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**THE ECONOMIC SYSTEM AS AN END OR AS A MEANS,
THE SOCIALIZATION OF CONSUMPTION,
AND THE ROLE OF THE THIRD SECTOR:
AND EVOLUTIONARY APPROACH**

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**The economic system as an end or as a means, the socialization of
consumption, and the role of the third sector: an evolutionary**

approach¹

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An economic system can be chosen instrumentally, as the best available for the pursuit of given ends, or its implementation can be seen as an end in itself, for eschatological or ethical reasons. After the demise of “real” socialism as a system founded on public ownership of the means of production, socialism can be salvaged as a social preference system oriented towards equality and social justice, to be implemented without systemic constraints in the organizational and institutional sense. However, even in case social preferences remain relatively egalitarian, the overall result can turn out to be more inegalitarian anyway, because of the different trade-offs that the refusal of the a priori socialist organizational constraint may entail. Notwithstanding the present eclipse of organizational socialism, capitalism in the future could gradually change towards a socialist system of organization, if non-capitalist productive forms were to reveal themselves capable to advantageously compete with capitalist enterprises. However, without a change in the social and economic context, in forms that may be only dimly foreseen, leading to such an outcome, a forced large scale substitution of non-capitalist production forms for capitalist enterprises could be hardly justified in view of past experience, and of the relevance that production, quality, technical progress and accumulation have for the growth of social welfare. But there is no need to prejudge the future. Instead, there is a case for creating an institutional framework allowing different forms of economic organization, capitalist and non-capitalist, to compete on equal footing, in an evolutionary perspective. Of particular relevance here is the role of the Third Sector. Independently of the predicament of socialism as a system based on a non-capitalist organization of production, another way for a spontaneous extension of the domain of socialism could derive from the socialization of consumption, if the consumption of public goods makes up a growing component of real consumption, as the trend seems

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to be at present. This trend, however, could bring about problems for incentives and the tax base.

The Economic System as an end or as a means.

A criterion for the choice between different (economic, political or social) systems may be based on the capability of a system to pursue the ends that correspond to one's interests and values (this means to one's system of preferences over alternative social states). The adoption of specific varieties of the institutions that make up a system can be calibrated to the pursuit of those aims, given the initial historical and institutional set-up.

In other terms, the system and the institutions that make it up and qualify its specific variety can be seen as a means, an empirically adaptable instrument rather than an end in itself. An alternative viewpoint attributes an intrinsic value to the choice of a system as such. This can be justified in some ways by the ultimate ends that the system is supposed to attain. The choice of the system becomes a choice of intrinsic, epochal or ethical, value, a choice of civilization, independently of the effective results that in the immediate or in the middle run such a choice brings about. This remark applies both to economic and political systems. For instance, the second viewpoint often applies to parliamentary democracy, seen as a value in itself rather than, à la Churchill, as the least obnoxious political system that has been invented up to now, which renders relatively more probable social states that are higher valued relatively to widely (albeit not unanimously) shared social values.

The fetishism of systems

The fetishism of socialism or capitalism thus leads to the persuasion that the choice of a system has an intrinsic salvific or thaumaturgic value, for two possible reasons. The first is the millenarian viewpoint, of the realization of the ultimate bliss in an indefinite future, which sometimes is perceived as imminent, the second is the ethical viewpoint. Historically the first viewpoint applied in particular to socialism. The millenarian force of "real" socialism lied in the official doctrine that the system was a transition towards a qualitatively superior stage, where the intrinsic imperfections of the intermediate state would have been overcome. This was supposed to apply in

particular to the limitation of resources in relation to needs, thus nullifying the relevance of the distributional issue. It is more difficult, even if not impossible, to attribute millenarian properties to an existing and well experienced system, whose characteristics are well known and there to be seen, that has already fulfilled its potentialities and manifested its intrinsic flaws and imperfections. In the case of transition economies the starting point is characterized by a much lower level of living standards than in the advanced market economies, and the attainment of the living standards of advanced democracies is seen as some kind of relative bliss, which is thought could be brought about simply by the institutional transformation towards a capitalist market economy. Thus, systemic transformation can become a pre-eminent objective to be pursued by all means as fast as possible, without adequately considering the specificities of the historical and institutional context and the transition costs, which in some ways are associated to its modalities. Or the relative well-being, achieved in the framework of the capitalist system, can be in some way be defended through an idealization of the latter, considered to be, à la Pangloss, the best of all possible systems, being the most natural one, not being artificially constructed, along a pre-determined model, like socialism. The latter is seen, unlike capitalism and market, as an unnatural constructivist deviation. At the same time the ideology may assume an ethical connotation and the market may be seen as intrinsically just, because through the market everybody gets according to his merits, etc. etc.

