

INSTITUTIONAL ECONOMICS





NEW

SZÉCHENYI PLAN

INSTITUTIONAL ECONOMICS

Sponsored by a Grant TÁMOP-4.1.2-08/2/A/KMR-2009-0041

Course Material Developed by Department of Economics,

Faculty of Social Sciences, Eötvös Loránd University Budapest (ELTE)

Department of Economics, Eötvös Loránd University Budapest

Institute of Economics, Hungarian Academy of Sciences

Balassi Kiadó, Budapest



The project is supported
by the European Union.

National Development Agency
www.ujszechenyiterv.gov.hu
06 40 638 638



HUNGARY'S RENEWAL



The projects have been supported
by the European Union.

ELTE Faculty of Social Sciences, Department of Economics

INSTITUTIONAL ECONOMICS

Author: János Mátyás Kovács

Supervised by János Mátyás Kovács

June 2011

INSTITUTIONAL ECONOMICS

Week 11

Reception of institutional economics in Eastern Europe I

Institutional thought before reform economics

János Mátyás Kovács

Contents

- *A kind of institutionalism*
- Normative institutionalism
- Mythical institutionalism
- Theoretical opportunities of the reformers
- An unexploited opportunity

A kind of institutionalism

- Reception of NIE: habitual delay; yet it was not fatal: Eastern European economists were, almost instinctively, searching for patterns of institutional theory during the past decades; instinctively because at least since the middle of the 19th century they have been working in the framework of various institutional traditions.
- They remain prisoners of OIE, choose the new strands of institutionalism rather late and sporadically; this contradicts reasonable expectations (see next presentation).
- Reasons for the delay: (until 1989) communist censorship? Constraints due to reform-making? Lack of Western scientific contacts?

A kind of institutionalism (cont.)

- Power of traditions: German/Austrian roots of economic thought in the region; socialist/Marxist/communist indoctrination; meanwhile, the region missed the standardization of neoclassical theory
- We have already spoken of the German/Austrian connection; let us look at real socialism: *a kind of institutional economics* was cultivated there (although the authors did not always know that).
- Following 1917, a Marxist economist was doomed to become a constructivist (to quote Hayek) in the Soviet Union; he/she dismantled and built up institutions in large numbers, rejected the idea of evolution, helped liquidate private property, money, markets, designed hierarchies, advocated Big Government, militarization, politicization of the economy, etc.

Normative institutionalism

- He/she received OIE in its Marxian, German historicist and utopian versions (the Austrian version was rejected as too individualist/liberal: Buharin versus Böhm-Bawerk)
- OIE was radicalized by the Bolsheviks to support war economy (economy in kind)
- War Communism is a real innovation in Marxist theory that advocated self-government, decentralization, communal ownership, etc.
- Its inventors and administrators (Lenin, Bukharin, Preobrazhensky, Larin, Kritsman, Trotsky, etc) were importing and planning economic institutions at all levels of the economy for more than three years (1918–21) in some sort of normative zeal; this was genuine social engineering.
- Description and analysis came only after the dysfunctional character of these institutions had become clear.

Normative institutionalism (cont.)

- "Normative institutionalism" (let us call it this way) turns into a critique of the new institutions but the concepts used in the critique also stem from Marxist theory (law of value, *khozraschet*, primitive accumulation of capital, equal exchange, material interests, sectoral balance, etc).
- Nonetheless, part of these concepts can be interpreted in a less collectivist manner: this is what the Russian "bourgeois" (Menshevik and Neo-Narodnik) economists tried to do (Groman, Bazarov, Feldman, Chayanov, Kondratieff, etc) .
- With the critique, a stop-go reform cycle starts: reform projects – loosening up the communist institutions – political reaction – back to rigidity – dysfunctional institutions – new wave of reforms.
- Whether it comes to war communism, NEP, Stalinist planning, post-Stalinist reforms or any subtype of these (e.g., New Economic Mechanism), the institutional projects that animate the reform cycle; even the political games are played in an institutionalist language.

Normative institutionalism (cont.)

