

# **THE ECONOMIC SYSTEM AS AN END OR AS A MEANS AND THE FUTURE OF SOCIALISM AND CAPITALISM: AN EVOLUTIONARY VIEWPOINT<sup>1</sup>**

Alberto Chilosi  
Dipartimento di Scienze Economiche  
Facoltà di Scienze Politiche  
via Serafini 3 - Pisa  
E-mail: chilosi@sp.unipi.it

## **ABSTRACT**

After the demise of “real” socialism and the decline of “western” socialism, 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. At the same time there is a case for maintaining an institutional framework allowing different forms of economic organization, capitalist and non-capitalist, to compete on equal footing, in an evolutionary perspective, thus allowing the second to develop if proven efficient. Another way for a spontaneous extension of the domain of socialism could derive from the socialization of consumption, if the consumption of public goods continues to make up a growing component of real consumption.

JEL Classification number: P50

---

<sup>1</sup> A much shortened version has been published in *Economic Systems* (vol. 26, 2002, n. 4, pp. 401-407). This paper was originally prepared for a session on the “Future of Capitalism” at the Annual Scientific Meeting of the Italian Economic Association, Rome October 2001. Subsequent versions have been presented to a seminar in the Department of Economics, University of Pisa, to the 7-th Conference of EACES, June 2002, and to the 11-th IAFEP Conference, July 4-6, 2002. I am grateful to Domenico Mario Nuti and to participants in those events for useful comments and suggestions. Needless to say, I am the only one to blame for its present contents.

### ***1. 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. Thus, 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. 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 (historically speaking) such a choice brings about. This remark applies both to economic and political systems. For instance, the second viewpoint is often applied 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, as it renders relatively more probable social states that are higher valued relatively to widely (albeit not unanimously) shared social values.

### ***2. 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 stage would be 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, as is 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 from 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.

### ***3. 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.<sup>2</sup> 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

---

<sup>2</sup> For a extensive non-technical consideration see Berliner (1999). As Stiglitz (1994, p. 243) puts it, “we live in an imperfect world, in which often we face nothing but the choice of the lesser of two evils!”

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, at least).

Owing to the inevitable shortcomings of really existing systems, and the experience of the last century, the only reasonable perspective seems to me to consist 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, rather than 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.

#### ***4. 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 a (“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 and the weighting of the objectives, independently of the institutional means that are used for their pursuit.

### ***5. 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”.<sup>3</sup> Moreover some institutions that are usually considered as socialist could be

---

<sup>3</sup> “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” (Schumpeter, 1976, p. 163).

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 evolution into a capitalist mixed market economy, where the capitalist element could become dominant in the future.

As far as the public<sup>4</sup> ownership and management of economic activities goes, they have been shown in the past to be on the whole less efficient,<sup>5</sup> but one cannot exclude that they may become relatively more efficient than private ownership and management in the future.

#### **6. Public goods, collective goods, and the socialization of consumption**

First of all the nature of available consumer goods could change, leading to an increase in the relative importance of public goods, thus increasing the scope for direct public provision, as a consequence of changes in technology and tastes, with possible egalitarian effects. Among the alleged characteristics of a socialist system there is the tendency towards socialization of consumption, this means an allocation of consumer goods independent of individual budget constraints. This view finds a counterpart in Marx's *Critique of the Gotha Programme*: the part of social 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

---

<sup>4</sup> Here and below by "public" ownership or entrepreneurship we broadly intend "non private".

<sup>5</sup> In particular, in dynamic terms, as to 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 unconstrained 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 Bergson, 1987, and 1992. For the issue of relative efficiency of public enterprises in mixed economies, see the many references to empirical analyses in Megginson and Netter, 2001, sect. 3, pp. 328–338.

