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4. Ownership, Controllability, and Equality in a Socialist Economy: Analytical Frameworks and Some Observations on Hungarian Economy

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1. Introduction

The main purpose of this paper is to draw, from recent Hungarian economic reforms, implications for the future development of both socialist and capitalist economies. From the perspective of convergence theory, the differences between the two systems seem to be quite large. But Hungary, now entering in the 1980s the second stage of its structural economic reforms, offers lessons for future socialist systems. I believe these dynamics resemble structural changes occurring also in the capitalist world. Therefore, our task here will be to examine common properties of the dynamics of contemporary economic systems and to indicate trends for future development of national economies.

In this context, the methodological approach of convergence theory requires reexamination. Recently M. Ellman, as well as A. W. Coats and S. Thompstone, conducted discussions in the *Cambridge Journal of Economics*.¹ In a lecture presented at Hosei University in Tokyo, J. Kornai examined some typical approaches to the convergence problem.² His contributions will be clarified with a view to furnishing preliminary introduction.

Kornai's contributions to the theory can be summarized in three points. First, he indicates various patterns of convergence between capitalist and socialist economies by the criteria of relative tendency, converging point, smoothness of the process, and whether the movement of the two economic systems is monotonous or oscillating. In terms of these four criteria, which system comes nearest to the other system? Do the two systems meet at the end or halfway? Is this process smooth and continuous? Is the whole movement monotonous or oscillating? By applying these criteria all possible patterns, including van den Doel's partial convergence, can be described.

Second, Kornai emphasizes the multi-dimensional comparison of the two systems. Compared to the usual formulation of convergence by the share between planning and market, his comparison employed five indicators: proportions of the form of owner-

1 M. Ellman, "Against Convergence," *Cambridge Journal of Economics* No. 4 (1980): 199-210; A. W. Coats and S. Thompstone, "Against 'Against Convergence,'" *Cambridge Journal of Economics* No. 5 (1981): 383-386.

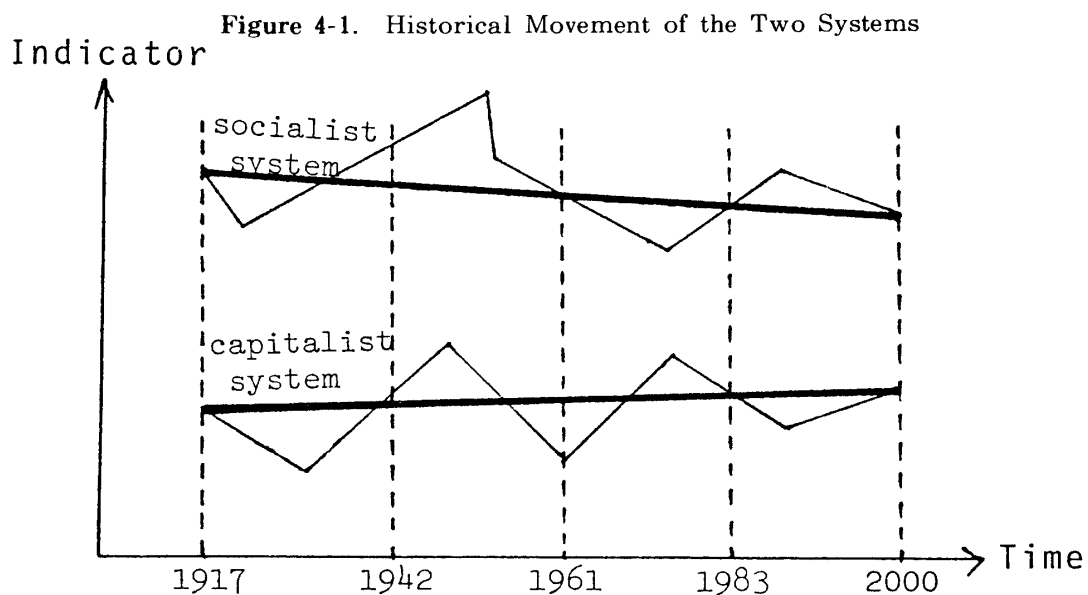
2 J. Kornai, "Convergence—Theory and Historical Reality: Twenty-One Years after Tinbergen's Article," *Shakai Rodo Kenkyu* (Tokyo: Hosei University) 30 No. 1/2 (1983).

ship, concentration of political power, planning level, allocating form of goods (bureaucratic or market allocation), and size of redistribution. He asserts that, whereas in terms of these five indicators the socialist system has been unchanged for the past twenty-one years, the capitalist system has been slowly approaching socialism with respect to the increase of state ownership, bureaucratic intervention, and redistribution. But it has been diverging in terms of political concentration, while remaining unchanged in the level of planning. According to Kornai's cautious approach, the tendency to converge is open to question, though it may be asserted at least that the conventional convergence theory exaggerates this tendency.

Third, Kornai avoids the usual "Planning vs. Market" approach, a one-dimensional formulation which he regards as wrong. He thinks the functions of markets should be contrasted with the vertical allocating functions of bureaucracies. Planning mainly concerns middle- and long-term economic administration, whereas vertical allocating functions have to do with daily allocation of goods and services. This suggests that, in the comparative analysis of economic systems, the distinction between horizontal market and vertical bureaucratic allocation is essential. In order to achieve a more comprehensive and precise comparison of the two systems, various functions of planning should be reexamined.

My intention here is not to participate in the convergence debate, but rather to raise some questions concerning the standard approaches to examining the convergence tendency. Three observations can now be made of the inherent limitations of previous approaches, including Kornai's.

First, despite Kornai's correct analysis of converging patterns, more attention should be paid to the time span of converging or diverging processes. He carefully chooses twenty-one years for corroborating historical processes. Nevertheless, as long as the issue concerns the long-term trend of historical change, there is a need to distinguish clearly short-, middle- and long-term changes in the historical process. Ten or twenty years should be regarded as the historical short-term. With some



combination of converging patterns articulated by Kornai, the real historical process would be, roughly, as described in Figure 4-1.

For example, during the period of NEP in the Soviet Union, the socialist system came close to the capitalist one. But in wartime the capitalist system came close to the socialist one. Some converging tendency may be seen in the early 1960s, when Tinbergen wrote his convergence article. At present we again seem to encounter movements of divergence.

Certainly political and economic policies in each period might be cited as plausible grounds for these fluctuations. But the real tendency behind these changes can be explained only by more deeply-rooted structural changes of national economies whose fundamental functions are historically restricted by contemporary environments. In any case, short-term fluctuations should be distinguished from middle- and long-term tendencies.

My second point, related to the first, is that a synchronic rather than diachronic comparison should be employed for short-term analyses. Synchronic comparison means an analysis of common relationships essential to contemporary environments in both systems. Only after this comparison, by synthesizing these approaches, can we say how profoundly the social forms of each system influence these relationships.

The illustration below shows the two contrasting approaches. The traditional approach usually examines only the degree of economic centralization, defined by state ownership on the time horizon. But the really crucial issue, apart from the exploitation problem, is not the degree of centralization per se, but its effectiveness in controlling the national economy. Therefore, the correlation between state ownership and the efficiency of the national economy should be carefully examined in order to clarify the contemporary common characteristics of both systems.

Turning next to Figure 4-3, we see one example of a synchronic approach. Despite the roughness of the description, one can see that the increase in state ownership contributes to some improvement in economic efficiency, first increasingly and then digressively. Beyond some point a further increase results in reducing the efficiency of the national economy; this is the case of over-centralization. This

Figure 4-2. Diachronic Approach

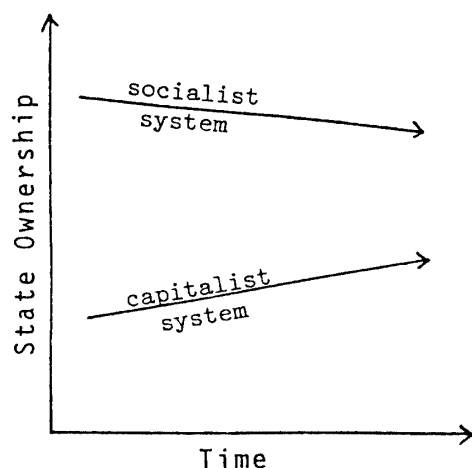
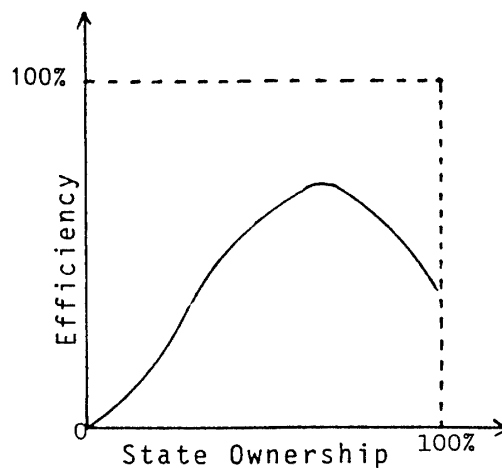


Figure 4-3. Synchronic Approach



kind of relation can be described at a given level of technological and social development in each country and economic system.

Third, diachronic multi-dimensional comparison³ by itself does not yield an integrated method for judging historical tendencies, not just because partial order is typical to vector comparison, but because it lacks key criteria for the judgment. Here also a synchronic approach would be desirable. Therefore, an alternative approach to the convergence problem should be some synchronic multi-correlation analysis for key variables which explain essential characteristics of contemporary national economies. Although various selections of key variables or concepts can be considered, I selected six key-concepts for describing the synchronic multi-correlation. These are ownership, market, efficiency, controllability, equality, and philanthropism. The first two are institutional concepts of economic systems; the next two concern criteria for fulfillment of economic activity and administration, while the final two are important ethical principles in modern societies. Of course, another set of concepts can be employed, but in the remaining part of this paper I have chosen to analyze synchronic relationships in terms of these six concepts.

The next part of this paper introduces theoretical frameworks for synchronic analysis and draws out important correlations between key-concepts. Along with the analysis new terminologies will be introduced for describing typical relationships within economic systems. The third part examines theoretical frameworks utilizing actual relationships in the Hungarian economy. The final part reveals the author's subjective anticipations.

2. Alternative Analysis of Comparative Economic Systems

A. Three-Dimensional Approach

Let us begin by grouping our six concepts into three conceptual groups describing the institutional system, ethical principle, and activity level. Figure 4-4 represents the relationship between these groups. There may be more appropriate selections of key-concepts, and it is also possible to make higher degree dimensional relationships. The task here, however, is not to count out exhaustively all possible conceptual sets, but to present one prototype describing and measuring the working of economic systems.

Figure 4-4 requires explanation. Each axis of a conceptual group measures the scale of property in question. For example, if we take state ownership on the institutional system axis, the scale measures the degree of state ownership, i.e. the weight of state ownership in proportion to all forms of ownership. The scale is simplified so as to measure the proportions of state ownership and private ownership. When we take market on the institutional system axis, the scale measures the weight of market allocation of goods and services. The complementary counterpart to market is not planning, but ordered allocation of goods and services.⁴ Thus, the scale

³ I agree with Kornai that various indicators should be examined. All five indicators mentioned by Kornai are equally important. My comments here concern only the methodology of comparison, though I think the political concentration indicator should be replaced by an indicator of the degree of political tolerance in a society.

