Efficiency vs. Equality and the Demise of Socialism

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One of my fellow graduate students at MIT had access to the Pentagon Papers at a time when they were still classified, and he was writing a dissertation on aspects of the American involvement in Vietnam. One morning over breakfast he discovered that he had been preempted by the New York Times. Every scholar recently working on the Soviet Union, China, and Eastern Europe must understand that student’s sensation that morning. By now, they must face newspapers with a mixture of hope and foreboding. Events outrun the most radical predictions. Not only has the Wall crumbled, with pieces of it being sold as souvenirs, but Albania has established telephone connections to the world not long after westerners came to believe Albania had been the only nation in modern times to succeed in disappearing.

Social scientists have been caught, often in press, with grievous misreadings of the events in Eastern Europe. Some of these social scientists had argued not merely that such events were unlikely, they had boldly asserted they were impossible. One of my colleagues says that 1989 shows that the discipline of comparative politics is intellectually destitute. But perhaps political philosophers have as much to learn from 1989 as do comparative political scientists.
In Democracy in America Tocqueville is concerned with the equality of condition that he thinks is "the fundamental fact from which all others seem to be derived." On Tocqueville's account this condition is intimately, causally connected with democracy. It was in their striving toward equality of condition — as in, for example, equality before the law — that the old regimes of Europe approached democracy in Tocqueville's time. In our own time, the egalitarian urge has more typically been intellectually associated with socialism, which has been associated in actual politics with non-democratic government. Indeed, the rhetoric of defenders of Soviet style political regimes has often suggested that authoritarian government by the Party was necessary to protect people against the ravages of democracy.

We may distinguish two urges in the current reorganizations of the eastern societies. The initial urge seems to have been Mikhail Gorbachev's — and, no doubt, other leaders' — concern to improve economic performance. The favored solution is to introduce some degree of capitalism to replace centralized economic control. The second urge is popular clamoring for political equality through democratic institutions, which supposedly fit the new economic order. The extraordinary events of 1989 are almost entirely from the second urge to create democratic institutions. Introducing capitalism may take far longer than introducing new, relatively democratic regimes.

What do these changes portend for political theory? They may raise doubts about the possibility of a political program of egalitarianism in incomes. This paper might be called, as a question, "Socialism without Socialists?" or "Egalitarianism without Socialists?" The fundamental issue for the short run of a generation or two is not whether there can be communism — there evidently cannot be for very long in a world dominated by economic competitiveness as we know it. The issue is whether there can even be socialism or a reasonable modicum of egalitarianism. It seems to be the conclusion of Soviet, Eastern European, and Chinese leaders that there cannot be socialism in competition with capitalism. There is a slogan popular in Poland today: Liberty, Equality, Initiative. That sounds like a minor variation on an old theme. It is not.

In the new slogan, 'Liberty' means freedom of enterprise. 'Equality' means equality of all forms of property. The new word in the slogan, 'Initiative,' is the only straightforward term. Its force, despite the rhetoric of equality of opportunity, is radically inequalitarian.

II Equality vs. Efficiency

The view that equality of income and efficiency of production inherently conflict has become almost a dogma in the West. In his theory of justice, John Rawls supposes that inequality can be just if the inequality leads to such greater production as to permit even the worst off in the society to be better off than they would be under a more egalitarian regime. This is a concession on his part to the seeming likelihood that economic incentives of greater wealth and income are necessary for stimulating higher levels of production. It might appear to be a staggering and conservative concession. But it is no more than a concession to the moral theorist's dictum: ought implies can. It cannot be true that we ought to do what is impossible for us to do. If the economist's dogma that greater productivity requires differential rewards as incentives is correct, then we cannot have greater productivity without at least Rawlsian inequality.

Until very recently the eastern bloc nations proclaimed a commitment to egalitarianism. And, although their practice did not meet their proclaimed aspiration, there was much greater equality of incomes among industrial, professional, and bureaucratic wage-earners in the East than in the West. A clear implication of the current capitulation to capitalism is the freeing of wages from central determination and the introduction of personal profits that must reduce equality of earnings. Leaders may talk as though the changes will hurt no one, that even if they increase inequality, they raise the floor for everyone. If this is true, their move is essentially Rawlsian. Against that sanguine view, consider just one minor group who, like many other groups, will not fit the new struc-

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2 Reported by Jacek Tarkowski in conversation, University of Chicago, 14 February 1990.