new society develops".<sup>6</sup> There are three types of consumption that can be of relevance here: 1) collective consumption proper, which may be made up by private, public or semi-public goods in an economic sense whose production and distribution is decided collectively through the political process and is not rationed through private budget constraints (such as public provision of health, education, social services, defence, law and order, national broadcasting, even private consumer goods under the future hypothetical abundance of Full Communism and saturation of needs. 2) Pure public goods, which are privately or publicly produced on a commercial basis and are freely available, usually financed through joint production of a public externality, typically advertising. But in case of advertising production of public goods is strictly derivative on the existence of a large market for private goods, where the returns to advertising could be reaped.<sup>7</sup> 3) Non-rival but excludable goods for the consumption of which a royalty could be charged. There is a clear market failure here that may (but need not) constitute a reason for public provision. Moreover, if the barriers to entry are low (such as in the case of the setting up of Internet sites), and no conditions of natural monopoly apply, competition would bring the fees down towards the point where fees just cover costs, where fees may be quite disproportionately low in relation with the consumer surplus that is created. Moreover, in order to have the provider of the good (say, the Internet site or the broadcasting site) known to the public, some initial losses would be occurred and the good would be made available, as it may often be the case, for nothing or very little fee. Since this is an ongoing process (as the dynamics of Internet sites may show) those whose opportunity cost of time is lower may look for the newcomers rather than pay the incumbent sites for their services. This opportunity would benefit the worse off, who by spending some of their time could avoid paying for the same kind of goods the others are enjoying at a fee. Thus their substantial nature of public goods, as far as non-rivalry is concerned, could still be dominant in

**Commento:** Si potrebbe fare un modellino dell' economia considerate nella nota, nell' ambito di una trattazione complessiva dei public goods.

---

<sup>6</sup> This statement was inspiring the 1961 Programme 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". Cf. Chilosi, 1978.

<sup>7</sup> At its turn public free provision of public goods may be effected only as long still remains a substantial part of consumer goods that are private in an economic sense. In a world in which all goods were public and publicly provided by the state for free there would no way of financing their production but through direct taxation of free time or through direction of labour.

the way consumption is allocated. In other words, in case dominant positions are realized through sunk costs and network economies of scale, because of significant dynamic contestability and the degree of the economies of scale, the fees would often tend to be very low in relation to the substantial nature of the goods, and to the consumer surplus that may be created, and consumers with low opportunity cost of time could avoid paying altogether.

Of the above three categories of goods, only the first makes up collective consumption in the sense that is collectively decided, through political representation and allocated irrespective of budget constraints. It is this category that is referred to by Marx in the *Critique of the Gotha Programme*, where he mentions schooling and health. Of course there could be some mixed cases, such as when the access to public health or education is conditional on the payment of a fee. On the other hand the expansion of multimedia products that have some intrinsic characteristics of public goods (radio and TV broadcasting, Internet) has been financed to a great extent through the simultaneous issuing of what we may call public externalities, namely externalities that have mainly the characteristics of a public good (or a public bad), as far as non-rivalry and non-excludability<sup>8</sup> are concerned, 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 revenue. This financing is however limited by the overall amount of advertising. There can be some obvious theoretical reasons in favour of pushing forward those limits through public financing or direct public production (in particular advertising-free production for the benefit of those, like the present author, who consider radio and TV advertising definitely as public bads). A difficult problem arises, however, as to who has the right to determine its contents. Moreover, the channels of delivery of those products (in particular cabling) can acquire the characteristic of natural monopolies, which in turn can justify public provision. The interesting experiment of infrastructural privatization, which has been made in the UK with Railtrack, has clearly shown the limits of privatization of public infrastructures amounting to national monopolies. An important element for the failure of the Railtrack experiment were safety considerations, which are specific to

---

<sup>8</sup> In case at least the public good they are associated with is consumed, even if non-excludability is partially jeopardized by remote control.

railways, but this points to the fact that in the area of basic infrastructures at least, public direct production may still present some comparative advantage. Moreover, public non-profit production, such as in the areas mentioned by Marx, health and education, may be preferable whenever the nature of the product cannot be sufficiently appreciated by the public, and there is need of strict quality control.<sup>9</sup> This may mitigate the potential impact of the growing importance of some types of medical services that are increasingly costly and are intrinsically private goods, as there could be some good reasons, owing to their specific nature, for a public provision, and an allocation through assignment rather than through the market. As to the growing relevance of public and semi-public goods, on the one hand the private provision of public goods may be simply financed by the state, and on the other those 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).<sup>10</sup> In the case of TV and radio broadcasting subsidies 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 the 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),<sup>11</sup> unlike other kinds of consumption. If the relative importance of this kind of public (or semi-public) goods grows, this could lead to a fiscal erosion of the tax base (because of the relative reduction of taxable goods together with the wealth effect), but perhaps, in the future, to a greater equality

**Commento:** Scartato: 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.

---

<sup>9</sup> 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.

<sup>10</sup> A private financing through payment of accesses could be impractical because of the high transaction costs in relation to the value of any single access.