Figure 4-4. Three-Dimensional Relationship

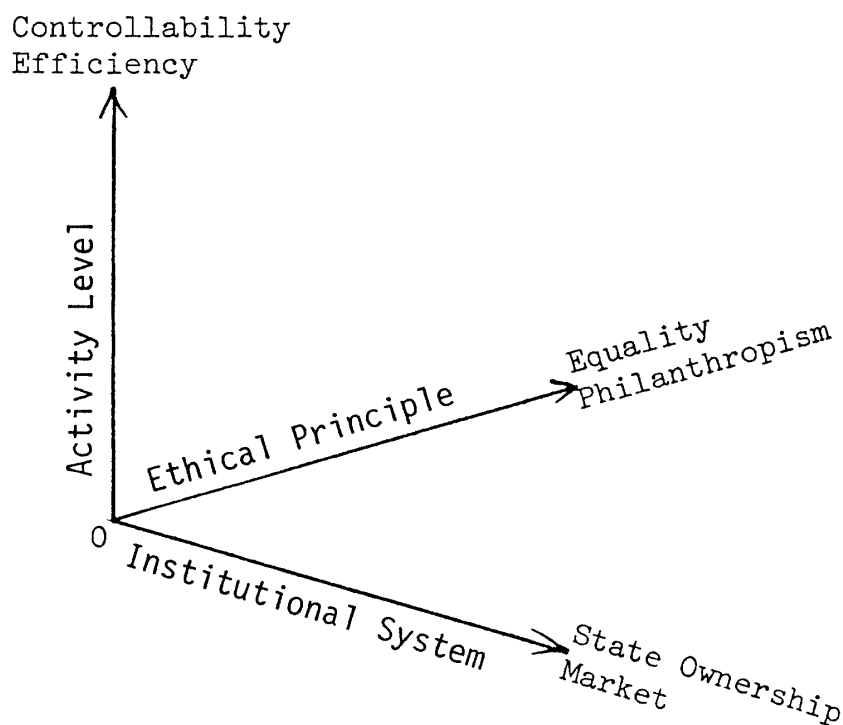


Table 4-1 Socio-Economic Binary Relations

	Equality	Philanthropism
State Ownership	$[(\bar{S}; M), (E; \bar{P})]$	$[(S; \bar{M}), (\bar{P}; E)]$
Market	$[(M; \bar{S}), (E; \bar{P})]$	$[(M; S), (\bar{P}; E)]$

Note: All the binary elements represent the head letters in question. The letters with bars indicate environmental parameters.

shows the division between the two allocating systems. Interestingly, there is no unique correspondence between ownership and allocating system. Of course, there might be a strong correlation between them, but the correspondence or correlation itself should be examined empirically as one of the relationships in an economic system.

Similarly, we can characterize the other axes. Equality on the ethical principle axis measures the degree of equalness in economic life. The conceptual counterpart of equality might be dictatorship in economic administration. Philanthropism on the same axis likewise measures the degree of solidarity and helpfulness in social life. The counterpart of philanthropism might be merciless competitiveness in economic society.

By combining the scales measured on these axes, we can get four conceptual pairs which describe some typical situations in economic societies having certain social

4 I agree with Kornai in this conceptual clarification. Heterogeneous functions of planning conceived so far should be clearly differentiated.

norms and economic organizations. Table 4-1 shows the four pairs. We call these pairs socio-economic binary relations which can be interpreted either as indicators for describing certain situations of economic systems or as policy-mixes for aiming at some objectives.

The activity level of economic systems should be measured according to each binary relation; e.g. controllability here means the degree of regulation ability of a given economic system which consciously drives working of the system to bring out definite objectives. In this context, high controllability means no more than strong regulation regardless of its actual effectiveness. On the other hand, efficiency here simply means labor productivity, which should be measured with proper attention paid to reasonable utilization of labor sources.

B. Conceptual Relations Between Basic Concepts

Before we examine socio-economic binary relations, the relations of conceptual pairs on each axis should be clarified. Through clarifying these relations, we will denote the typical state of economic systems on the coordinate formed by the pairs. Moreover, illustration of the relations introduces important new concepts: that is, *failure of socialization*, *dilemma of philanthropism*, and *illusion of control*.

First of all, the relationship between state ownership and market is illustrated. As mentioned before, the correspondence is not unique because the increase of market share is compatible with some given constant share of state ownership. In Figure

Figure 4-5. The Relation between State Ownership and Central Allocation

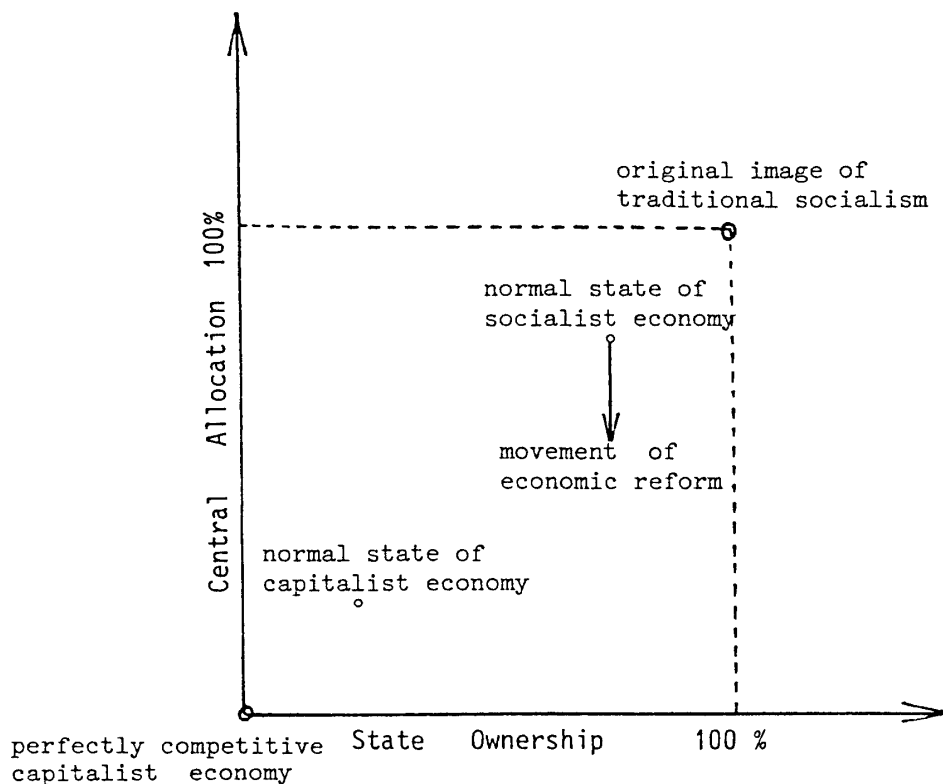
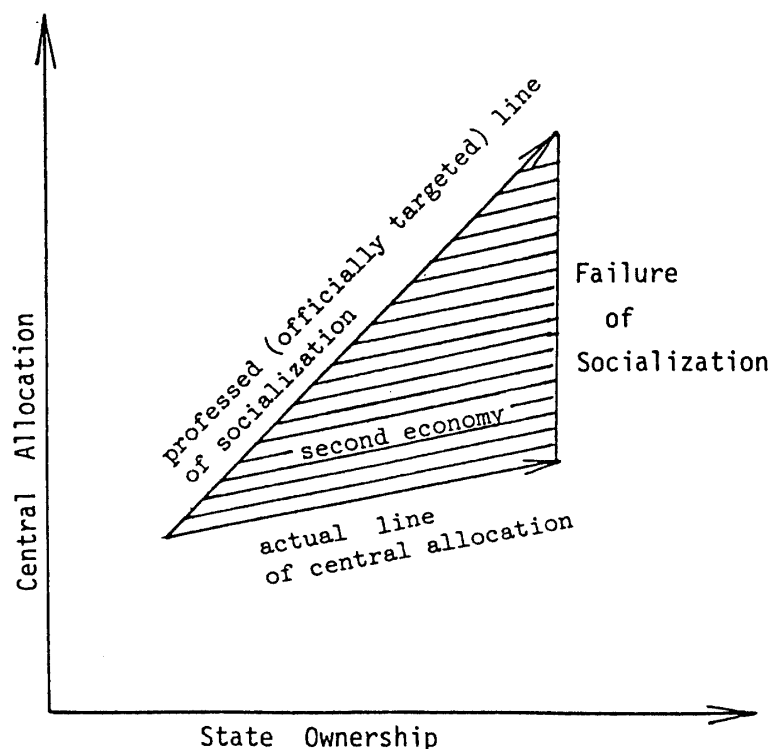


Figure 4-6. Failure of Socialization



4-5 the share of state ownership is taken on the horizontal axis and the share of central allocation on the vertical one. Each of the indicators can be observed and measured by various methods. For example, professed share of state ownership can be found in statistical yearbooks. In the case of central allocation, we can take the share of products which are transacted in the form of centrally-fixed prices and directly distributed in the form of rationing as its indicator.

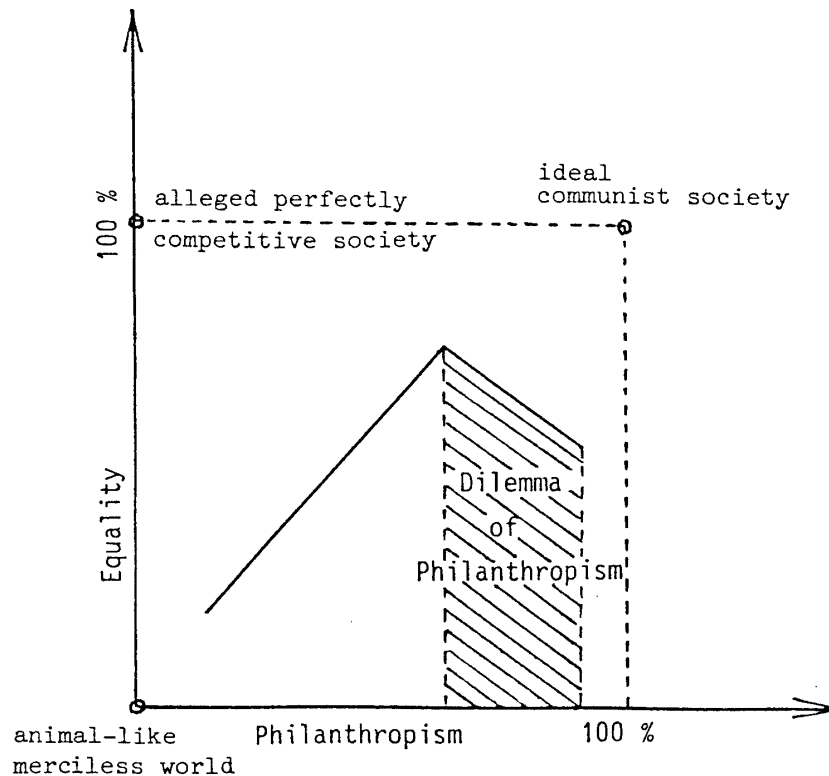
The *normal state*⁵ of economic systems can be denoted on this coordinate. The origin of the coordinate represents the state of the perfectly competitive capitalist economy; the opposite corner shows the original image of traditional socialism or Communism. The actual normal states of capitalist and socialist economies are described by two symmetrical points in Figure 4-5. The arrow in the figure shows the direction of economic reforms in socialist countries during the 1960s when they aimed at enlargement of the market transaction sphere without touching forms of ownership. This movement verifies the statement above which asserts the non-uniquely determined correspondence between state ownership and central allocation.

Figure 4-6 illustrates the so-called *second economy*⁶ on the same coordinate.

5 The concept of normal state is borrowed from Kornai. See J. Kornai and B. Martos eds., *Non-Price Control* (Budapest-Amsterdam: North Holland, 1981), chap. 4.

6 Theoretical analysis of second economy can be found in R. I. Gábor and P. Galasi, *A Második gazdaság [The Second Economy]* (Budapest: Közgazdasági és Jogi Könyvkiadó, 1981). According to their definition, the second economy has a broader sense so as to comprise legalized market transactions. However, I use the concept here in the narrower sense, excluding legal private activities.