As far as socialism is concerned, the fetishism may be based, even independently of any millenarian view, on the moral foundation deriving from the belief in the ethical illegitimacy of profit. This view can be based on ad-hoc theories (such as the Marxian theory of labour value and exploitation), on simplistic viewpoints (such as the idea that the wealth of somebody must originate in the poverty of somebody else), and on erroneous perceptions of the functioning of the real world. Or, more simply, it can derive from the consideration that capital and entrepreneurial incomes can lead to wide income differentials that are ethically unjustified.

The intrinsic imperfection of economic systems and their comparison

The institutions of both “real” capitalism and socialism are largely imperfect, and are

characterized by an unavoidable set of shortcomings and inefficiencies, on which there is no need to dwell because they are well known. The actual contest between “real” capitalism and “real” socialism during last century has eventually seen the former to prevail. The experiment has been of enormous value in deepening our understanding of social facts and possibilities. The costs have been sustained on their very flesh by the countries of the former socialist bloc, the same that have later served as guinea pig for another original experiment, of lesser, but still great, social significance, that of the post-communist transition, aiming (according to Branko Horvat’s preferred terminology) to the restoration of capitalism, or, rather, to the construction of modern capitalist institutions.

Does all this mean that socialism is doomed not only for the present, but also for the indefinite future? Will it worthwhile to try again? In the name of what? Certainly it is not enough for justifying a new experiment of organizational socialism, however partial, the simple consideration that the capitalist system, in all its variations, leads to questionable results, both with respect to ethics as well as to efficiency, in comparison with some abstract benchmark. The view that the proved imperfection of a system is a sufficient reason for the establishment of a new, after the removal (be it forcible or peaceful) of the first, is a fallacy which has led to tragic consequences, but that continues to find new supporters (such as by late, apparently, the so-called no-globals, with respect to the regime of international economic relations).

Owing to the inevitable shortcomings of really existing systems, and the experience of last century, the only reasonable perspective consists in an instrumental and pragmatic approach towards systems and institutions, whereby the latter are not considered to have intrinsic value, and their merit lies exclusively in the societal objectives they allow to reach in a limited horizon, not in what they are alleged to bring about in an indefinite future. Moreover, one must be aware that the consequences of introducing new institutions depend on the specific historical circumstances, as is shown by the different impact of the introduction of analogous institutions in different countries. In particular, the introduction, or restoration, of market institutions has in general produced better results in the countries where a functioning market economy was present in a not too distant past.

Socialism of the means and socialism of the aims

In this perspective we can make a distinction between socialism of the means and socialism of the aims. The means consist, on the negative side, in the prohibition of private entrepreneurial activity, and of private ownership of productive assets. The positive part is the substitution of public, or “social”, ownership and entrepreneurship for private (“capitalist”) ownership and entrepreneurship. But socialism can also be seen as a set of aims, such as equality, or social security, the same that would be usually advocated for justifying the adoption of a variety of socialism of the means, apart from the Marxist justification of socialism as being a historically inevitable, much more productive, economic system. Theoretically speaking these aims translate in preferences over social states. More precisely, one may characterize as “socialist” a subset of the possible preference sets, the set of those preference sets that are relatively more informed by socialist aims. Thus, one may conceive a socialism of aims, independent in principle from the choice of a particular social system through which socialist aims can be pursued, independent in particular of the socialism of means. In this case the socialism of aims, not being constrained to a particular choice of means, acquires in theory a degree of freedom, and its pursuit should bring about outcomes superior (in the weak sense of not being inferior) to those that can be achieved through the constrained pursuit of socialism, given the (“socialist”) preference system. In this perspective what is left of socialism, possibly in a context where capitalist institutions prevail, because they are seen as more suitable to achieve preferred social outcomes on the basis of the given “socialist” preference system, is the specificity of the aims that are pursued, where socialist aims, such as equality or social security obviously cannot be exclusive, but must be traded off with alternative relevant ones, such as material affluence or span of choice. Summing up, in this perspective socialism is characterized by the nature or the weighting of the objectives, independently of the institutional means that are used for their pursuit.

Is there socialism in the future of capitalism?

The fact that in the past century the socialism of means (or organizational socialism)

has failed in the contest with capitalism does not mean that in a different set-up it could not reveal itself superior in the future. In a very long-run perspective the failing could turn out to be only temporary; in Schumpeter's words a simple "surface" in relation to "the tendency toward another civilization that slowly works deep down below".² Moreover some institutions that are usually considered as socialist could be usefully imported into capitalism (or rather, into the mixed economy), as has been the case in the past, such as with the social security systems. The opposite grafting could also be successful. One can refer for instance to the insertion of capitalist institutions into Soviet socialism during the NEP, or the transformation of the Chinese economy since 1978, which points to a gradual transformation into a capitalist mixed market economy, where the capitalist element could become dominant in the future. As far as the public³ ownership and management of economic activities goes, they

² "From the standpoint of immediate practice as well as for the purposes of short-run forecasting—and in these things, a century is a 'short run'—all this surface may be more important than the tendency toward another civilization that slowly works deep down below." (Joseph A. Schumpeter, *Capitalism, Socialism and Democracy*, London: George Allen & Unwin, 1976, p. 163).