<sup>11</sup> One should not be confounded by the fact that taxes are paid on the medium of access. This kind of taxation can be compared to the taxation of printing paper, with respect to

in consumer levels, as the constraining factor becomes (in the more prosperous countries at least) time, rather than purchasing power, as well, in the case of some public goods, education (and in this a regressive element may persist). 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 may be in a period when the nature of consumption is quite different from those times when, even in relatively more prosperous countries, the great bulk of consumption was made up by predominantly private goods (food, first of all, but also clothing, shelter, transportation and personal services) that were unequally distributed.<sup>12</sup> This implies an involuntary, but important element of socialism, because of the socialization of a growing part of consumption, which basically is not rationed through purchasing power.<sup>13</sup> (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 could also contribute to explain why the Internet revolution has not brought

---

the taxation of books, or the taxation of vinyl for the production of vinyl records, a trifle in relation to the value of the contents of the media concerned.

<sup>12</sup> It should be noted however that a specific type of public goods consumption, such as the satisfaction deriving from the power and prestige and the territorial conquests of one's country, which could be achieved through investments in armies and wars, seems to play happily enough a lesser role in the modern world than in a not too distant past.

<sup>13</sup> There is a countertendency however in the expansion of very costly medical treatments (such as transplants) following steady medical advances, that have the intrinsic nature of private goods (but see the remarks above in the text), 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). Moreover cost effectiveness (as well as equity) considerations could lead to privilege those sectors of medical expenditure which lead to production of public goods in the area of prevention, diffusion of medical knowledge, hygiene and epidemiology. An obvious case concerns the alternative between medical expenditure in the treatment of Aids (which is essentially rival) and that towards prevention through the diffusion of the knowledge leading to a decrease in those types of behaviour that favour its spreading.

about the increase of the growth rate of productivity that some would expect.<sup>14</sup> 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 national income accounting. The incentive problem of a society where an ever-increasing part of consumption is made up of public goods, for the enjoyment of which the only relevant constraint is the availability of free time, is obvious. The relative utility of leisure increases, 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.<sup>15</sup> 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, such as in particular, the time used for accessing the Internet.<sup>16</sup> But such a measure would be hardly popular, and could have intrinsic negative costs in terms of efficiency, given the quasi-public good nature of Internet access. In the end, given the contradiction between the efficiency objective pointing towards encouraging and possibly subsidizing the production of Internet contents, given their nature of public (or quasi public) goods, and the financial considerations leading to the taxation of the time spent on the Net, the actual situation where the Net is basically neither taxed nor subsidized may appear as a reasonable compromise, resulting in the minimization of transaction costs.

---

<sup>14</sup> For these kinds of issues one may refer to Gordon (2000). Unlike other authors (in particular those whose contributions are contained in the same issue of the *Journal of Economic Perspectives*) Gordon does have a reductive consideration of the potential impact of Internet and IT on productivity.

<sup>15</sup> See however Corneo (2001), according to whom there is a positive correlation in OECD countries between hours of work and hours of television viewing. This is explained by the existence of an inefficient equilibrium, which is dominated by another possible one, in which work hours are shorter and agents spend more time socializing; the dominant equilibrium is blocked by the externality implicit in socialization (the availability of others to socialize increases the advantage of socialization). Another relevant consideration (which is made by Gordon, 2000) is that free time spent using new technologies is alternative not so much to work time and consumption of private good and services, but with other kinds of uses of free time (playing cards for instance).

<sup>16</sup> See Anderberg, Andersson, Balestrino, 2000.

### **7. Will Public Production Ever Become More Efficient Than Private Production?**

Let us turn now to the consideration of the relative expediency of public vs. private production, both of public and of private goods. As long as the sentiment of individual responsibility and respect for the public interest grows with civil and economic progress, through the accumulation of human and social capital, one cannot exclude that public management of production could eventually become as efficient as the private capitalist one, or even more if people will prefer to work in the framework of an organization aiming to the direct fulfilment of the public rather than of private interest. For instance, the number of those who dislike 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 or with a public principal, may increase in time.<sup>17</sup> This attitude can express itself in the private but communal production of public goods, where a motivation, which can be appreciated as “socialist”, is to be part of a community of producers and consumers, without the pursuit of a private gain in some ways related to the overall value of the public (in the 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-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.<sup>18</sup> 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 could grow more

**Commento:** Soppreso: In fact one cannot exaggerate the importance of the overall cultural environment for the performance of a market economy. Weber's consideration of the relationship between religion and economic performance, and the very poor performance of some previously socialist economies, turned to market, are two cases in point. Some recent corporate catastrophes brought about in the USA by a selfish and opportunistic business culture deprived of an adequate sense of responsibility and public service are another

---

<sup>17</sup> This kind of attitude could also be more compatible than the selfishness or some types of narrow business culture for building those relations of trusts and cooperation that are of fundamental importance for a successful market economy.