Figure 4-7. Dilemma of Philanthropism



Second economy means concealed market transactions which are either partly illegal and partly semi-legal or implicitly tolerated. I call this phenomenon the *failure of socialization*. The figure itself shows a rough illustration of second economy. However, it is sure that the sphere of second economy grows increasingly as the share of state ownership grows in contemporary socialist economies. According to my illustration, there are two ways of reducing the sphere of the second economy. One strengthens the actual effective central allocation; the other legalizes, partly or totally, the activity of the second economy; this leads to a reduction of the shares of both central allocation and state ownership.

Second, Figure 4-7 describes the relation between equality and philanthropism. As already noted, the equality axis measures not legal equality but equality of opportunity for actual participation in economic activity. Income distribution is one of the indicators measuring the results of equality of opportunity in economic life. One can, for example, choose a Gini coefficient or a similar indicator for the vertical axis. On the other hand, it is difficult to choose appropriate indicators for measuring the degree of philanthropism. In the case of firms functioning in traditional socialist systems, it becomes synonymous with the degree of paternalism named by Kornai.⁷ However, philanthropism here has a broader sense which includes the level of social security for the entire population of the society. Consequently, it is suitable to choose the proportion of redistribution income in NNP used to bail out firms confronted with difficulties and bankruptcy and for social security as

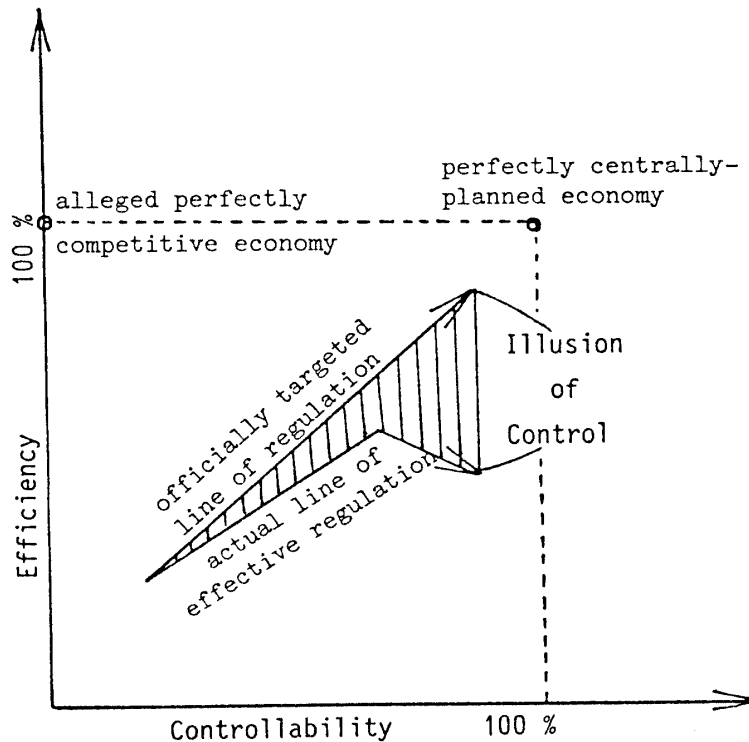
⁷ Kornai, *Economics of Shortage* (Budapest-Amsterdam: North Holland, 1980), chap. 22.

one of the approximate indicators.

Although the degree of equality in an economic system is basically determined by its social structure, various policies based on philanthropism in contemporary society also largely contribute to establishing or securing equality in economic-social life. Therefore, we can assume that there is a strong positive correlation between philanthropism and equality. Nothing in Figure 4-7 needs explanation, except *dilemma of philanthropism*. The dilemma asserts that in a given economic system, characterized by some development and some social structure, philanthropical measures beyond a certain point injure equality itself. For example, in constructing a socialist system, the distribution principle according to work done on one hand, which manifests equality in obtaining results of production, and wage policy restricting income difference on the other hand, are fairly compatible with each other. However, excessive restriction leads to a reduction of equality in economic life and to lower working efficiency. This phenomenon, which is inevitable in socialist construction, might be called the *dilemma of philanthropism*.

Third, the usual goal of increased economic regulation is to promote economic efficiency in business administration. If regulations perfectly fulfill their functions, then, to some extent, they effectively control the behavior of firms. However, firms always employ escape maneuvers, cancelling the effects of central regulations. Therefore, they adjust readily to any regulations as long as they can preserve their conventional favorite status in economic administration. This is why a large number of targeted regulations usually fail to attain their planned levels. The phenomenon which illustrates this kind of false control might be called the

Figure 4-8. Illusion of Control



illusion of control, as charted in Figure 4-8. Of course, it is difficult to properly choose indicators representing the degree of regulation and that of efficiency. As for the former, suitable indicators can be the proportion of wage-bill in the total wage fund, profits in total profits of firms or centrally-allocated investment in total investment. As for the latter, aggregated factor productivity may be appropriate. Other indicators showing the degree of discrepancy between targets and real effects also can be acceptable.

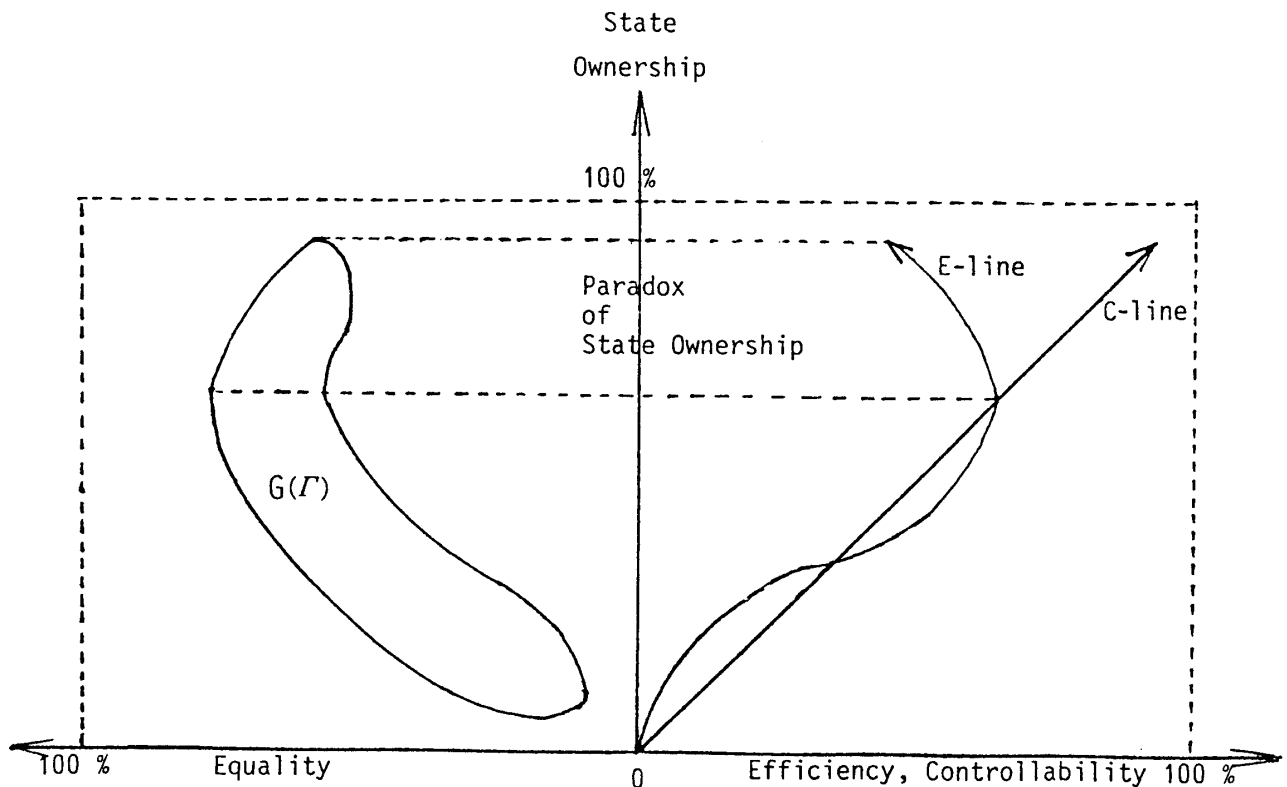
The three new concepts introduced so far just illustrate a few important correlations in economic systems, especially in contemporary socialist economies. It bears noting that this paper introduces only analytical frameworks and a few Hungarian examples. Further empirical work and more precise observations remain to be done.

C. Three-Dimensional Analyses

From Table 4-1 we have four direct products — $S \times E$, $S \times P$, $M \times E$, $M \times P$ — which make coordinate planes. The points of these planes represent ordered pairs constituted from elements of the sets concerned. In the following pages correspondences defined on direct products or described between institutional indicator and activity levels will be examined. Although I do not employ empirical data here, I do try to draw hypothetical relationships for the general framework of an alternative approach to comparative economic system analysis.

First, let us examine direct product $S \times E$, i.e. (state ownership) \times (equality).

Figure 4-9. Paradox of State Ownership



This set makes, so to speak, the coordinate plane of *distributive justice*. Let Γ be correspondence from S to E ; then we have a graph of Γ as a subset of $S \times E$:

$$G(\Gamma) = \{(s, e) | s \in S, e \in \Gamma(s)\}.$$

Figure 4-9 illustrates the graph of Γ and a plausible relation between state ownership and activity levels.

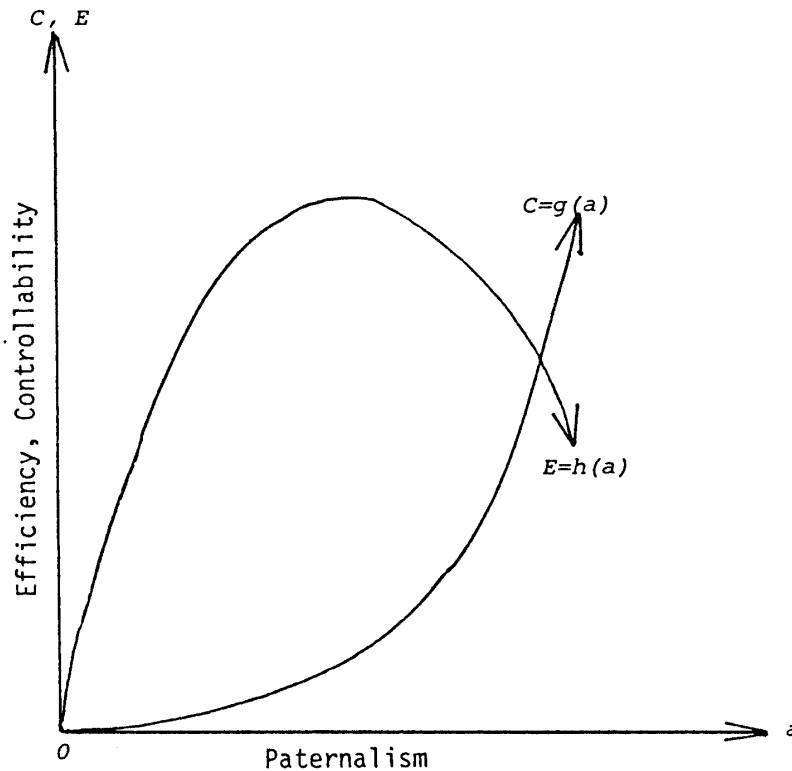
The graph can be interpreted as an illustration of the correlation between state ownership and equality. It shows that distributive justice grows as state ownership increases, because state ownership abolishes exploitation based on private ownership of means of production; but too much centralization in ownership in contemporary environments leads to another type of inequality. That is, lobbying and bribes in bureaucratic systems bring out another type of exploitation. The upper part of the graph represents the sphere of harmful bureaucratism. In addition, the same harmful phenomenon also dampens the efficiency of the national economy, even though professed regulatory ability might be strengthened. These relationships are illustrated in Figure 4-9.