tures: vast numbers of teachers and professors of Marxism-Leninism surely wonder whether they will lose in the transition. The eastern nations provide some unique evidence for the equality vs. efficiency thesis. The evidence touted at the moment is their current economic difficulties. But this evidence is very unclear. In general, the eastern economies seem in recent years to lag behind some capitalist economies at similar levels of development in their rates of growth but they share this sad fate with most of the non-socialist economies of Latin America. In any case, the differences are not great. Indeed, the conservative American economist Herbert Stein concludes that the slight differences do not explain the capitation to capitalism. The differences might even have been transitory. While working on East Germany twenty years ago, I collected many West German books with such titles as The Shattering of the East German Economy, The Collapse of the East German Economy, The Disastrous Failure of the East German Five-Year Plan, and so forth. Every year through the ‘fifties and ‘sixties, new such books appeared, saying that, although the East Germans had got by up until then, they were bound to collapse soon. Throughout the period the East German economy marched along at roughly the same per capita rate of growth as in West Germany. Its per capita production lagged behind West Germany’s by about twenty-five percent from beginning to nearly the end. About a decade ago, it ranked as one of the most productive economies in the world, although its population was only about sixteen or seventeen million. Of course, East Germany had the advantage of subsidies from West Germany and de facto membership in the EEC, advantages not shared by other nations of the eastern bloc.

The debate over the presumed conflict between efficiency and equality in the West is generally about gross productivity, not really about efficiency in a narrower sense. It is about the role of unequal rewards in motivating people to work. The eastern economies have suffered from another problem of inefficiency: the failure to produce goods that are desired. Without greater inputs in production, consumer demands could have been better satisfied. This inefficiency results from centralized control and from the mismatch of incentives with what is produced.

The real evidence of conflict between equality of income and efficiency of production is less obvious. Note four kinds of evidence.

First, economic pressures allowed egalitarian commitments to be severely undercut for the past couple of decades in the form of letting citizens receive hard currency gifts from relatives in the West. A large fraction of East Germans received such supports in West German marks, which could be used to buy various goods and even access to apartments immediately without going through normal queues that could take as long as a decade. Many of the purchases were nominally illegal, but they were openly tolerated because of the need for hard currencies, without which nations lacking commodities for foreign sale cannot enjoy the benefits of world markets. Getting hard currencies benefited everyone, even though it benefited some more than others.

Second, the eastern nations have increasingly tolerated certain black markets over the decades, even legalizing some of them. Production of many agricultural goods for domestic consumption has been turned over to farmers working on their own plots while earning much of their staple income from wage labor on their collective farms. Farmers who are good at their private production are well rewarded at de facto market prices for their efforts. Throughout industry in the eastern bloc there are arbitrage agents who, for bribes, facilitate trade in inputs for production. Some of these activities are presumably parasitic on the system, as they often are in democratic, capitalist societies. But some of them seem to be genuinely facilitative. The bribes are unequal rewards that give managers and others incentive to put extra effort into making things work better.

Third, in the years before the Wall, East Germany suffered substantial losses of workers to emigration, almost all of it to West Germany. The emigration was not random but was strongly correlated with occupation and potential earnings differences east and west. There was a reverse flow of about thirty percent of the westward movement. The net movement was highly skilled and professional workers going west, low-skill workers going east. Chile under Allende reputedly suffered a similar experi-

5 Many scientists must also lose, because Eastern European research departments are overstaffed by competitive western standards (Science [6 April 1990], 23).


7 Its gross rate of growth was significantly lower because its population declined slightly over the years as a result of net out-migration that offset the modest natural increase. The West German population grew from net in-migration and natural increase, and its workforce grew through the recruitment of foreign ‘guest workers.’

8 The argument is not about what goods are produced, although higher incomes for some may generally imply demands for different goods. For example, high-income earners in the West commonly buy luxury cars, very expensive dinners, international travel, and vacation homes, which are seldom bought by low- or even moderate-income earners. Hence, unequal rewards are likely to affect the pattern of production.
ence of top-heavy emigration, although the data are subjective because no one had an interest in collecting them for Chile. Similar, less dramatic experiences have afflicted the entire eastern bloc. This problem suggests that egalitarianism faces special obstacles in a larger world in which inequitable incentives and rewards prevail. Alternative rewards may induce adverse exit, as Albert Hirschman argues.

For the fourth piece of evidence return to the failings of the past decade or two. For all we know, the problems of the moment in the socialist economies would pass and those economies would begin to show substantial rates of growth and technological and organizational innovativeness. The usual western view is that innovativeness depends heavily on entrepreneurial incentive and, therefore, on some variant of capitalist ownership. That may be true, especially in new technologies, such as electronics and computing in our era. But it seems also to be true that very large organizations, such as Dupont and Toyota, are superb innovators who lead, rather than follow, economic change. What the eastern economies face at the moment, however, seems to be difficulty in making the major transition from follower to leader economies just when the latter seem to have enormous advantages for growth and international domination through the subordination of all activities to the information technologies.