<sup>18</sup> There is nothing essentially new into it, as is akin to the motivation of political or philanthropic activity at its best or even, to some aspects of the motivation of entrepreneurial activity as such.

rapidly than the private ones, and in the contest of the two systems some sort of the socialism of the means could anew appear as a viable alternative.<sup>19</sup>

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.<sup>20</sup>

In the countries of the old Soviet 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, requisition, 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.<sup>21</sup>

The forcible suppression of organizational competition and of the tool of progress given by rival competition by firms independently of their ownership structure, has led in the end to the doom of the socialist regimes, as they could not bring about those higher living standards that their citizens were able to observe in the West. However, if non-capitalist 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

---

<sup>19</sup> But is the ideology of public service compatible with the one of profit making? They are not necessarily mutually exclusive, once profits are seen as the source of the means through which the pursuit of public service can be increased. Obviously there are many reasons to deny the significance of profit as an adequate measure of entrepreneurial efficiency. 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 is up to the state to determine, however imperfectly, the rules and the conditions that make 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 significance, and no better exists.

<sup>20</sup> A good case in point seems to be that of the Régie Renault. For other relevant cases see for instance Stiglitz, 1994, p. 20.

<sup>21</sup> One must consider here that while in Western economies competition to capitalist firms remained open in principle by firms privately organized according to alternative principles (such as cooperatives or non profit of any sort), as well as, in a number of countries, by state-owned enterprises, this kind of competition was not allowed in the East: non-socialist firms were either completely outlawed or severely restricted. Hence, when eventually real socialism collapsed, this meant the defeat of a comprehensive

maintained. In this evolutionary perspective every artificial intervention to alter the equality in the rules of competition between enterprises characterized by different ownership structures should be rejected.

### ***8. 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.<sup>22</sup> It would not be a necessary condition, insofar as those who have 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, greater weight given to equality) and a socialist system were to allow the attainment of greater equality for every efficiency level, the attainment of a non-lower efficiency level would be a sufficient condition for bringing about the implementation of a socialist system. This is in theory. In practice the divergence in efficiency that has been shown 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 socialism of the means as a choice alternative. All depends however on the structure of social preferences. If socialism of the 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 no less unequal than those in the countries of real socialism (as far at least personal income distribution is concerned) could be brought about even in capitalist

---

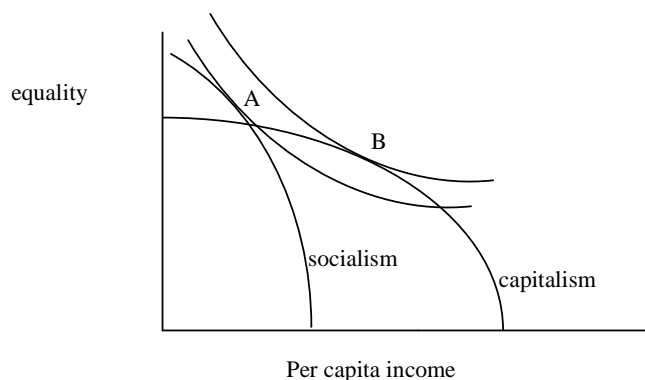
system of production, with no available real ready alternatives. This may partly explain the severity of the consequences of the fall.

<sup>22</sup> 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 with the existence of a private market economy. On the other hand this is no automatic guarantee of pluralism, as is demonstrated, as a clear-cut case, by the overwhelming control of mass media by a single tycoon, leader at the same time of the strongest political party, in Italy. Moreover 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.

economies, in presence of suitable redistributive policies.<sup>23</sup> 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 same time higher income levels and higher levels of social preferences, at the cost, however, of higher inequality, as expounded in the following figure:

---

<sup>23</sup> This is not entirely certain, however. For one, socialist countries were at lower development levels. Therefore the significance of the comparison is affected by the long-drawn question of the relationship 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 Chilosi, 1994. For the data concerning the comparisons in income distribution between western market economies and the countries of real socialism, see Atkinson and Micklewright, 1992; Chilosi, 1990, and the literature quoted there.