³ Here and below by "public" ownership or entrepreneurship we broadly intend "non private".

have been shown in the past to be on the whole less efficient,⁴ but one cannot exclude that they may become relatively more efficient than private ownership and management in the future.

Public goods and the socialization of consumption

First of all the nature of goods and the nature of productive processes could change, leading to an increase in the relative importance of public goods, as a consequence of the changes in technology and tastes, thus increasing the scope for direct public provision. Among the possible characteristics of a socialist system there is the tendency towards socialization of consumption, this means the special merit attributed to public vs. private goods, which, insofar as the access to public goods is

⁴ In particular, in dynamic terms, as the generation and absorption of technical progress in production to consumer advantage goes, and, more in general, in terms of factor dynamic efficiency (growth in the value of production deriving from total factor growth) and also, more trivially, in terms of X-efficiency. At the same time, the relative organizational slack that in general characterizes public activities, which theoretically speaking could be not incompatible with Pareto-efficiency, may well be inefficient from the point of view of the principle of compensation, and thus from the Paretian viewpoint as well (in other terms the advantage for public employees could be less than its cost for taxpayers). For the comparative efficiency of real socialism and capitalism, see in particular Abram Bergson “Comparative Productivity: The USSR, Eastern Europe and the West”, *American Economic Review*, vol. 77, no. 3, (June 1987), pp. 342-357 and “Communist Economic Efficiency Revisited”, *American Economic Review*, Vol. 82 no. 2 (May 1992), pp. 27-31. For the issue of relative efficiency of public enterprises in mixed economies, see the many references to empirical analyses in William Megginson e Jeffrey Netter, “From State to Market: A Survey of Empirical Studies on Privatization”, *Journal of Economic Literature*, vol. XXXIX (June 2001), paragrafo 3, pp. 328–338.

not rationed through the market, could in principle have an egalitarian impact.⁵ The recent expansion of multimedia products that have some intrinsic characteristics of

⁵ This view finds a counterpart in Marx's *Critique of the Gotha Programme*: "the part of total product which is intended for the common satisfaction of needs ... from the outset grows considerably in comparison with present-day society and it grows in proportion as the new society develops". This statement was inspiring the 1961 Program of the Communist Party of the USSR, according to which "as the country advances towards communism, personal needs will be increasingly met by public consumption funds, whose rate of growth will exceed the rate of growth of payments for labour". See on this Alberto Chilosi, "Socialist and Communist Income Distribution in Marxian and Soviet Marxist Thought", *Il Politico*, 43 (1978), 4, pp. 698-710. The "public consumption funds" refer to consumption that is not rationed in principle through budget constraints and whose basic criterion of distribution is in principle "according to needs". There are three types of goods that may qualify in relation to this requirement: 1) collective goods that may be private, public or semi-public goods in an economic sense, but whose production and distribution is decided collectively through the political process (such as public provision of health, education, social services). 2) Pure public goods, because of their very nature, be they privately or publicly produced. In case of pure public goods, if they are produced at all, consumption is up to saturation. In order to be privately produced, they should be in principle financed through joint production of a public externality (be it a good, neutral or a bad for the recipients). This is typically advertising. But in case of advertising production of public goods is strictly derivative from the existence of a large market for private goods where the returns to advertising could be reaped. 3) Non-rival goods that can be practically excludable and for the consumption of which a royalty can be charged. There is a clear market failure here that may constitute a reason for public production. Moreover, if the barriers to entry are low (such as in the case of the setting up of Internet sites), or relatively low, and no condition of natural monopoly applies, as in the case of digital broadcasting, the access fees could tend to nought and not constitute an effective basis of allocation of the good according to budget constraints: namely the substantial nature of public goods, as far as non-rivalry is concerned, could still be dominant in the way their consumption is allocated.