Leader economies did not so clearly have such advantages twenty or thirty years ago. Lacking the leadership to make a transition from the top, the eastern nations are on the verge of trying to make it by decentralizing economic control and even creating capitalist incentives. But, had there been no capitalist world markets or if these had been less successful, the socialist nations would not have incentive now to reconsider their own organization. In the ‘thirties, the prospects for capitalism seemed poor enough to lead to popular support for fascist reorganization of societies. Stein notes that his lecture, mentioned above, on comparative economic trends in eastern and western economies was given two weeks before the ‘sixtieth anniversary of the onset of capitalism’s greatest crisis.” He quotes a German economist, Moritz J. Bonn, writing in 1932:

[The] question arises in thousands of hearts and brains: Is the capitalist system any longer justified if, in the richest country in the world, it is incapable of shaping an order which will guarantee to a comparatively sparse population, admittedly industrious and capable, a subsistence consonant with the human needs developed

by modern techniques, without millions being from time to time reduced to beggary and to dependence on soup kitchens and casual wards?

The real significance of the American crisis consists in the fact that today it is not merely the present economic leadership or economic policy that is being questioned, but the capitalist system itself.11

It sounds familiar. Now socialism seems to have poor economic prospects and the system itself is being questioned although its economic problems are far less grim than what capitalism suffered in the ‘thirties. It may often be true of judgments such as Bonn’s 1932 judgment that they are merely transitional, not fundamental. Still, it may be that the transition from uncompetitive to competitive socialist economies would be so hard as to result in economic collapse in the short run, so that, even if the challenges were only momentary and not fundamental, making a transition instead to capitalism would still be the intelligent policy for the moment.

Oddly, the main problem may be the simple one of ossification of organizations that have strong personnel protection policies when they come to face changing technologies. Featherbedding or its analog becomes an obstacle to change. In a free market economy, the response to ossification of old enterprises may be displacement by other firms or even industries that utilize new, more productive technologies and perhaps differently trained workers. Among the most effective forms of differential incentives not available in the East are bankruptcy and unemployment. In a centrally controlled economy, displacement of an ossified industry or firm requires decisive action by someone, not merely the brazen actions of a couple of smart-ass teenagers working in their garage to compete with gigantic IBM.

Oskar Lange, John Roemer, and others have argued that socialist firms can be competitive, just as Dupont and Toyota are. They merely need not to be monopolies and to face real competition. In what was essentially an antitrust move, the Polish government recently voted to crack monopolistic control of the distribution and sale of food by prohibiting cooperatives from associating into larger, controlling units. They did not create a new, alternative system of distribution to compete with the present cooperatives, which have been transmuted into capital-stock firms and which may continue to collude in monopolizing distribution. Perhaps a society run by edict can become a society in which law can


10 Stein, ‘The Triumph of the Adaptive Society,’ 1

effect changed relationships, so that the monopoly of the former cooperatives can finally be broken.

But the general point of creating private property is to give opportunity to entrepreneurs. It is entrepreneurial creativity that is fundamentally important, not property. In genuinely competitive markets — that is, markets with many sellers and many buyers — creating property may be sufficient to let entrepreneurial talent and initiative bring about much greater productivity, as has happened with vegetable farming on quasi private plots in the Soviet Union and East Europe. But there are few genuinely competitive markets in this sense — the only ones of any significance may be vegetable farming, restaurants, and a few services. These make up a very small part of national economies in industrial states and they are not central to the problems of eastern bloc economies in their misfit with international markets. Creating property without entrepreneurs in other industries by simply turning firms over to the current bureaucrats who manage them cannot change much in the short run and may even hinder developments in the longer run by tying up capital in sick firms.

III Egalitarianism in One Society

Return to the third problem, noted above, of inefficiency in the eastern nations under communism. Imagine two neighboring nations that are similar in many relevant respects. They have similar populations, levels of economic development, education, and gross domestic product per capita. But East is a nation with relatively egalitarian incomes and wealth while West is a free-wheeling market economy with unequal incomes and wealth. Successful entrepreneurs in West may amass fortunes such as those of Bill Gates (about five billion dollars from his computer software firm, Microsoft) or Sam Walton (an even greater fortune from his retail discount chain, Wal-Mart) in their own lifetimes. Suppose the unequal incomes and wealth in West are produced by market forces and that there are characteristics of individuals that put them well above or well below the median income and that individuals tend to know whether they have these characteristics, if not at the beginning of their working lives, then soon enough.