- In the course of the 1920s: numerous ideas of institution-building; however, no synthetic works like those of Weber, Sombart, Veblen or Commons (aborted attempts: e.g., Preobrazhensky's "New Economics")
- Yet, the NEP is a (brief) experiment to set up a mixed economy with public and private as well as planned and market institutions: lack of scholarly blueprints
- Axiomatic view: institutions are transitory; soon they will turn into technical organizations.

Mythical institutionalism

- Communism will not have an institutional political economy because political economy as such will cease to exist (a heated debate about the end of economic science in 1925)
- Instead of political economy, a kind of technical discipline will arise ("economic technique", "social technique")
- No one will write "*Das Sozial*" that would be equal to Marx's *Das Kapital*: analysis will be replaced by description
- The outcome of this in the 1930s:
 - Politics-driven subscientific economic works
 - Falling behind the West
 - From utopias to utopias (Engels' promise: from utopia to science)
 - Proud isolation
- End result: a kind of institutionalist mutant: let us call it "mythical institutionalism".

Mythical institutionalism (cont.)

- The most comprehensive example: 1954 textbook of political economy of socialism
 - Notion of system: artificial comparison with capitalism
 - Statist concept of the institutional system: centralization, homogenization, naturalization; yet, the party-state is no subject of inquiry
 - Objective laws: “planned-proportional development“, “work-based distribution“, etc; hierarchy of laws; at the same time, some degree of “commodity – money relations“ is also postulated; a variety of ownership forms?
 - No new institutions are suggested but the existing ones are justified (normative versus apologetic approach) by means of the myths of Soviet-type communism: magic, religion, superstition, irrationalism; coding/packaging rational decisions

Theoretical opportunities of the reformers

- The pride conceals a basic failure: a communist economy that erases private property but remains efficient (without operating markets) does not come into being
- Naive expectations (Lenin and the postmaster/cook who will be able to guide the national economy);
transparency, end of alienation

Theoretical opportunities of the reformers (cont.)

- In principle there was a chance for cultivating institutional economics:
 - The Soviet economists faced a quasi-centralized/militarized state economy.
 - Scarcity did not disappear, choices were to be made, economic calculation was unavoidable.
 - Markets reappeared everywhere even within the state sector.
 - Private property became the “private“ property of the party-state.
 - Dictatorship over needs, indoctrination, mobilization, terror.
- All these represent challenging institutional problems.

Theoretical opportunities of the reformers (cont.)

- What could those do who recognized these problems (and have not been arrested, exiled, killed yet)? Double-speak, coding, etc.
- Winning strategy: instead of markets, he/she has to talk about the law of value or socialist commodity production, instead of equilibrium, about proportionality, instead of competition, about independence of firms, etc.
- Those who think that forced industrialization and the impoverishment of agriculture (cf. the “Stalin revolution“) with all its planning in kind, campaigns, etc bring chaos, have to suggest the “introduction“ of the law of value, scientific planning, improving the economic mechanism and refer to concepts featuring in the official discourse (interests, incentives, coordination, etc).

Theoretical opportunities of the reformers (cont.)

- Nonetheless, no political economy of the transition period emerged for a long time
 - Long break (1927/28 --1953/54): Stalin's three unsuccessful attempts to establish the discipline (1936, 1943, 1951)
 - Why Stalin? How does he join the reformers? Mobilization or consolidation? Oligarchic fights in an allegedly totalitarian system, which push and pull scientific projects.
 - At the same time: linking political economy to economic reform (i.e., to agricultural development, small private enterprise, markets, shadow economy, etc) may result in some improvement of scientific performance, including the development of institutional thought.

An unexploited opportunity

- The key question of SCD (“is the communist economy feasible at all?”) does not bother anyone in the Soviet Union of the 1920s (exception: Brutskus); instead: seeking alternative ways of transition to communism or trying to defend the mixed economy
- The Bolshevik economists construe models of reproduction (Preobrazhensky: unequal exchange, preliminary socialist accumulation), write about shortage of goods (Novozhilov), analyse monetary issues (Shanin, Sokolnikov), agrarian markets (Bukharin); the quality of their research programs are rather low.
- The “bourgeois” experts work on the academic level of their contemporaries in the West: Feldman, Groman, Bazarov (growth theory), Kondratieff (theory of business cycles), Leontief (input-output models) – without strong institutionalist conclusions (it is only Chayanov who takes part in SCD).