public goods (radio and TV broadcasting, Internet) has been financed to a great extent, interestingly enough, through the simultaneous issuing of what we may call public externalities, namely externalities that have mainly the characteristics of a public good, as far as non-rivalry and non-excludability are concerned (even if non-excludability is jeopardized by remote control), but which the receiving party can variously consider either public goods or public bads, or indifferent, and that for producers are the principal source of revenues. This financing is however limited by the overall amount of advertising budgets that can be earmarked for this sort of advertising. There are some good theoretical reasons why these limits should be pushed forward through public financing or direct public production (in particular advertising-free production for the benefit of those, like the present author, for whom radio and TV advertising is definitely a public bad). A difficult problem arises, however, as to who has the right to determine its contents. A solution to it can be encryption and decoders, or access to Internet sites on subscription, or invoking the protection of the copyright law (in case of computer programmes). This type of solutions may imply high transaction costs and certainly leads to inefficiency because of limitation to access, if not justified by congestion. These inefficiencies could justify some kind of public provision. Moreover, the channels of delivery of those products (in particular cabling) can acquire the characteristic of natural monopolies, which in turn can justify a public provision or public supervision. The interesting experiment of infrastructural privatisation, which has been made in the UK with Railtrack, has clearly shown the limits of privatization. An important element for decrying the failure of the Railtrack experiment are safety considerations, which are specific to railways, but this points to the fact that in the area of basic infrastructures at least, public direct production may

present some comparative advantage.⁶

It is also true that on the one hand private provision of public goods may be simply financed by the state, and on the other that externalities can be, albeit imperfectly, internalized, through, in our case, Pigouvian subsidies. For instance, with respect to Internet one could conceive of a subsidy dependent on the number of accesses (even if an unbiased determination of the latter could be difficult). In the case of TV and radio broadcasting the subsidy could be related to the audience determined by some independent authority. In both cases there could be some contraindications, aside from the obvious one related to the cost of financing. In the first case one could turn out to financing porn sites. In the second case, garbage TV. In both cases the same result would be associated to financing through advertising. Here, indeed, enters the controversial issue of merit goods. An implicit subsidy to the enjoyment of Internet is anyway associated to the absence of taxation to Internet accesses and utilization (such as sending and receiving messages or seeing or downloading contents),⁷ unlike other kinds of consumption. If this is maintained, and the relative importance of this kind of public (or semi-public) goods grows, this could lead to a fiscal erosion of the tax base, but perhaps, in the future, to a greater equality in consumer levels, as the constraining

⁶ One may also refer to well known arguments in Public Economics concerning the choice of various organizational solutions, relating, for instance to issues of imperfect and asymmetric information, or to transaction and supervision costs, which in specific sectors may lead to prefer public to private production. Public non-profit production may be preferable whenever the nature of the product cannot be sufficiently appreciated by the public, and there is need of strict quality control (such as in the provision of education or health services: for instance a recent inquiry has established that in the USA the mortality rates in for-profit hospitals are higher than in non-profit hospitals. Source: BBC news bulletin 27/05/2002).

⁷ One should not be confounded by the fact that one pays taxes on the medium of access (in particular telephone calls). This kind of taxation can be compared to the taxation on paper, with respect to the taxation of books, or the taxation on vinyl for the production of vinyl records, a trifle in relation to the value of the contents of the media concerned.

factor becomes (in the more prosperous countries at least) time, rather than purchasing power. Analogous considerations can be made with respect to TV broadcasts, as with digital TV the number of channels increases and entry barriers decrease. Thus we have entered a period where the nature of consumption is quite different from those times where, even in relatively more prosperous countries, the great bulk of consumption was made up by predominantly private goods (food, first of all, but also clothes, shelter and transportation). This implies an involuntary, but important element of socialism, because of the socialization of a growing part of consumption, which is basically allocated without being rationed through purchasing power.⁸ (There is a kind of paradox here. In most cases the new goods are enjoyed individually, in the intimacy of one's homes, even if through the access to a virtual agora, while some of the kinds of consumption that the new ones are displacing--theatres, cinemas, concerts, conferences--represent forms of collective enjoyment, even if their prevailing character is, economically speaking, of being private goods.) This can also explain the fact why the Internet revolution has not translated, in the USA in particular, where it was particularly strong, into a corresponding increase of the growth rate of productivity. Simply, part of the "output" of Internet is made up by public goods that directly enter into the consumer utility function, and could be measured in theory in terms of the value of private goods that can substitute in the formation of real income, but in practice may be not adequately accounted for in the calculation of national income. It is obvious the incentive problem of a society where an ever increasing part of consumption is made up by public goods, for the enjoyment of which the only relevant constraint is the available free time. This implies a progressive increase in

⁸ There is a countertendency however in the expansion of very costly medical treatments following steady medical advances, that have the intrinsic nature of private goods, and in the present emphasis towards the reduction of some traditional types of collective consumption, derivative to the general emphasis towards reduction of the share of public expenditure in national income. But this trend could be easily reversed, in relation to experience and the awareness of the inconveniences associated to private substitutes (see the above mentioned case of Railtrack).

relative utility of the latter, with increasing negative effects on labour supply and on the creation of the tax base needed to finance, among others, the production of public goods. In the limit, the only way out could be the re-introduction of such outdated revenue sources such as capitation, wealth taxes or state monopolies. An obvious additional second best measure could be, whenever possible and not too costly, to tax the time used for accessing public goods, and in particular, the time used for accessing the Internet.⁹ But such a measure would be hardly popular, even if in the future it could become necessary.