The equality in East could come about through various devices. East could have socialist ownership of production (reducing the possibilities for entrepreneurially based inequality) and of distribution. Or it might not be socialist at all but might let the market generally determine what gets produced and consumed (perhaps subject to some regulatory constraints). To achieve greater equality, it might merely have an incomes policy, effected through progressive taxation on incomes and stiff taxes on wealth.

Suppose East and West do not suppress migration between them, so that they have essentially a joint job market. We can expect that there will be a steady stream of those with the characteristics for high incomes from egalitarian East to inegalitarian West, and a steady stream of those with the characteristics for low incomes from inegalitarian West to egalitarian East. During the years (1949-1961) of massive migrations between East and West Germany before the Wall was built there was a marked selectivity, with less-skilled workers migrating in large numbers to the east and highly skilled workers, professionals, the well-educated, and perhaps likely entrepreneurs migrating in even larger numbers to the west. If it is generally true that high incomes tend to go to more productive and low incomes to less productive individuals, these migration flows would work systematically to the advantage of West and the disadvantage of East. The result would be slightly higher total productivity growth in the inegalitarian society, which would lead to grossly higher productivity after a generation or so. As a result, one would expect economic prospects in the egalitarian society to deteriorate in comparison with those in the inegalitarian society. After a long enough period of such deterioration, one might even expect that the median welfare in the egalitarian society would fall well below the median welfare in the inegalitarian society. Political liberty of movement may therefore destroy an egalitarian society.

In a world of non-egalitarian societies, egalitarianism is not self-enforcing unless people are normatively in favor of it. If people are predominately or even largely self-interested, egalitarianism in a competitive world with inegalitarian alternatives may require substantial, ongoing intervention to enforce it. Such intervention is likely to be costly and therefore to reduce productivity. Hence, there is likely to be a contingent connection between egalitarianism and autocracy. A nation may successfully achieve modest egalitarianism with democratic, politically liberal devices, as Sweden seems to do. But if popular approval fails, the outside world competes too strongly, or the move to equality goes too far, even a Sweden may face decline.

This is, of course, not merely a theoretical conclusion. Its truth depends on empirical relations, such as the claim that market inequalities correlate with productivity. Many social scientists and others seem to

12 Viktoria Mullova, Dmitri Rostopovich, and many others may have emigrated to the west to secure greater artistic freedom, but they may also have been motivated to emigrate to where their talent would be far better paid.
believe this claim. Unfortunately, the claim masks a conceptual problem: productivity and incomes are circularly related. For many things that matter to us, we can compare productivity levels in different societies if what they produce is similar enough in kind and different primarily in quantity. If very much is simply provided by the state without market measures of demand, we may have difficulty evaluating those things in comparison to other things and we may succumb to the fallacy of measuring them by the inputs to them rather than by the unpriced outputs. In the end, even the very careful comparisons of East and West German productivity grew increasingly tenuous as consumption patterns in the two societies diverged. Converting from one to the other economic organization would make the converted economy look bad by comparison.

In our imagined pair of nations, does East trade productivity for equality? If there are real costs of resources or lost opportunities for production that result from enforcing egalitarian distribution, then yes. East also loses productivity in its labor-force competition with West. This loss is not inherent in East’s egalitarian system per se because it depends on the existence of a West. But it may make East’s egalitarianism untenable in our world.

IV Egalitarianism Without Socialism

Concerns with efficiency and productivity seem to have destroyed socialism in the East. Does egalitarianism still have a voice in the world? During the rapid process of the absorption of East by West Germany, the West German novelist Günter Grass regularly appeared on television to bemoan what was being lost. Ian Buruma writes:

His constant invocation of “Auschwitz” as a kind of talisman to ward off a reunited Germany had the air of desperation, the desperation of a man who had lost his vision of Eden. His Eden was not the former GDR (German Democratic Republic), to be sure, but at least the GDR carried, for Grass, the promise of a better Germany, a truly socialist Germany, a Germany without greed, Hollywood, and ever-lurking fascism.13

There may be other ways to pin one’s aspirations to an egalitarian political program than by reference to an ideal corrupted in practice. But the desperation that Buruma read into Grass’s complaints may be real and understandable.

In western usage, ‘socialism’ and ‘communism’ are distinctly different in the vernacular language of ordinary politics. ‘Communism’ is a denotive term that refers to the immediate past systems of the eastern bloc, to Soviet-type economies and polities. ‘Socialism’ is a plausible political goal under systems quite different from those of the eastern bloc. It is not quite utopian but it is more ideal than real, at least up to present experience. In eastern usage, ‘communism’ was always only a utopian aspiration at best. In the East, ‘socialism’ is the reified term, the ‘communism’ of western vocabulary, and it has been tarred by its association with the immediate past systems. Rejection of those systems makes invocation of the term ‘socialism’ politically unacceptable, as though ‘socialism’ as a term had been fully appropriated by the Ceausescus and the Honeckers.