Second, direct product $S \times P$, i.e. (state ownership) \times (philanthropism), forms the coordinate plane of *paternalism*. Each element of the direct product represents a certain degree of paternalism or interdependence between state and firms which is determined mainly by philanthropical-paternalistic policy-measures under state ownership. If we denote each ordered pair with a certain degree of paternalism, then a surjection f from $S \times P$ to finite sequence of paternalism a is defined:

$$f: S \times P \longrightarrow a = \{a_i | i = 1, 2, \dots, n\}$$

or $(s, p) \longmapsto f = (s, p) = a$

Figure 4-10. Trade-Off between Efficiency and Controllability



where a_i is a certain degree of paternalism and $a_i < a_j$ is held for every $i < j \in \{1, 2, \dots, n\}$. For example, Kornai shows five degrees of paternalism in his book.⁸ In this case, the set of the sequence a consists of $\{a_1, a_2, a_3, a_4, a_5\}$.

Let us suppose that there are controllability function g of a and efficiency function h of a . Then it seems plausible that the two functions trade off of each other as in Figure 4-10. This phenomenon might be called the *trade-off between efficiency and controllability*.

Third, direct product $M \times E$, i.e. (market) \times (equality), forms the coordinate plane of *market effectiveness*. Let Γ' be correspondence from M to E ; then we have a graph of Γ' as a subset of $M \times E$:

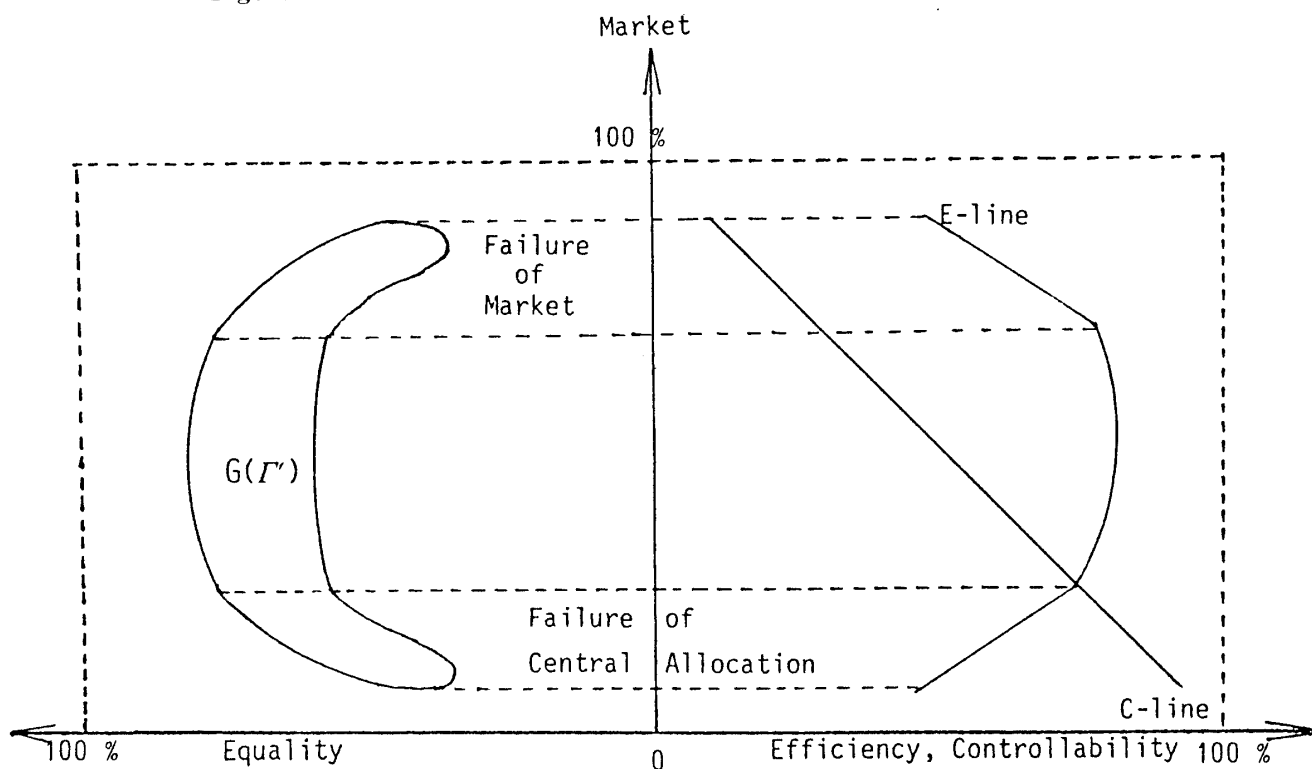
$$G(\Gamma') = \{(m, e) | m \in M, e \in \Gamma'(m)\}.$$

Figure 4-11 illustrates the graph of Γ' and a plausible relation between market and equality.

Similarly, as in Figure 4-9, the graph shows the correlation between market and equality. Market mechanisms do not assure equality and efficiency of economic activities in spheres of goods and services allocation which have public importance in a society. This *failure of markets* is drawn in the upper part of the graph in Figure 4-11. As a counterpart to market failure, there also occurs *failure of central allocation* which leads in the case of over-centralization of allocation to inefficient and unequal management of the national economy.

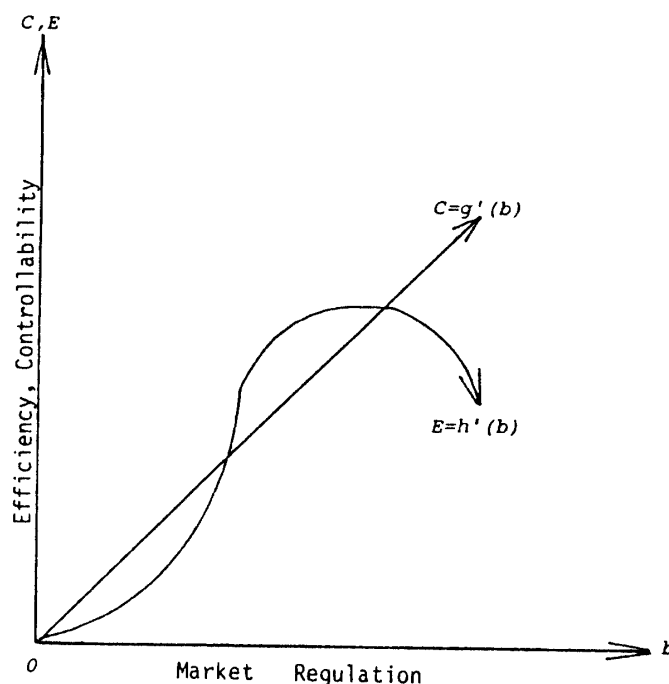
Fourth, direct product $M \times P$, i.e. (market) \times (philanthropism), forms the coordinate plane of *market regulation*. Each element of the direct product represents a

Figure 4-11. Failure of Market and Failure of Central Allocation



⁸ Ibid., chap. 22.

Figure 4-12. Activity Curves of Market Regulation



certain degree of market regulation determined mainly by philanthropic measures for restricting market mechanisms. Therefore, if we denote each ordered pair with a certain degree of market regulation, then a surjection f' from $M \times P$ to finite sequence of market regulation b is defined:

$$f' : M \times P \longrightarrow b = \{b_i | i = 1, 2, \dots, n\}$$

or $(m, p) \longmapsto f'(m, p) = b$

where b_i is a certain degree of market regulation and $b_i < b_j$ is held for every $i < j \in \{1, 2, \dots, n\}$.

Let us suppose that there are controllability function g' of b and efficiency function h' of b . Then it seems plausible that curves of the functions are described as in Figure 4-12.

3. Some Observations on Hungarian Economic Reforms

What were the essential issues of the 1968 economic reform in Hungary? What has been brought about by the reform? As is well known, the biggest change occurred in the field of national economic management. The traditional command system of allocating goods and services was basically replaced by voluntary transactions among firms which are fulfilled through markets. The main aim of the reform was to make firms more flexible in their adjustment to domestic demands and external environments by increasing their independence. However, in spite of the radical changes, a few critical issues remained untouched. For example, problems of bankruptcy of firms and consequent unemployment were excluded from the beginning, for the state has continued to play the role of insurance company. Moreover, the reform did not involve any radical changes in the field of ownership. It is easy to imagine that the functioning of markets is rather restricted by the paternalistic interdependence be-

tween firms and the state under state ownership. Economic and social factors consisting of these critical issues have been altogether softening the budget constraints of firms.⁹

Through the 1970s the Hungarian economy registered steady growth and remarkable successes in raising the people's living standards. Among the CMEA countries that struggled with the dual oil-shocks of the 1970s, Hungary maintained a relatively stable economic position. Hungary's relative success, so far, however, cannot be attributed primarily to the 1968 reform. In my view, the success should rather be attributed to the wise and reasonable maneuvers of economic management which have been accomplished by cooperation between politicians and economists. In other words, unanimous consensus of Hungarian leaders on the course of Hungarian development, which I think is mainly due to the smallness and isolatedness of the Hungarian nation among East European countries, largely contributes to the successful management of the national economy.

My assertion seems to be contradictory to the ideals of 1968. However, it should be noted that the reform was just the first step of a comprehensive reform of the Hungarian economy. Historical process also shows that Hungary entered a second stage of economic reform in the 1980s which involved changes in ownership and stronger functioning of market mechanisms. The continuing objective is real independence of firms which calls for hardening their budget constraints.

In the remaining part of this paper some observations on Hungarian economic reforms will be analyzed along the approaches already introduced.

A. State Ownership and Market Share

First of all, the relation between state ownership and market will be described in a form similar to that in Figure 4-5. Because of space limitation, only the simplest and most typical data will be used to corroborate the hypothetical relationships shown in the previous chapter.

Table 4-2 The Number of Persons Engaged in Small-Scale Private Industry*

year	Self-Employed	Employed	Assistant skilled worker	Total
1955	104,986	4,425	10,748	120,159
1960	87,526	14,765	16,396	118,687
1965	68,685	15,599	11,510	95,794
1970	85,850	14,728	15,584	116,162
1975	86,254	16,907	5,930	109,091
1980	99,405	16,640	4,029	120,074

* Actual numbers.

Source: Béla Gervai, "A magánkisipar fejlődése, helyzete és szerepe Magyarországon (The Development, Situation, and Role of Private Small-Scale Industry in Hungary)," *Közgazdaság; Szemle*, (March, 1983): 302.

⁹ As for the soft budget constraint, see *Ibid.*, chap. 13.

Let us look at Table 4-2. Surprisingly, as shown in the table, hardly any changes occurred for thirty years in the number engaged in legal small-scale private industries whose main products are provided to the people. Of course, there have been growing needs for convenience goods and services which cannot be supplied by large industrial firms and organizations. Inevitably, economic enforcement gene-

Table 4-3 The Share of Market Pricing by Consumption of the Population*
(percentage)

	year	Public pricing	Market pricing
Food & luxury	1968	87	13
	1978	78	22
	1980	72	28
Clothing	1968	75	25
	1978	20	80
	1980	11	89
Building materials	1968	90	10
	1978	72	28
	1980	55	45
Fuel	1968	100	0
	1978	100	0
	1980	100	0
Chemical & petroleum products	1968	79	21
	1978	71	29
	1980	66	34
Total Products	1968	83	17
	1978	63	37
	1980	50	50
Small-scale industry	1968	10	90
	1978	0	100
	1980	0	100
Services	1968	60	40
	1978	56	44
	1980	45	55
Consumption Total	1968	77	23
	1978	55	45
	1980	45	55

* Proportions of each price form in consumption value.