Will public production ever become more efficient than private production?

Let us now pass to the consideration of the relative expediency of public vs. private production, not only of public, but also private goods. As long as the sentiment of individual responsibility and the respect for the public interest will grow with civil and economic progress, through the accumulation of human and social capital, one could not exclude that public management of production could eventually become as efficient as the private capitalist one, or even more, especially if people would prefer to work in the framework of an organization aiming to the fulfilment of the public rather than of the private interest. For instance, there are those who are allergic to the specific business culture of private firms in general, and of corporations in particular, and would rather work, even at lower wages, in organizations with a different culture, aiming to the satisfaction of social needs and of a public interest. This attitude can express itself in the private but communal production of public goods, where an important part of motivation, which could be appreciated as a “socialist” one, is to be part of a community of producers and consumers, without the pursuit of a private gain corresponding to the overall value of the public (in sense of non-rival) goods that are created, and of which excludability is not sought. This obviously applies to the Linux-Thornvald open-source model, as opposite to the rival one Bill Gates-

⁹ See Dan Anderberg, Fredrik Andersson, Alessandro Balestrino, “Time, Self-Selection and User Charges for Public Goods”, *FinanzArchiv*, vol. 57 (2000), pp. 137-154.

Microsoft. We have here private production for the generation of public goods, where the individualistic profit motive is moderated by a communitarian philosophy aiming to a, partly at least, disinterested pursuit of communitarian objectives. There is nothing essentially new into it: it is the same kind of motivation of political or philanthropic activity at its best.

Aside from the latter case, if the supposed future higher efficiency of public production leads, as it should in a market economy, to higher profitability, public enterprises, or may be mixed enterprises with public control, in equitable competition, without bending rules or budget constraints in favour of anybody, being more profitable would grow more rapidly than the private ones, and in the contest of the two systems socialism of the means could anew appear as a viable alternative. Obviously there are those who would deny the significance of profit as an adequate measure of entrepreneurial efficiency, and they would have many valuable reasons for their denial. Unfortunately, it seems that no better rule of thumb for measuring performance does exist. In the end it is on the formation of profit (or surplus value) that the possibility of enterprise development and, in the aggregate, of the development of the economic system as a whole, depends. It up to the state to determine, however imperfectly, the rules and the conditions that make of entrepreneurial profit an adequate (if by far imperfect) social efficiency index of economic performance: here again we have to deal with the fallacy of (im)perfection. If an index is imperfect, this is no sufficient reason to throw it away if it has some significancy, and no better exists.

As we have already mentioned, in the experience of Western economies in general the public sector has been characterized by lower efficiency. But there have been cases where public enterprises have shown to be no less efficient than the capitalist ones (a good case in point seems to be that of the Régie Renault). In the countries of the old Socialist bloc, the socialist system did not arise from the factual demonstration of the superiority of public towards private production, but from the prohibition of private ownership and entrepreneurship, implemented through repression, requisitions and the introduction of radical limitations to the freedom of contract, thus blocking the competition between different forms of ownership and organization. But the contest

continued outside the borders of the socialist block. The forcible suppression of institutional competition and of the tool of progress given by rival competition between firms, independently of their ownership structure, has brought about in the end the doom of the socialist regimes, as it has not allowed bringing about those higher living standards that their citizens were able to observe in the West. However, if public entrepreneurship were one day to prove more efficient, at least in some sectors of the economy, the process of privatization of the economy could reverse, provided competition between different types of entrepreneurship is guaranteed. In this perspective, every artificial intervention to alter the equality in the rules of competition between enterprises characterized by different ownership structures must be rejected.

Public production, private production, efficiency and egalitarianism

For those who have an intrinsic preference for socialism of the means, the greater, or even equal, efficiency of public enterprises could be a sufficient condition for the choice of a socialist system, as in this case their preference could be satisfied without sacrificing efficiency.¹⁰ It would not be a necessary condition, insofar as who has an intrinsic preference for a socialist system could be ready to sacrifice efficiency in order to bring about its implementation. But if preferences were socialist in the aims only (for instance, great weight given to equality) and a socialist system would allow to attain, for every efficiency level, greater equality, the attainment of a not-lower efficiency level would be a sufficient condition for the implementation of a socialist system. This is in theory. In practice the divergence in efficiency that has been shown

¹⁰ Obviously, other non-economic factors enter in the choice between public and private, in particular those relating to the economic conditions for political and cultural pluralism. Generally speaking the latter is associated to the existence of a private market economy. On the other hand this is no guarantee of pluralism, as is demonstrated, as a clear-cut case, by the overwhelming control of mass media by a single tycoon in Italy. At the same time one could envisage, even in a system with overwhelming public ownership, some decentralization in decision making, and competition between enterprises owned by different public entities.

in history is such that only a clear demonstration of a change in the nature and functioning of public enterprises could bring back into play the socialism of the means as a choice alternative.