Even in the West, socialism may lose its appeal by association with the eastern judgment. As the eastern societies have associated socialism with political repression and autocracy, so they seem to associate capitalism with political freedom and democracy. Both associations may be causally correct, although we have no compelling theory of why they must be, and they might only be denotive. Many in the West share the association of capitalism with freedom and democracy and western opponents of socialism have long touted the association of socialism with repression and autocracy as a causal law.14 Oddly, these opponents of egalitarian policies may now draw on eastern arguments to support their position.

Without socialism as an aspiration, it is hard to frame an agenda for egalitarianism. The English Levellers at the time of Hobbes and the Radical utilitarians at the time of Bentham and the elder Mill rallied for equality but they were unable to found lasting movements at all comparable to the political and intellectually powerful socialist movement of the past century or more. For the near term, it seems likely that support for more nearly egalitarian incomes policies will depend very heavily on the benevolence of many who will not benefit from such policies. Recent evidence in many western nations is that even such


14 For enlightening discussion of these associations, see Charles E. Lindblom, Politics and Markets (New York: Basic Books 1977). Several of the articles in the special issue of Social Philosophy and Policy on ‘Socialism’ (Spring 1989) are of interest on this issue, although, despite their recent publication, they are already dated by events — an unusual fate for philosophical work.
benevolent motivations are in decline as tax policies have become less progressive while welfare programs havegone into decline.

On many reports there remains a strong commitment to economic egalitarianism in many eastern nations. Indeed, my history colleague Friedrich Katz thinks the acrimony against East German leaders' secret privileges was so intense just because Honecker and his associates betrayed a commitment to egalitarianism that was shared by the populace. But despite such sentiment, there may remain no political party for egalitarianism. Can peoples aspire to greater equality without socialism as a party and a possible form of political economy?

Democratic politics seems to have certain egalitarian tendencies. It may not do very well at equalizing wealth, income, or even benefits provided by government. But it may push for uniformity in many rights assignments. In the United States, for example, it has become difficult for government agencies to sponsor social and medical experiments that assign subjects to different treatment groups. Various theories of the impact of welfare programs on incentives to work could be tested by trying different welfare regimes on selected populations. Congress has become hostile to such experimental tests not so much because they are experiments or because certain members of Congress think it obvious which theory or program is right but, rather, because many people think it unfair, for example, to apply differential work incentives to people who are otherwise similarly situated. Similarly, tests of new drugs for treatment of AIDS have been blocked before they could reach statistically sound results on the grounds that it is unfair to give people different life chances. But these correlates of democracy are minor instances of equality. Historically, the propertied class has worried about the equalizing tendency of democratic government. In the modern experience of democracy coupled with great inequality of wealth and income, that issue has virtually dropped from concern.

V Concluding Remarks

It is a striking fact of the growth of economies and polities historically that none has really faced the task of the East Europeans at this moment. In East Europe, the task of creating democracy and making it work is being undertaken simultaneously with the task of creating a market, perhaps capitalist, economy. Although some democratic tendencies preceded much of the development of major western economies, broadband democratic participation and institutions have invariably followed the growth of market elements of the economy. The events of 1989 seem to have produced instant democracies in many East European nations. It is now up to these newly democratic regimes to create the new economic order. Can they do it? Can a government that needs majoritarian support afford to shut down virtually whole industries, temporarily reducing economic production while causing substantial unemployment? During the Great Depression, the complaint against President Hoover was not that he deliberately brought it about for some reason but merely that he failed to stop it sooner. If they choose to switch to capitalist organization of their economies, Vaclav Havel and Lech Walesa may face the accusation that they have brought about a similar transitional disaster that ruins lives for a decade. The hesitations of Gorbachev may therefore rightly be shared by all the Eastern European leaders.

It is a discouraging thought, but an arguably plausible one, that China may follow its own events of 1989 with greater success in making the transition to market economies with democracy than most of the East European nations are likely to have. Autocratic development of a market economic regime may be easier than democratic development of it. Of course, there may be much greater variance along the autocratic path, with nations following something like the South Korean example or, alternatively, the Romanian. But democracy may have much better hope of survival and success if it follows successful economic change than if it has to stimulate and manage the change. That must be a discouraging prospect for anyone who is committed to the priority of liberty.15

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