Source: B. Csikós-Nagy, *A magyar árpolitika [Hungarian Price Policy]*

(Budapest: Közgazdasági és Jogi Könyvkiadó, 1980), pp. 53, 54, and 224.

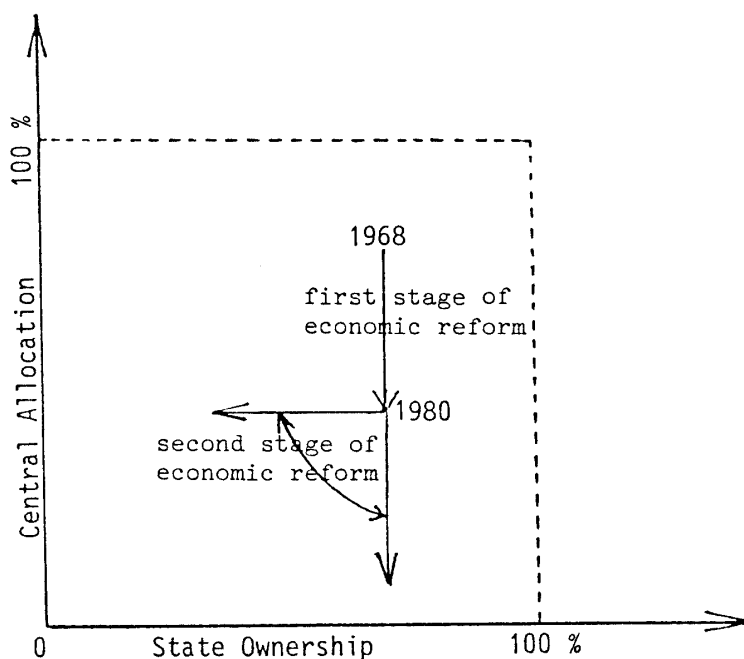
Table 4-4 Summary Economic Indicators by Social Sectors (percentage**)

	Socialist sector	Within it state sector	Private sector	Total
1970				
Active earners (actual number)	95.8	67.7	4.2	100.0
Fixed assets	99.3	73.6	0.7	100.0
National income	97.4	70.7	2.6	100.0
Investments	90.7	74.1	9.3*	100.0
Industrial gross production	99.0	93.2	1.0	100.0
Output in construction industry	93.7	70.0	6.3	100.0
Agricultural gross production	98.4	17.2	1.6	100.0
Retail trade turnover	99.2	65.5	0.8	100.0
1980				
Active earners	96.6	71.1	3.4	100.0
Fixed assets	99.6	71.4	0.4	100.0
National income	97.0	70.3	3.0	100.0
Investments	88.9	77.2	11.1*	100.0
Industrial gross production	99.3	93.8	0.7	100.0
Output in construction industry	92.7	70.1	8.3	100.0
Agricultural gross production	99.3	20.1	0.7	100.0
Retail trade turnover	99.2	62.0	0.8	100.0

* Investments by the population. ** Value data are based on current prices.

Source: Központi Statistika; Hivatal, *Statisztikai évkönyv 1980 [Statistical Yearbook]* (Budapest, 1981), p. 31.

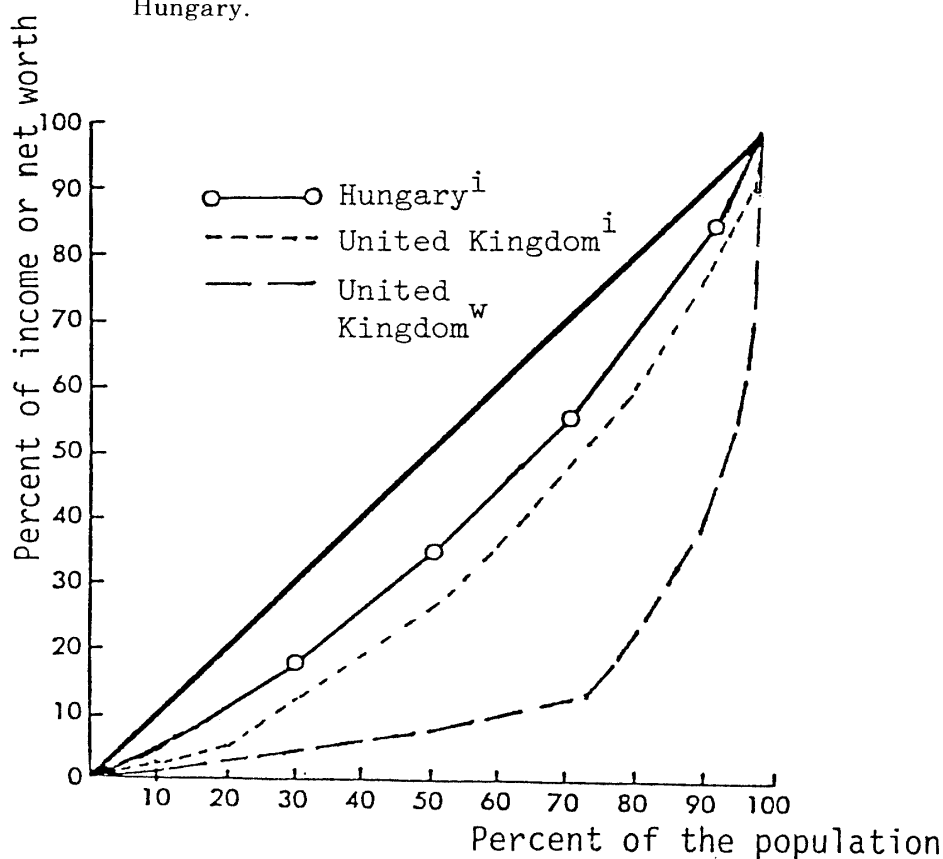
Figure 4-13. Increase of the Market Share in Hungarian Economy



rates illegal or semi-legal markets in goods and services for daily life. In other words, growth in the need for well-organized suppliers of consumer goods and services has been parallel with economic growth. This is the main reason for the existence of a second economy. The objective of the policy-measures taken from the beginning of 1982 is to enlarge the sphere of small private production and to permit management on a rental base, thereby stimulating the supply of consumer goods and services. Although various attempts are being carried out at present, meaningful data will be available only after a few years. In any case, certain kinds of reprivatization are taking place.

Next, paying attention to the market in consumer goods and services (see Table 4-3), we see that the share of market pricing has been growing since 1968. Table 4-4 also summarizes the facts which corroborate the unchanged weight of the private sector under the growing rate of market pricing. The sole exception is own-account build-

Figure 4-14. The Distribution of Income and Wealth in the United Kingdom and Hungary.



Note: Small suffixes *i* and *w* indicate respectively income and wealth data. The Lorenz-curve of Income for the U. K. shows the distribution in 1974-5. The other two curves show the distributions in 1976.

Source: Zs. Dániel, "Jövedelemeloszlás, lakáseloszlás és társadalmi egyenlőtlenség" [Income Distribution, Housing Distribution, and Social Inequality] *Valóság*, no. 2 (1981): 75-88 and Royal Commission on the Distribution of Income & Wealth.

ings of the population which rather belong to the activity of the second economy.

The dynamic relationship between state ownership and market share can be described as in Figure 4-13, taking into account all the facts shown above. On the coordinate plane, the national income's share of the state sector is taken as the indicator of state ownership, while the share of public pricing is taken as the indicator of central allocation. The share of national income had not changed during the first stage of economic reform. On the contrary, the share of central allocation (market) has been continually decreasing (increasing) since the 1968 economic reform. The introduction of various methods in business management, including private management in 1982, will surely result in the decrease of national income share for the state sector. However, the result is not clear yet. Nevertheless, the second stage of Hungarian economic reform can be regarded as a very important experiment which might provide a means of reconstructing the traditional socialist economy.

B. Distributive Justice

According to data on income distribution for whole households, Hungary shows very equal distribution. To simplify description, I equate the term "equality" here with "equity." Of course, it is questionable whether equity in income distribution really expresses actual equal earning opportunity according to work done. It depends on how we evaluate the quality differences of works. If the differences are regarded as negligible and therefore unimportant, then equity becomes a synonym

Table 4-5 The Distribution of Income and Wealth for Whole Households

Country	Gini	Coefficient
	income	wealth(net worth)
Hungary	0.222 (1976)	—
United Kingdom	0.324 (1974/5)	0.77 (1976)
United States	0.49 (1969)	0.72 (1969)
Japan	0.344 (1974)	0.534 ^f , 0.615 ^r (1974)

Note: Japanese wealth data show the distribution of financial assets (0.534) and that of real assets (0.615) in non-agricultural households.

Sources: Zs. Dániel, "Jövedelemeloszlás, lakáseloszlás és társadalmi egyenlőtlenség [Income Distribution, Housing Distribution and Social Inequality]," *Valóság* No. 2 (1981): 75-88.

Satoshi Mizoguchi, Noriyuki Takayama, and Yasuhiro Terasaki, Sengo Nippon no Shotokubunpu (Income Distribution in Post-War Japan)," *Keizai Kenkyu* 29, No. 1 (Jan., 1978): 44-60.

Poyal Commission on the Distribution of Income & Wealth, *Report* No. 7 (1979): 15.

Noriyuki Takayama, Fubyodo no Keizaigaku (*Economic Analysis of Inequality*), (Tokyo: Toyokeizai, 1980), p. 28.

E. N. Wolff, "The Size Distribution of Household Disposable Wealth in the United States," *The Review of Income and Wealth* 29, No. 2 (1983): 141.

for equality. Distributive justice, in this case, alleges equality grounded on the distribution principle of work done.

Figure 4-14 shows Lorenz-curves of the distribution of income and wealth for whole households in Hungary and the United Kingdom. It is worth noting that the biggest difference between the two countries exists in property distribution, while the difference in income flow is relatively small. This fact can be corroborated by comparisons with data on other capitalist countries. As shown in Table 4-5, the difference between Hungary and capitalist countries manifests itself in the distribution of wealth.

It is fairly important to pay attention to the distribution of financial assets, because there exist no capital markets in socialist countries. As for the distribution in the United States in 1969, E. N. Wolff writes :

The most concentrated of these is trust funds with a Gini coefficient close to unity; the next is corporate stock with a Gini measure of 0.98; third in line is net equity in unincorporated business and investment real estate, with a Gini value of 0.94; fourth is bond and securities, with a Gini of 0.94; and the fifth is time and saving deposits with a Gini coefficient of 0.89. Except for the last of these assets, each was owned by at most 31 percent of households.¹⁰

The appropriate indicator for measuring the amount of state ownership is the proportion contributed by public corporations to GDP. However, there is no such information in SNA accounts. Therefore, as an alternative indicator, the proportion contributed by general government to GDP is used for the United States and Japan. As for Hungary, the contribution of the socialist sector to national income is taken from Table 4-4, while U. K. data are taken from the research of J. D. Wells.¹¹

Now, to draw the coordinate plane of distributive justice, we measure the size

Table 4-6 The size of public sectors

Country	Percentage of Gross Domestic Product %	
	public corporations	general government
Hungary (1976)	70	20*
United Kingdom (1975)	11.2(13.8**)	19.0
United States (1969)	n. a.	12.69
Japan (1974)	n. a.	7.9

* Net tax revenue excluding profit transfer as a percentage of net national income.