All depends however on the structure of social preferences. If the socialism of means were acknowledged as the most suitable instrument to bring about egalitarian outcomes, and the social preference system is bent very much toward equality, this could lead to the reintroduction of classical socialist solutions. However, what we have learned of income inequality under capitalism and socialism suggests that distributional structures not less equal than those in the countries of real socialism could be brought about in capitalist economies, in presence of suitable redistributive policies.¹¹ But the issue is far from simple. In different economic systems, independently of preferences, the effective trade-off between efficiency (however defined) and equality can be different. This trade-off can also be different nowadays in relation to the past, because of the changes intervened in the international and technological context. Thus, even if preferences are unchanged, the choice between efficiency and equality could in practice lead to a different mix, with an increased weight given to the first, bringing about at the

¹¹ This is not entirely certain, however. For one, the socialist countries were at lower development levels. Therefore the significance of the comparison is affected by the long-drawn question of the relation between development and distribution. Moreover there are a host of statistical problems that derive from some fundamental differences in the two systems to be compared, which are usually disregarded, in particular how to make allowance for the different structure of the prices consumer goods, and the limitations to the availability of the latter under real socialism. On these issues see Alberto Chilosi, "Comparisons of Income Distribution East and West, before and after Transition: Some Methodological Issues", *Statistics in Transition*, vol. 1, n. 5, Sept. 1994, pp. 641-653. For the data concerning the comparisons in income distribution between Western market economies and the countries of real socialism, see A. Atkinson, J. Micklewright, *Economic Transformation in Eastern Europe and the Distribution of Income*, Cambridge, Cambridge Un. Press, 1992; A. Chilosi, "Distributional and Redistributive Processes in Soviet-type Economies and the Distributional Impact of Institutional Change", in: Camilo Dagum, Mario Zenga (ed.), *Income and Wealth Distribution, Inequality and Poverty*, Berlin, Springer Verlag 1990, pp. 389-403, and the literature quoted there.

same time higher income levels and higher levels of social preferences, at the cost, however, of higher inequality, as shown in the following figure:

equality

A

B

capitalism

socialism

Per capita income

Alternative choices between equality and per capita income above subsistence level (as an efficiency index), by given preferences, but in two different systems, or contexts, that variously favour equality or efficiency. (It must be noted that the preferences that are represented are relatively egalitarian, as the indifference curves are relatively flat, even if not to the point of being lexicographic.) As to the shape of the frontiers, which can be assumed as deriving from the effective specific characteristics of functioning of the two systems, there is no pretension to realism, and it can be drawn making the most various assumptions. For the sake of the argument it is enough to assume that the tangency point with the map of indifference curves is placed in capitalism to the northeast of that of socialism and corresponds to a higher indifference curve. One may note that the degree of “socialism” of preferences is given by the flatness of the indifference curves. In case they were more “socialist” than those drawn here, the tangency point corresponding to the highest indifference curve could correspond to the choice of a socialist system. But, according to the experience of socialist countries, even there the degree of socialism of preferences has not been strong enough to compensate for the reduction in the average living standards and in the scope of consumer choices, in relation to those believed to be possible in the long run with a different systemic choice.

Obviously, the preference structure can be system-dependent, but it is far from

obvious in what sense it would be. It is not obvious that the instauration of a socialist system, for instance, could alter the preferences in favour of equality, even more if the public understands that, as in the case of the figure, the choice in favour of equality is to the detriment of the living standards. In some ways the preference structure itself could in fact be altered by the effective outcomes. For instance, the awareness of the stronger inequalities generated in market economies could determine a flattening of the indifference curves, as a consequence of the moral indignation that this could generate.¹²

The relevance of the third sector

The Darwinian argument can also apply to specific non-capitalist entrepreneurial forms that normally are considered to have socialist character, such as cooperatives. These have a role to play, aside from a marginal existence, artificially fostered by ad hoc policy measures, as long as they are able to successfully compete and prevail at equal conditions with the capitalist firms of traditional type. Moreover, the problem of how to organize the competition to capitalist entrepreneurship by the possible non-capitalist entrepreneurial forms that may spring from collective initiatives in the framework of civil society is trivial, as the basic organizational principle on which this competition can be based is simply the fundamental principle of the freedom of contract. More complex issues are implied by the organization of the competition by state entrepreneurship. Enterprises with a state majority ownership could be free to organize themselves, provided they could pay their ways and not depend on public subsidies for their survival. Their growth should be dependent on their possibilities of self-financing, and of drawing resources on the financial markets and, thus, in the end, on their ability to generate profits.

