, the English land enclosures in the 16<sup>th</sup>–18<sup>th</sup> centuries, the treatment of native Indians in America, the whole process of colonization). Summing up, one can rightly say that it protected a minority with property against a majority without it. Its attitude to human life was certainly different than today – it is sufficient to recall the carnages of the First World War. In the light of all these, one can have some understanding for Marx not appreciating the benefits of a bourgeois democracy and parliamentary system.

It is true, on the other hand, that Marx undoubtedly underestimated the ability of capitalism to develop and self-correct, as a result of which the capitalism of the 20<sup>th</sup> century luckily bears no resemblance to the one existing in the 19<sup>th</sup> century. This was, to no small extent, due of the activity of the Western organized workers' movements initiated and encouraged by Marx himself.

Perhaps, like so many geniuses before and after him, Marx can be faulted for a sort of intellectual arrogance, for falling in love with his brilliant brainchild and ignoring objections which can be rightfully brought up against it. The necessity of dictatorship directly and logically followed from the idea of revolution and expropriation. To serve him justice, what he had in mind was a temporary dictatorship

of the majority over the minority. Certainly, this is not what happened in the 20<sup>th</sup> century. Perhaps he considered this an acceptable price to help a beautiful dream come true. We have to blame him for this view, even allowing for the fact that peoples' attitude to violence and the value of human life in the 19<sup>th</sup> century was entirely different from what we have come to believe in today.

It is therefore with the above *caveat* that I come along with Kornai; it is true that those who know are undoubtedly responsible for what they commit to paper and the greater the impact of their writings, the greater their responsibility.

When discussing Marx's responsibility, however, the *hic et nunc* is of essence, because I believe that it is neither possible, nor appropriate to ignore the fact that in Eastern Europe and Hungary, especially after the political changes, it became a kind of axiom to equate communism and fascism.

However, I am not at all convinced that this equation is justified. Perhaps in the case of communism or socialism that existed throughout the 20<sup>th</sup> century, it is. One cannot, after all, forget the monstrosities committed predominantly in Stalin's Soviet Union. (Having admitted that I think that in a fair and impartial discussion, arguments could be brought up even against this statement). However, as far as communism as a utopia or dream is concerned, it is certainly not, and this is exactly in my opinion what the communism prophesied by Marx is all about.

### III.

In the *Introduction* to the essays, Kornai calls the book half finished, "a half finished statute carved from stone". During crisis time, the book offers no explanation for the reasons of the crisis, "the content has not been developed into a consistent structure" (p. 24).

This is certainly true. On the other hand, all four essays contain a wealth of information, a host of new insights, evaluation and judgement. Reading them is intellectually rewarding for a reader who is interested in economic as well as broad social issues.

It can only be hoped that the author will keep his promise and "try to add a few more chapters to what should become a major piece of macroeconomic thought" (p. 24).

*Péter Felcsuti*