** Excluding general government services.

Sources: Wells(1982), Wolff (1983), OECD(1976), and my own calculations.

10 E. N. Wolff, "The Size Distribution of Household Disposable Wealth in the United States," *The Review of Income and Wealth*, 29, No. 2 (1983): 141.

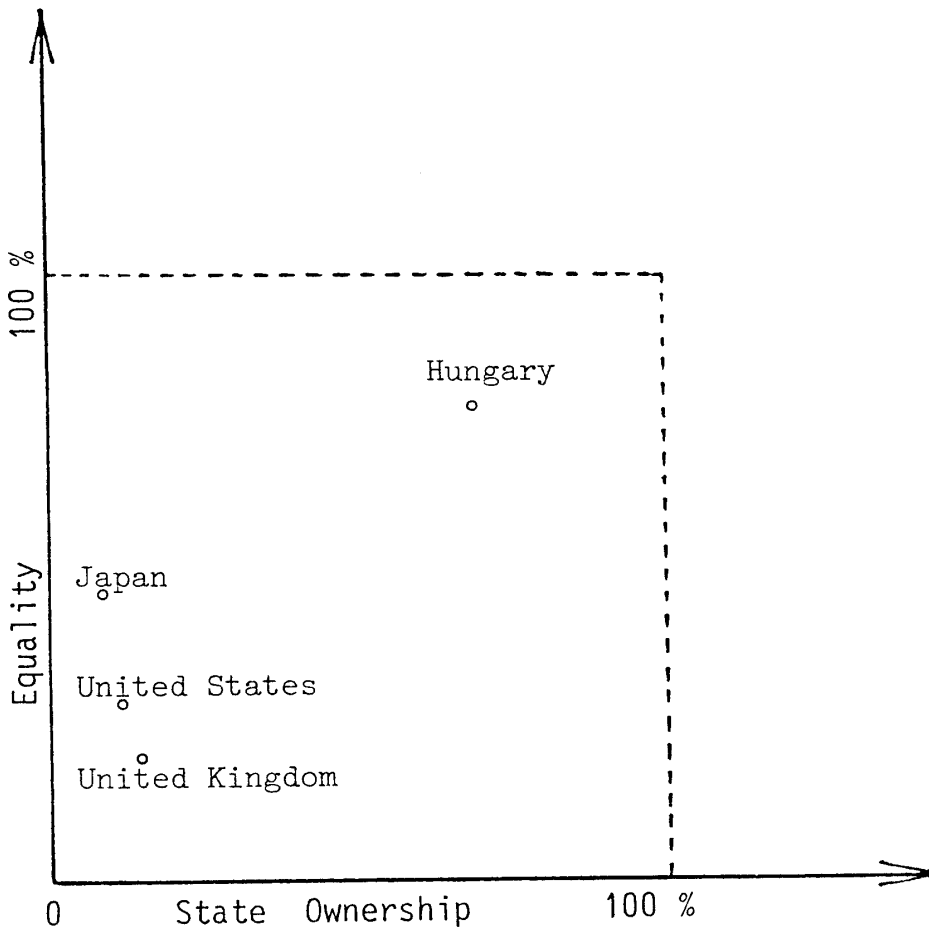
11 J. D. Wells, "Public Sector Statistics for the United Kingdom," *The Review of Income and Wealth*, 28, No. 2 (1982): 178.

of the public sectors on the horizontal axis using data from Table 4-6. On the vertical axis, $(1 - \text{Gini coefficient}) \times 100$ is denoted as an indicator of the degree of equality. Here, as a Gini coefficient, we take that for wealth and not for income, because the wealth indicator reflects more appropriately the essential differences between socialist and capitalist systems than does the income indicator.

Figure 4-15 shows the positions of the countries on the coordinate plane of distributive justice. These points might be interpreted as the normal points for these countries. In spite of the introduction of market transactions in Hungary, there seems to be no big change in distributive justice. As long as the market transactions concern only commodity markets, the market mechanism does not exert influences on income distribution. The critical issue for distributive justice is whether capital markets are opened or not, because, as seen in the advanced capitalist countries, inequality in distribution mainly exists in the distribution of wealth, and especially of financial assets. Therefore, how capital markets should be introduced if the introduction becomes inevitable will become an essential issue for Hungary.

The paradox of state ownership described in Figure 4-9 can be characterized as the inequality created by bureaucratic income distribution in circumstances where capital markets do not exist.

Figure 4-15. Distributive Justice

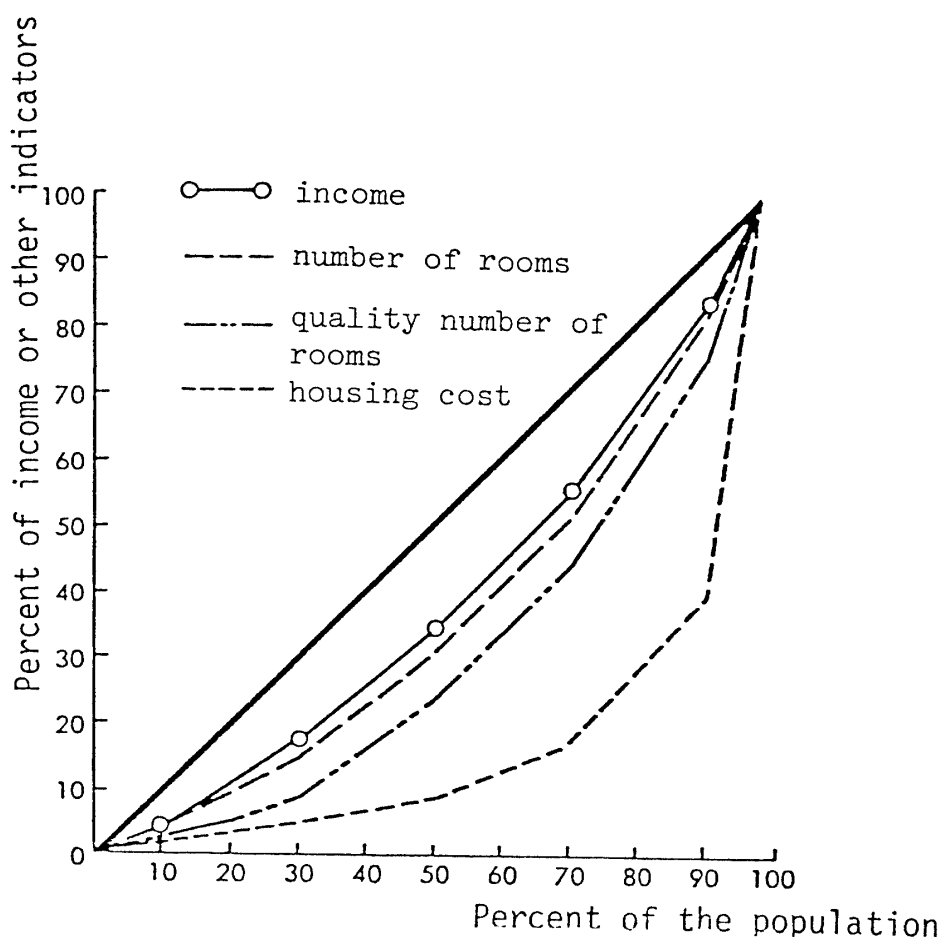


C. Failure of Housing Allocation

Interesting results on the distribution of housing benefits in Hungary are found in the work of Dániel.¹² According to her research, housing allocation contributes not to improvement of equality, but to the enlargement of inequality in income distribution. Figure 4-16 shows that the distribution of flats in Hungary is more unequal than that of income. Moreover, the distribution of the housing cost burden represents still more unequal distribution. The coefficient of variation of housing cost is 269 percent, while that of income is 46 percent.

Of course, the objective of housing policy in socialist countries is to compensate for income differences by securing houses for lower-income earners. However, the facts show that the central housing allocation system in Hungary has failed so far to promote equality in social life. This is partly because indirect subsidies in

Figure 4-16. The Distribution of Income, Housing Benefits and Housing Cost in Hungary (1976).



Note: The differences in quality of flats are evaluated by the number of rooms in the indicator of "quality number of rooms."

Source: Dániel (1983).

¹² Zs. Dániel, *The Effect of Housing*, mimeographed, (Budapest: Institute of Planning, Hungarian National Planning Office, 1983).

the form of housing benefits are relatively large compared to income differences. Therefore, in our terminology it can be said that the failure of central allocation in the housing field brings out the dilemma of philanthropism.

Although Dániel suggests the introduction of market mechanisms into the field of housing transactions in Hungary, the problem is not that simple.¹³ The housing transactions market can be characterized as being composed partly of commodity transactions and partly of capital transactions. For example, the Lorenz-curve of housing cost in Figure 4-16 shows inequality in the housing burden, on the one hand. However, on the other hand, the same curve shows property inequality as the other side of the coin. If free transactions are introduced into the housing field, it is possible that implicitly existing property inequality might be consolidated and further enlarged.

Here we have encountered the dilemma of socialism in the sense that the inevitable introduction of the market mechanism to complement the failure of central allocation results in the consolidation and enlargement of inequality in the ownership of real estate, because real estate is transformed into capital goods in market transactions. The dilemma derives not simply from the failure of central allocation, but from socialist construction itself under personal ownership of consumer goods, especially of such durable consumer goods as flats.

4. Implications for the Future Development of Economic Systems

Because of space limitations, exhaustive application of our analytical frameworks to existing national economies remains to be done elsewhere. In the remaining part of this paper I will try to draw a few implications from the previous analyses for the future development of economic systems.

First, it becomes clear that the introduction of market mechanisms into the field of commodity transactions, in itself, brings no changes in income distribution, and mainly contributes to the improvement of efficiency in the allocation of goods and services. In this sense, the traditional formulation "planning vs. market" should not be taken as the problem of choice between socialist and capitalist systems, but as the problem of allocation efficiency under given technological developments of collection and processing of information. As shown in Figure 4-11, neither the market nor central allocation has the ability to efficiently distribute goods and services among economic transactors. Therefore, all contemporary economies are consciously or unconsciously forced to employ compromises between the market and central-public allocation of goods and services. Of course, there are still many differences in the concrete forms that these compromises take, especially between socialist and capitalist economies. However, as long as these differences do not necessarily result from differences in forms of ownership, I think that the distances between countries in terms of the way they mix market and central allocation will be diminishing.

13 Dániel, "A lakasszektor reformja [Reform of the Housing Sector]," *Valóság*, No. 12 (1981): 55-67.

Second, as is clearly shown in the description of distributive justice, capital markets have a decisive role in the distribution of surplus value and therefore assets. It has become an urgent problem in socialist countries whether capital markets, even if strictly regulated, should be opened to strengthen the independence of firms. It might be said at least that the legalization of market transactions of real estate, which becomes inevitable because of the failure of central allocation of housing, will surely enlarge inequality in property ownership. As an aside, it is worth noting that more than 50 percent of the differences in property ownership in Japan can be explained by the difference in ownership of flats, although overall distribution in income and wealth in Japan is relatively equal compared with other advanced capitalist countries.

Generally speaking, inequality in property ownership is quite serious in advanced capitalist countries. However, there is also a remarkable tendency in contemporary capitalist economies to diminish personal investment and to increase institutional investment. Of course, the institutionalization itself does not naturally diminish inequality in property ownership, but it makes it easy to restrict personal investments and to employ policy-measures for correcting inequality from the standpoint of distributive justice. Thus, in the contemporary environments surrounding national economies, the economic distance in distributive justice between contemporary economies will be diminishing in the future.