¹² A recent ample empirical inquiry has shown a marked orientation much more in favour of equality in the economies in transition than in Western Europe (Marc Shrecke, "Preferences for Inequality: East vs. West". Innocenti Working Papers, No. 89, October 2001). Thus, it seems that the persistence of the distributional values of the previous system prevails there.

One could avoid to actively privatize the existing state-owned firms, and at the same time to finance them from the public purse, leaving to the market the decision whether their relative importance in the economy should grow or should sink, or whether, in order to survive, they should change their ownership structure, accepting growing shares of privately owned capital.¹³ For those firms that enjoy monopoly rents the solution is not privatization as such, but the elimination of monopoly power. It is well known that private monopolies are no better, even with respect to efficiency, than public monopolies. A difficult issue is how to organize the freedom of entry of publicly owned enterprises, in name of pluralism and of the competition of different entrepreneurial forms. One could for instance attribute the power of establishing them to the authorities of local self-government (such as communes, regions, provinces), in the framework of the general freedom of economic initiative. But obviously one would need some kind of limitation as to their continuing financing by the founders. Similar considerations could be made with respect to mixed-ownership enterprises.

The argument of systemic externalities

It remains, for the supporters of socialism of the means, the countervailing argument of the systemic externalities, according to which success in bringing about socialism could follow only after the complete suppression of capitalist institutions.¹⁴ The

¹³ This was the solution, Darwinian in character, that I proposed, at the beginning of the transition process, for the transformation of the socialist economies, obviously accompanied by the abolition of the prohibitions to private entrepreneurial activities (cf. Alberto Chilosi, "Privatisation through Competition", *Jahrbuch der Wirtschaft Osteuropas*, vol. 14, n. 2, 1990, pp. 182-184).

¹⁴ A motive could be the possible relationship between economic institutions and social preferences, the nature of which however is not necessarily obvious or of simple determination. See in this respect Samuel Bowles, "Endogenous Preferences: The Cultural Consequences of Markets and other Economic Institutions", *Journal of Economic Literature*, vol. XXXVI (March 1998), pp. 75-111.

argument is rather worn-out. The suspicion is that in practice this could occur only because in this way the terms of comparison for judging success or failure are suppressed. The same applies to the argument that justifies the special support to given types of organization of economic activity (cooperative, with elements of industrial democracy, small firms vs. big firms etc.) with the argument of the political and social externalities.¹⁵ Often these arguments and the ensuing subsidization of “non profit” are the reflection of a preconceived ideological aversion towards entrepreneurial profit, derogatorily identified with “speculation”, such as one could find, disgracefully, even in the Italian Constitution (art. 45). The argument is dangerous because it allows the justification of every possible intervention altering the competition between alternative forms of productive organization. In particular, it is worn-out in Italy where it was variously utilized in practice, in relation to the different propensity towards the financing of the various political parties by the different entrepreneurial forms. In reality, measures of this kind do not help the alternative organizational forms to develop all their supposed potential, favouring rather their lingering in a protective niche, the extent of which depends on the actual transfers of resources (possibly in the indirect form of fiscal exemptions) from the more productive organizational forms. If one sees in the development of non-capitalist forms of entrepreneurship an opportunity for an eventual transformation of the overall organization of productive processes, one cannot make their survival conditional to the existence of other organizational forms from which to be able to suck resources. If they are considered as a permanent minor organizational feature, their continuous non-self sufficiency and subsidization can jeopardize their legitimization. One must also consider that special concessions (which in the end amount to subsidies) for given organizational forms induce the distortion of the apparent entrepreneurial form, with the purpose of taking advantage of those special conditions. The latter then come to be applied to those who

¹⁵ This reminds one of the potential justification of every type of protectionist policies by the infant industry argument. Even the support of decrepit industries can be justified through an adaptation of the argument to that of rebirth and new development (“restructuring”).

should not been entitled, unless a host of specific limitations, controls and verifications of a bureaucratic nature are introduced. This would otherwise hinder the development and expansion of those entrepreneurial forms that in the first instance one would like to favour and promote.