Alternative choices between equality and per capita income above subsistence level (as an efficiency index), with 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 the functioning of the two systems, there is no pretension to realism, and they 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 southeast 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”, and thus flatter, 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. Of course there are a lot of further questions concerning political institutions, but these are out of the scope of the present paper-

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, would 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. The preference structure itself could in fact be altered by the effective outcomes. For instance, the awareness of the stronger inequalities in a market economy could determine a flattening of the indifference curves, as a consequence of the moral indignation that this fact may generate.<sup>24</sup>

### ***9. The Relevance of the Third Sector***

The evolutionary argument can also apply to specific non-capitalist entrepreneurial forms that normally are considered to have a 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 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 for self-financing, and for drawing resources in the financial markets and, thus, in the end, on their ability to generate profits. One could also avoid to actively privatize the existing state-owned firms, while avoiding 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

---

<sup>24</sup> A recent ample empirical inquiry has shown a marked orientation in favour of equality in the economies in transition much more than in Western Europe (Shrcke, 2001). Thus, it seems that persistence of the distributional values of the previous system prevails there.

ownership structure, accepting growing shares of privately owned capital.<sup>25</sup> 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 any 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, 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.

### ***10. 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. A motive could refer to the dynamics of organized interests and pressure groups altering the conditions of competition, possibly “capturing” those in charge of determining and enforcing these conditions. But in reality every existing organization enters in this kind of dynamics. Non-capitalist types of firms, such as cooperatives or non-profit, not to speak of state-owned enterprises, may succeed in building forms of social representation and defensive lobbying that by no means are less effective than those of capitalist firms.<sup>26</sup> An additional motive could be the possible relationship between economic institutions and social preferences, whose nature however is neither obvious nor of simple determination.<sup>27</sup> The same applies to possible changes in individual personality induced by the nature of the social and economic system.

On the whole the argument of systemic externalities is rather worn-out. The suspicion is that in practice its real justification lies in the objective of suppressing the terms of

---

<sup>25</sup> 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. Chilosi, 1990).

<sup>26</sup> As borne out at least by the Italian case.

<sup>27</sup> See in this respect Bowles, 1998.

comparison for judging success or failure. One could also be wary of the justification of the special support to be given 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. 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 justifies every possible intervention altering the competition between alternative forms of productive organizations. 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 on the existence of other organizational forms from which they are 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 for given organizational forms induce distortion of the apparent entrepreneurial form, with the purpose of taking advantage of those special conditions. The latter then may be applied to those who should not be entitled, unless a host of specific limitations, controls and verifications of a bureaucratic nature are introduced. But this would hinder the development and expansion of those entrepreneurial forms that in the first instance one would like to favour and promote. In any case a specific automatic support would remain: as much as profit taxes apply to *distributed* profits, a non-profit organization by definition does not distribute profits, and the surplus it is able to create is not diminished by the tax on distributed profits. Thus its growth could be favoured by two circumstances: 1) profits are not distributed (even if the negative side of the coin of course is that this prevents them to be financed through equity); 2) profits are not subjected to the taxation on distributed profits, since no profit is distributed.

### ***11. Institutional Experiments and Transition***

Even if the basic institutional foundations of a system (presently the capitalist one) have turned out as winners in the systemic contest, one is still left with the issue of what 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 well undergo a gradual transformation in an opposite direction, whenever the conditions that have been discussed above for a successful transition towards non-capitalist forms of entrepreneurship are 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 and could be restricted initially to a part only of a country with a huge population and territory, 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.<sup>28</sup> 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.<sup>29</sup> But whenever the

---

<sup>28</sup> Cf. Roland, 2000, p. 57. The great advantage of territorially limited reform is that it can pay due attention to a set of interrelations that more difficultly could be managed in a national framework without introducing strong elements of irreversibility. In a limited territory the costs (non only economic, but political and social as well) associated to reform reversal are much lower than when the reform applies to the whole economy.

<sup>29</sup> Moreover, one should not downplay the relevance of the tradition of the autonomous role of the peasant village (cf. Krug, 2000a, p. 12). This tradition of autonomy has allowed the local communities 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 may be hidden, making of these enterprises masked forms of private or mixed

legitimation of the previous system collapses abruptly, in much more advanced economic contexts, gradual processes of transformation are much more difficult to sustain, 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).<sup>30</sup> 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.