Third, it is interesting to note that the ranking shown in Table 4-7, based on total tax revenue as a percentage of GDP, can hardly be attributed to the distinction in forms of ownership. For example, it cannot be asserted that the difference between France and the United States in this respect is smaller than that

Table 4-7 Total tax revenue (including social security contributions) as a percentage of gross domestic product as market price in 1980

Sweden	49.9
Netherlands	46.2
Hungary	45.2(61.8*)
Denmark	45.1
Belgium	42.5
France	42.5
Irish Republic	37.5
German Federal Republic	37.2
United Kingdom	35.9
Italy	32.8**
Canada	32.8
Switzerland	30.7
United States	30.7
Japan	25.9

* Including profit transfer from firms to government in 1976.

** 1979.

Sources: Wells (1982) and my own calculations.

between France and Hungary, even if the profit transfer is taken into account for the calculation.

The large amount of profit transfer is the sole and the biggest difference between socialist and capitalist economies in the sphere of income redistribution. However, contemporary economic reforms designed to tighten the budget constraints of firms in Hungary will lower the degree of profit redistribution. Therefore, it is hard to imagine that the difference in the proportion of redistribution in GDP between socialist and capitalist countries will be increasing.

I think the statements above also demonstrate the usefulness of a synchronic approach in comparative analyses of economic systems.

Comment

Časlav Očić

Morita's thought-provoking paper elaborates on the convergence approach aiming at offering a fresh look at the problems of economic systems comparison. The approach he suggests seems to be particularly useful for the description and analysis of "real" (or reformed "real" — in his case: Hungarian) socialism but a less suitable tool for the analysis of phenomena and processes which go beyond traditionally conceived capitalism and socialism (or Communism). The proposed approach leaves out — actually, it is not properly equipped to grasp — genuine innovations which transcend the realities (and categories) of both capitalism and (state) socialism. Everything essentially different from the "classical" capitalist and "classical" (statist) socialist systems passes practically unnoticed. A very strong inclination to reduce socio-economic systems to economic mechanisms (paralleled by the formalization and quantification of the systems' qualitative characteristics) leads, first, toward a pronounced tendency to use mechanical analogies (focusing on formal [dis-] similarities) in comparisons of the two systems, and, secondly, toward interpretation of any change as a "reform," that is, as a *new* ("optimal" or "compromising") *combination* of existing, well-known, *old elements* (instruments, mechanisms), while leaving the essence — the societal power structure (and its impact on the economy) — untouched. Failure of the undertaken economic reforms might be attributed to the power structure, which practically remains unchanged.

This by no means denies the necessity of an "optimal mix" of economic mechanisms within any socio-economic system: the more complex (and probably more "ambitious") economies and societies will have to employ a larger number of coordination instruments. This applies equally to both traditional systems (capitalism and state socialism) and to the self-determinative, polyarchic, associationist alternatives to them (the contemporary Yugoslav self-management system, for example.)

Why then does convergence/divergence theorizing (not comparative systems theory in general, which can be illustrated by the emergence of a new discipline — Comparative Socialist Economic Systems) confine itself to a dichotomous view of the systems? When Tinbergen originally formulated his convergence theory, two huge rival blocs of countries were struggling for world supremacy. And the two blocs used to be (and still often are) identified with two socio-economic systems: capitalism and Communism — *tertium non datur!* Morita, more or less consequently, also adheres to the popular traditional image of capitalism and socialism. For him only two basic types of ownership exist: private and state ownership; social ownership is excluded — actually, it is identified (following the identification of society with the state) with state property. (In general, ownership is treated only as a legal, and not as an economic, category.)

What are the possible relationships between the two systems/blocs? They can

coexist peacefully or fight to the death. If they opt for peaceful coexistence (which does not exclude certain varying degrees of tension between them), then their paths of development can converge or diverge. If they converge, various patterns of convergence can be observed. Leaving aside differences between *structural* features of the systems, their patterns of *behavior*, and the mechanisms they employ in order to *function*, one might operationalize all of those concepts in the same way, introducing various indicators as quantifiable representatives of selected (very often qualitative) features. Substituting each indicator for the actual figures one would then *measure* the *historical* tendencies. There should be no surprise if the main finding of such a (“Newtonian”) procedure is: in socialist countries during the twenty-one year period under observation, in terms of five indicators representing deeply rooted real tendencies, there was no change, i.e., there was no history. This rather puzzling conclusion is probably a consequence of the fact that at the initial stage of the analysis some important distinction failed to be made. In this particular case it is a distinction between chronological (calendrical) and historical times. This conclusion about historical tendencies is based on the analysis of the passing of a certain number of calendar units, not on historical analysis, where *causality* emerges as an essential problem.

It seems that the “dychotomous” approach reflects more the military, political and ideological dimensions of the world in the early 60s than an exact picture of the economic (and other basic) features of then (or now) existing socio-economic systems. Its primary concerns are East-West bloc relationships; it almost completely neglects North-South problems. It actually implies that recently emerged less-developed countries can only choose between market-oriented capitalism and state-dominated socialism.

Is it possible to escape from the “magnetic field” felt strongly in both theory and practice? Do theoreticians really need to reduce the diversity and complexity of the contemporary world reality to a rather simplistic vision in which blocs dominate? Practically, is the choice for poor Bangladesh really so easy, so simple—and so fatalistically limited?

Morita’s paper needs a few more comments:

1. Besides the planning concept there are some other concepts (market: factors, goods and services, perhaps sectors of the economy; ownership: private, state, collective, social; efficiency: micro, macro, static, dynamic; also “state” cannot stand as an approximation for “society” — the state/society distinction is not only a matter of semantics) which should be differentiated. Equality is also one of them. Morita said that “equality on the ethical principle axis measures the degree of equality in economic life.” In economic life equality can (and should) be secured in production and consumption. Equality of producers implies equal access to the productive capital of the society, i.e., social (as opposed to private, group or state) ownership with its two fundamental consequences: self-management (equality of participation in decisionmaking) and social (as opposed to administrative, bureaucratic) planning. Equality of consumers implies an equitable and just distribution of income. (For more details see: Branko Horvat, *The Political*

Economy of Socialism: A Marxist Social Theory, London: M. Robertson, 1982.)

2. It seems that the "conceptual counterpart" of equality cannot be "dictatorship in economic administration." It can simply be inequality, whether of wealth, of income, or of any other type.

3. Loose (and not always consistent) links among proposed "key-concepts" give the impression of a "mechanical set" rather than an "organic entity." How are "key-concepts" interrelated? Are "key-concepts" all equally important as is claimed in the same place? They represent qualities of different (institutional, ethical, economic performance, etc.) types. Their interrelationships are defined within certain general theoretical frameworks.

4. A "general theory" serves also as a source of criteria for the selection of indicators and the evaluation of their "use value." This can be illustrated by the following example: In Morita's opinion, "the political concentration indicator should be replaced by an indicator of the political tolerance in society." It is very difficult to agree with him on this point. First, political tolerance can imply a very high degree of inequality in both wealth and income (not to mention non-economic inequalities.) This once again underlines the need for choosing consistent elements, i.e., it illustrates the necessity of a "general theory." Second, a "general theory" might also help in formulating "key-concepts" in a positive rather than negative way. To formulate the political equality indicator not negatively (as "tolerance") but positively (say, as "meaningful participation in political decision-making") can be advantageous from a theoretical and methodological point of view. Third, compared to Morita's, Kornai's indicator of political concentration appears to be a more suitable, though insufficient, one. It is useful in the description and analysis of "real" (state) socialism, but it is not of equal importance for capitalism: in capitalism social power is derived mostly from economic sources, while in state socialism it is derived from political ones. In that sense capitalism can be defined as an economic, and state socialism as a political, society. It seems at first glance that such a definition emphasizes "primary concerns" or principal goals, of the respective systems. However, it also points out the main driving forces operating within the given societies.

From the methodological point of view, this example illustrates very well the fact that some indicators can have different meanings (weight, importance) within different contexts ("systems"). Also, it reminds comparative analysts that not only is it important *how* something is compared, but it is equally (or even more) important *what* is compared. This fact requires a thorough analysis of reality aiming at the precise identification of and clear distinction between more permanent structural characteristics and more fundamental behavioral patterns, on one side, and accidental phenomena, on another.

Comment

Aladár Sipos

The first problem is the methodological approach of convergence theory. According to Morita, during the period of NEP in the Soviet Union the socialist system approached the capitalist one. I think this is incorrect, because during the period of NEP in the Soviet Union huge changes took place in society. In 1922 the Soviet Union had five economic sectors; in 1930 only two existed (cooperative and state-owned). Consequently during the period of NEP the socialist system did not approach the capitalist one; on the contrary the Soviet Union moved further and further away from it.

According to Morita the increase of state ownership initially increases economic efficiency but later serves as a detriment. Beyond some point further increase results in reduction of the efficiency of the national economy. The latter case corresponds to over-centralization.

First, it is not clear to me what is meant by over-centralization. Does it concern the proportion of state-owned enterprises, or something else? Second, this assertion does not square with the facts. The facts show that productivity increases in the state sector. Furthermore, Hungarian production, particularly that of industry, is extremely concentrated. Our economy is characterized by the existence of many big enterprises and the number of small and middle enterprises is insignificant. It is remarkable that precisely in the years immediately preceding the reform a new wave of concentration evolved: enterprises merged, "nation-wide enterprises" were formed, monopoly trusts developed, etc. In spite of this the efficiency of the national economy in Hungary significantly increased after the reform. However, fundamental improvement had not been made.

Morita considers the existence of the so-called second economy to be the failure of socialization. I think this is incorrect. Morita points out that "needs for well-organized suppliers of consumer goods and services have been growing in parallel with economic growth. This is the main reason for the existence of a second economy." I agree with this assertion. Why call this a failure of socialization when it is not a consequence of socialization but of economic growth?

I should like to emphasize that every economy has an informal sector. At low levels of development it exists because large formal organizations have not yet been established. At more developed stages it is present because some people try to at least partly evade state supervision and taxation or the structure and discipline of large organizations. In Hungary too, this sector has always existed. Over the last ten to fifteen years the informal sector has broadened rapidly. It has made up for shortages in the truest sense of the word: it partly satisfies demands that the formal sector is to meet.

The informal sector is a collective notion. It comprises illegal and tacitly tolerated activities, as well as those which are not illegal but are carried on out-

side of the formal organizations with approval of and patronization by the state. The main objective of the new 1982 measures in Hungary is to bring to light those informal activities which have been judged to be beneficial to the economy, to create for them legal frameworks and, to a certain extent, to support their expansion.

Furthermore, it is true, as Morita writes, "that the objective of the policy-measures taken from the beginning of 1982 is to enlarge the sphere of small private production and to permit management on a rental basis, thereby stimulating the supply of consumer goods and services." Satisfaction of such needs is not the only way to increase the sphere of small private production.

One of the characteristics of the new wave of the reform started in 1979 is that it is intended to diminish the concentration of the state sector. There are two ways to achieve this. The first is to break up the huge existing organizations by enacting higher administrative resolutions. The second is to found new small state-owned enterprises. According to the new legal regulations put into effect in 1982, the existing large state enterprises can found affiliates through their own initiative. In addition, ministries and local councils may establish new small firms. Also, so-called "small cooperatives" can be founded.

According to Morita, the main aim of the Hungarian Economic Reform was to establish a flexible system for responding to domestic demands and external environments. I think Morita oversimplifies the main purpose of the reform.

Let us examine the aims of the Hungarian Economic Reform. In the New Economic Management in 1966-1968 the following six interrelated goals were formulated.