Institutional experiments and transition

Even if the basic institutional foundations of a system (presently the capitalist one) have turned out as winners in the contest of the systems, one is still left with the issue of which kind of specific institutional varieties and combinations of them would bring about the best results. That a system can gradually and successfully be transformed through experiments and insertion of original elements deriving from another system, until, possibly, changing into a fundamentally different one is shown by the lesson of the progressive Chinese transformation after 1978. The direction of change in China points in fact towards a progressive reduction in the scope of state ownership and entrepreneurship in favour of different kinds of entrepreneurship and ownership structures (municipal, private, mixed). Similarly, in the future the capitalist economies could be transformed gradually in an opposite direction, whenever the conditions that have been discussed above for a successful transition towards non-capitalist forms of entrepreneurship would be met.

This approach, of gradual and empirically founded institutional transformation, could hardly solve the problem of institutional transformation in the countries of Central and Eastern Europe after the demise of the Soviet model. In the case of China we have institutional experiments that in case of favourable results are expanded, possibly restricted to a part only of a country with a huge population and territory, what was feasible because of the territorially instead of sectorially based structure of socialist planning, in the framework of a political and social system that has stability and

internal consistency.¹⁶ One should also consider that this was taking place in a context of great economic backwardness, where at the basis of the economic system, after the liquidation of the communes, there was the productive unit made up by the peasant family.¹⁷

Whenever the legitimation of the previous system collapses abruptly, in much more

¹⁶ Cf. Gérard Roland, *Transition and Economics*. Cambridge (Mass.), MIT Press, 2000, p. 57. The great advantage of territorial reform is that it can pay due attention in a limited territory to a set of interrelations that more difficultly could be managed in a national framework, without introducing strong elements of irreversibility, because of the costs (non only economic, but political and social as well) needed to reestablish the previous state.

¹⁷ Moreover, one should not downplay the relevance of the tradition of the autonomous role of the peasant village: “ever since Ming-dynasty villages and rural communities became the natural owner of natural resources (except land), the agency of last resort for civil and moral law, the basic unit of defense, and the primary collective actor in the political and social arena. Despite some attempts by Chairman Mao, this did not change much during the Mao Zedong-era” (Barbara Krug, “Ties That Bind: The Emergence of Entrepreneurs in China”, ERIM Report Series reference number ERS-2000-44-ORG, November 2000, p. 12, downloadable from www.irim.eur.nl). This tradition of autonomy has allowed the village to develop its economic and organizational potentialities, stimulating the institutional innovations that lie at the basis of the Town-Village Enterprises. The nature of the latter is somewhat controversial, but under the appearance of the formal municipal ownership complex contractual relationships are hidden in many cases. This makes of these enterprises masked forms of private or mixed entrepreneurship, remedying, at the same time, for the institutional restrictions to a market for those capital goods whose ownership remains public. (Cf. Barbara Krug, “The Interdependence Between Political and Economic Entrepreneurship”. Erasmus Research Institute of Management, November 2000. ERIM Report Series reference number ERS-2000-43-ORG, downloadable from <http://www.eur.nl/WebDOC/doc/irim/erimrs20010209141037.pdf>; Oxford Analytica, “Battered and Cherished: The Private Sector in China”, *Transition Newsletter*, vol. 11, n. 6, January 2001, pp. 13-14).

advanced economic contexts, gradual processes of transformation are much more difficult, and a natural tendency to engender a great leap forward arises, sometimes in the same vein as the old voluntaristic fallacy. The ex-post results have not been, to say the least, really brilliant, in the short-middle run at least (where the middle run is, in our case, a ten-years period).¹⁸ Moreover, one may consider that on average the worst results have occurred in those countries that have not undertaken the institutional transformation with singlemindedness and consistency. But the issue of transition is really complex and could easily carry us away.

The future of capitalism and socialism

In the end, considering the future of capitalism and of socialism we must exert caution. Everybody can have the hindsight of the past, but nobody has the hindsight of the future, and so many false predictions have been made, even by prominent authorities, in the past. The only comfort is that posterity will certainly not read our speculations here, and even in the improbable case it will, we will not there to bear the brunt of their well deserved criticism. Speculation about the immediate future may be risky, but about the distant future has the advantage, in the end, to be harmless, for the speculator at least.

¹⁸ A problem with gradual reform lies in the institutional compatibilities that it can engender. For instance, a problem, in the case of liberalization of private entrepreneurship, lies in the fact that in an economic system with price control and unbalanced market, private activity can profitably concentrate on mere arbitrage. In the case of China this issue is solved through liberalization at the margin, without destroying in sudden and radical way the old system of compulsory consignments and of price controls, as has taken place in various Eastern European countries that have adopted the big-bang strategy, with adverse social and economic effects. On these issues cf. Gérard Roland, *Transition and Economics*. Cambridge (Mass.): MIT Press, ch. 6, pp. 131-152.