An unexploited opportunity (cont.)

- Mythical institutionalism is canonized by the 1954 textbook; simultaneously, the mythical approach switches to a “speculative” one (see later), without digesting the “Austrian” lessons of SCD about institutions, information, knowledge and the market process.
- Most reformers do not join the third wave of SCD, and raise the question of feasibility; will not be enchanted by computopia.
- Instead of that dead-end street, he/she opts for a longer impasse that lasts up until 1989 or even longer.
- Reformist institutionalism will gain in realism but remain speculative (Kornai’s twisted road from “Overcentralization“, through “Anti-equilibrium” to “Shortage”).

An unexploited opportunity (cont.)

- Computopia: there had been numerous chances before for engaging in institutionalist research programs, which were unfortunately missed; this very opportunity also remained unemployed – fortunately so.
 - The second wave of SCD opened, through the Lange model, a window of opportunity; linear programming and the computer were still missing; East-West cooperation in input-output analysis (Leontief); end of 1950s, beginning of 1960s.
 - The illusion of optimal planning (planometrics, computopia) results in a small analytical revolution (optimal choice, mathematization, macro-economic view); experimenting in an ideal macro-world while disregarding Austrian criticisms; instead: non-institutional solutions.

An unexploited opportunity (cont.)

- Basic conviction: the economy of real socialism can be made optimal.
- Original “Eastern“ discoveries (Kantorovich, Kornai–Lipták); two-level planning, game theory?
- Huge attraction: a scientific project tolerated by Soviet ideology (Nemchinov, Novozhilov, Fedorenko, Petrakov, Shatalin, stb) and being popular in the West (convergence?); doing economics with some Marxian flavor (reproduction models, Bródy) but without official political economy
- Radical (institutionalist-minded) reformers: aversion without open debate

An unexploited opportunity (cont.)

- Misfortune of computopia: it has to be tried whether it works; more and more concessions, ambiguous results, vast disappointment; the Hayekian arguments are verified (the models do not work because of a lack/distortion of information, plan bargaining, political versus economic preferences, etc).
- Out of the dead-end street: returning to the institutionalist research program left behind in the 1950s (and the rehabilitation of the micro-perspective).
- Insisting on the verbalist tradition (advantages of ignorance in mathematics); however, one might leave computopia through the concept of decentralized/indirect planning as well (Nemchinov/Novozhilov and hozraschet).
- For instance, Kornai was able to reach a higher level of institutional analysis in the economics of shortage.
- There appeared a new research program, too, which focused on institutions in the form of quasi-anthropological case studies.

An unexploited opportunity (cont.)

- The failure of computopia has an adverse consequence: it reassured the would-be institutionalists that High Theory is not unavoidable (a few liberal catchwords and local knowledge is enough); or we develop our own High Theory (Kornai's ambiguities with general equilibrium theory).
- What remains from computopia? Hardly any practical programs on how to improve planning in institutional terms; yet, a formal/mathematical culture develops, which will be crucial in taking over modern micro- and macroeconomics in the late 1980s.
- In the West the key questions of computopia continue to interest the scholars (mechanism design, Hurwicz, see presentation No 8).

Readings

Mandatory

- Bukharin and Preobrazhenky: ABC of Communism, 1918
The Political Economy of Socialism (textbook), 1954 (chapters)
Kornai: The Socialist System, 1992 (chapters)
Wagener (ed): Economic Thought in Communist and Post-Communist Europe, 1998 (chapters)

Additional

- Kornai: Anti-equilibrium, 1971 (chapters)
Brus: A szocialista gazdaság működésének általános problémái, 1967 (chapters)
Nove: The Economics of Feasible Socialism, 1983 (chapters)
Sutela: Socialism, Planning and Optimality, Helsinki 1984 (chapters)
Vanek: The General Theory of Labor-Managed Market Economies, 1970 (chapters)
Wiles: Economic Institutions Compared, 1977 (chapters)

Annex

- Biographical sketches
 - Bukharin
 - Kantorovich
 - Leontief
- Final questions
 - Predecessors/successors of the school
 - Friends and foes
 - Discoveries
 - Changes in the research program