1. Persistence of the multisectoral nature of the economy, by which was meant overcoming hindrances to development of the cooperative sector and promoting rational small-scale private activities which complement operation of the state and cooperative sectors.
2. Unrestricted trade between enterprises in materials and products.
3. Introduction of a system of mostly unfixed prices that reflect demand and supply conditions.
4. Establishment of close links between production and foreign trade.
5. Independence of the profit-motivated enterprises with uniform and normative state control.
6. Increase of the democratic rights of workers in determining the operation of the enterprises.

These six basic tenets of the reform were not satisfactorily put into practice. After a good start in 1968, progress came to a halt for the following reasons.

1. Diversification of state enterprises was not attained. Their number continued to decrease until 1980. The development of small industrial, construction and servicing ventures was still hindered by many administrative factors in the 1970s. It was only after 1980 that some expansive industrial and food industrial enterprises and trusts were dissolved. But in many areas, particularly in construction, home and foreign trade, and also in several fields of industry, enterprises of economically unjustified large size are still operating. The forms of enterprise are not diversi-

fied enough. Development of the small entrepreneurial units has led to a significant upswing in this respect. However, there are still many administrative factors hindering the healthy integration into the socialist economy of small ventures, which have grown in number since 1982. Among the obstacles, besides the unsolved problem of supply of materials and machinery, the system of income tax has to be mentioned. It particularly hinders the non-agricultural ventures from developing their activities in a legal framework.

2. The number of commercial channels did not increase according to intentions, and at times those efforts which asserted the methods of central allocation of materials through forced monopoly channels gained momentum.

3. In spite of the growing proportion of the so-called free prices, prices did not reflect supply and demand. Neither the official nor the free prices played a sufficiently active role in harmonizing the interests of buyers with those of sellers.

4. The relationship between production and consumption, though having become closer, could not adequately affect the development of production for export and the efficiency of import use, because of the many firm-by-firm regulations.

5. The individual nature of regulators and the general over-regulation did not allow the independence of enterprises to evolve to the desired degree.

According to Morita, "the reform did not involve any radical changes in the field of ownership." He emphasizes that, "it is easy to imagine that functioning of markets is rather restricted by the paternalistic interdependence between firms and the state under state ownership." The latter is true. But what does it mean that the reform did not involve any radical changes in the field of ownership? It seems to me that Morita is thinking of the reprivatization of state ownership. I do not think that the increase in the percentage of small private production in the national income means reprivatization. Reprivatization refers to the transformation of state ownership into private ownership. Such action is out of the question. State ownership will be developed in another way.

Hungarian practice abolished the plan directives. The abolition of the direct control of the economic units by the center substantially increased the degree of enterprise autonomy and improved the possibility of adjustment to market requirements. However, by maintaining the old institutional forms of supervision by state organs and by narrowing the scope of movement through the financial regulators, a framework for management was created, in which the direct control was replaced by an indirect one. (That is a situation in which the activity of enterprises is still strongly dominated by the will of the state, frequently in the form of plans.)

The inelasticity of the money supply seems to contradict what Kornai characterizes as soft budget constraints. The real situation, in my opinion, cannot be described simply along the lines of Kornai's reasoning. I think that the paternalistic center motivated by generosity helps its enterprises when they run into trouble. In fact, the center links itself with monetarily deficient enterprises and forces them to grow, a practice which is loved by the enterprise managers. Thus the enterprises are forced to give way to central pressures, and the center, wishing to retain its power, finds itself in a peculiar trap; it cannot resist credit claims

from enterprises even if the economic equilibrium and the maintenance of market pressure demand such resistance.

One alternative for developing the market is for the state, having abolished the plan directives, to restrict the role of the plan to direct and indirect control of public utilities as well as to government influence on the competitive sphere of the economy according to the concepts of the plan. What extent of enterprise independence is adequate under state ownership in a socialist society and whether or not restructuring relations between enterprises and the controlling state organs is needed for attainment of independence remains to be clarified.

I think that uniform treatment of the whole economy is not expedient. Organizations financed by the state budget, such as those of the cultural and health sectors, are of course nonprofit organizations. In this field the tasks of institutions can be defined and separated so that this will not disturb their efficient operation.

In another area of the economy are such enterprises as the basic utilities (gas, water, electricity works, mail, telephone, railways, and other transportation industries), which should be treated differently. The economically justified monopolistic positions of these nationwide organizations, for which import competition is out of the question, call for the maintenance of the present hierarchical state control and the limitation of enterprise independence.

The scope of economic activities of the other enterprises (mining, raw material production, agriculture, building material production, construction, manufacturing, domestic and foreign trade, various services) must be regarded in a broad sense as a competitive sphere.

In this sphere a resolution of the practical conflict between economic control systems and socialist ownership becomes necessary. If we expect vigorous and purposeful entrepreneurial behavior from the enterprises, we must protect these beneficial endeavors from the direct interference of central and local state organs.

The choice of a development strategy was not clear even in 1966-68. Although plans had been made to adjust the institutional position of enterprises, the framework for this necessary change was not yet fully designed. Consequently, implementation of the first measure of the program, the transformation of the supervision by branch ministries, was postponed.

After 1968 the changes in institutional conditions were omitted from the agenda. Changes since 1979 have been more market-oriented. But partly owing to the bad economic situation, the freedom of management of enterprises has still not increased adequately.

If the Hungarian government chose further expansion of the market, it still would not get into conflict with the main demand of socialism, the liquidation of private expropriation. Nevertheless it is not easy for the government to take an unambiguous stand, partly because if it adopted this policy it would have to face the established social structure. Furthermore, it is really difficult to take steps towards a new market system when the living standards are not rising and even their maintenance is a difficult task. In the 80s it will be unavoidable to draw away financial means from economic circulation, and it will not be easy for the center to

neutralize the effects of this by regulating the money supply. The withdrawal of circulating funds may lead to minor or major economic changes, local unemployment, and inflation.

Morita states that "Hungary's relative success so far cannot be attributed primarily to the 1968 reform . . . but rather to wise and reasonable maneuvers of economic management which have been accomplished by the cooperation between politicians and economists." I don't agree completely with this opinion. It is a fact that the cooperation between politicians and economists is very good. Economists played an important role in the work of the economic reforms. The results of the cooperation are especially apparent in this field. However, Hungary is one of the members of the CMEA, and CMEA integration had a positive effect on Hungarian economic development. Under the circumstances we cannot properly speak about Hungary as an isolated nation in Eastern Europe.

Finally, I would like to emphasize the role of agriculture in our economic development. It is well known that highly productive cooperatives, as well as household and complementary farms, are supplying the population with food. Agricultural production is a strong sector in our economy. Agricultural export is the most important source of our convertible currency receipts, and a further rapid increase in such export is expected in both rouble and dollar relations.

Discussion

Katsenelinboigen made some comments on Morita's report from a broader perspective to stimulate discussion. First, he stressed that the dichotomy "socialism versus capitalism" is not conducive to the true understanding of the wide variety of societies in the world. It leads us to reduce the spectrum of free societies to the term "capitalism," to which a certain pejorative meaning has been attached, and it inclines us to understand "socialism" *a priori* as a society which is to replace "capitalism." Second, Katsenelinboigen said that Morita and Sipos had been going in the wrong direction when discussing NEP. He agreed with Sipos that NEP had been far from capitalism, but his argument was completely different. The crucial point is that rival political parties and factions within the Communist party were prohibited by Lenin at precisely that moment when the introduction of NEP was announced at the Tenth Congress in 1921. He asserted that NEP had been far from capitalism if the latter was understood in a broader sense as a society with a pluralistic political system.

Third, he said that although many scholars including Morita have used a structural approach to considering the problem of divergence versus convergence, the importance of a functional approach — an approach from the point of view of the people's needs — has to be emphasized. The function of socio-economic systems is to satisfy the needs of the people. Katsenelinboigen then tried to explain the basis of these needs from the standpoint of human rights and from that of socio-

economic rights. In the former case the people say, "Don't take what we need from us." In the latter, they say, "Give us as much as possible of what we need." He contended that there are essential differences between a society based on the emphasis of human rights and a society constructed on the emphasis of socio-economic rights. These essential differences can be observed and examined from the functional point of view.

Katsenelinboigen continued that the true problem is whether both groups of rights are compatible or not, or to what extent they can coexist in a single system. He seemed to believe that the sphere of coexistence is very small and that coexistence is almost impossible. Therefore, he reminded us of the positive effect of the second law of thermodynamics in the history of technology. Many talented engineers had tried in vain to design and construct perpetual motion machines before the second law of thermodynamics was formulated in the nineteenth century. Consciousness of the impossibility of the coexistence of both groups of rights — a theorem of incompatibility of human rights and socio-economic rights — could play as important a role in the field of social engineering as the second law of thermodynamics did in the field of motor engineering.

Ocić commented that Katsenelinboigen's analogy of the second law of thermodynamics was too mechanical in this context to help us grasp the complicated relations between both groups of rights. He added that as far as the problem of impossibility was concerned no pure model can be fully realized in real societies. He suggested neoclassical planning models as an example. Katsenelinboigen replied that his impossibility problem was located on a logical level which was different from the one which Ocić had mentioned. Iwata criticized Katsenelinboigen's failure to mention the famous impossibility theorem proven by K. J. Arrow, which can be interpreted as demonstrating that there are inescapable contradictions even within the fundamental set of human rights. He suggested that the implications of this are as serious for social scientists as Katsenelinboigen's proposition. Katsenelinboigen's response was that according to his interpretation Arrow's theorem had to be understood as being connected primarily with the problem of democratic procedures, to which his impossibility proposition could not be reduced.

Besançon also took part in the discussion, saying that the problem raised by Katsenelinboigen is interesting but cannot be solved only on the technical and scientific level. This had been discussed by Tao philosophers in ancient China and by classical Greek philosophers. His second remark was related to the dichotomy of capitalism and socialism. He argued that this dichotomy had to do not with reality but with ideology because, on the one hand, the Soviet Union, which is usually regarded as an example of a socialist society, is not a living organism which ought to be called a society but a mere set of political controls on the population through a lot of apparatuses like police, education, state enterprises and so on. On the other hand, the societies which are called capitalist are nothing but societies. He emphasized that this dichotomy is comparable only to the notorious Nazi dichotomy of Aryans and Jews. Finally he made a play on words as follows: "We cannot speak of the political economy of socialism in the same sense as we speak of

the political economy of capitalism, because in the Soviet Union there is no "oikos," no "nomos," no "polis." Ocić chimed in "But there is a police."

Yoshino made a methodological comment that such pair-based analytical concepts as state ownership-market, equality-philanthropism, and controllability-efficiency are so strongly connected with each other that any two pairs cannot be taken out to be drawn separately on two-dimensional planes. Morita answered that, of course, he knew how complex the mutual relations of the three pairs of concepts are but, as his figures show, the difficulty can be skirted.

Kuboniwa asked what was meant by the "alleged perfectly competitive society" which was put at the 100 percent point on the equality axis in Figure 4-7. In the same figure an "ideal Communist society" was defined as a society of 100 percent equality. Kuboniwa could not understand in what sense Morita considered both a perfect market society and a perfect Communist society to be societies of 100 percent equality. He asked what criteria of equality Morita had used. Morita replied that the term "alleged perfectly competitive society" was used to denote the market mechanism in standard economics. Kuboniwa was not satisfied with this answer because, he said, the neoclassical concept of a purely competitive mechanism had nothing to do with the problem of equality or inequality of wealth distribution.

Iwata warned Morita against using imaginative graphs without theoretical foundations to express his thoughts. He pointed out that some of his ideas such as "failure of socialization," "illusion of control," and "failure of central control" can be explained deductively using traditional tools like convex production sets, indifference curves, and isoquant curves, without relying on vague ways of drawing imaginary graphs.