### ***12. 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.

---

entrepreneurship, remedying, at the same time, for the institutional restrictions to a market for those capital goods whose ownership remains public (cf. Krug, 2000b; Oxford Analytica, 2001) and for the absence of adequate legal guarantees against the predatory tendencies of public authorities (cf. Sun, 2002, p. 252). One may refer to the latter source for describing and explaining the evolutionary trend of township-village enterprises towards the transformation into ownership structures where public participation is progressively lower.

<sup>30</sup> 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 a 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., Roland (2000), ch. 6, pp. 131-152.

**REFERENCES**

- Anderberg, Dan, Fredrik Andersson, Alessandro Balestrino, “Time, Self-Selection and User Charges for Public Goods”, *FinanzArchiv*, vol. 57 (2000), pp. 137-154.
- Atkinson, Antony, and John Micklewright, *Economic Transformation in Eastern Europe and the Distribution of Income*, Cambridge, Cambridge Un. Press, 1992
- Bergson, Abram, “Comparative Productivity: The USSR, Eastern Europe and the West”, *American Economic Review*, vol. 77, no. 3, (June 1987), pp. 342-357.
- Bergson, Abram, “Communist Economic Efficiency Revisited”, *American Economic Review*, Vol. 82 no. 2 (May 1992), pp. 27-31.
- Berliner, Joseph S., *The Economics of the Good Society*. Oxford: Basil Blackwell, 1999.
- Bowles, Samuel, “Endogenous Preferences: The Cultural Consequences of Markets and other Economic Institutions”, *Journal of Economic Literature*, vol. XXXVI (March 1998), pp. 75–111.
- Chilosi, Alberto, "Socialist and Communist Income Distribution in Marxian and Soviet Marxist Thought", *Il Politico*, 43 (1978), 4, pp. 698-710.
- Chilosi, Alberto, "Privatisation through Competition", *Jahrbuch der Wirtschaft Osteuropas*, vol. 14, n. 2, 1990a, pp. 182-184.
- Chilosi, Alberto, “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 1990b, pp. 389-403.
- Chilosi, Alberto, “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.
- Corneo, Giacomo, “Work and Television”, Iza Discussion Paper No. 376, October 2001, <http://papers.ssrn.com/abstract=287317>.
- Gordon, R. J. (2000), “Does the ‘New Economy’ Measure up to the Great Inventions of the Past?”, in *Journal of Economic Perspectives*, vol. 14, n. 4, pp. 49-74.

- Krug, Barbara, "Ties That Bind: The Emergence of Entrepreneurs in China", ERIM Report Series reference number ERS-2000-44-ORG, November 2000a, p. 12, <http://www.eur.nl/WebDOC/doc/erim/erimrs20001201150211.pdf>.
- Krug, Barbara, "The Interdependence Between Political and Economic Entrepreneurship". Erasmus Research Institute of Management, November 2000b. ERIM Report Series reference number ERS-2000-43-ORG, <http://www.eur.nl/WebDOC/doc/erim/erimrs20010209141037.pdf>.
- Marx, Karl, *Critique of the Gotha Programme* (1875), [www.archive\marx\works\1870\gotha\ch01.htm](http://www.archive.marx.works/1870/gotha/ch01.htm).
- Meggison, William and Jeffry Netter, "From State to Market: A Survey of Empirical Studies on Privatization", *Journal of Economic Literature*, vol. XXXIX (June 2001), pp. 321-389.
- Oxford Analytica, "Battered and Cherished: The Private Sector in China", *Transition Newsletter*, vol. 11, n. 6, January 2001, pp. 13-14
- Roland, Gérard, *Transition and Economics*. Cambridge (Mass.): MIT Press, 2000.
- Schumpeter, Joseph A., *Capitalism, Socialism and Democracy*. London: George Allen & Unwin, 1976 [1942].
- Shrcke, Marc, "Preferences for Inequality: East vs. West". Innocenti Working Papers, No. 89, October 2001
- Stiglitz, Joseph E., *Wither Socialism*. Cambridge (Mass.): MIT Press, 1994.
- Sun, Laixiang, "Fading out of Local Government Ownership: Recent Ownership Reform in China's Township and Village Enterprises", *Economic Systems*, vol. 26, 2002, n.3, pp. 249–269.