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The market does not spontaneously generate democratic or participatory economic institutions. This book asks whether a modern, efficient economy can be rendered democratically accountable and, if so, what strategic changes might be required to regulate the market-mediated interaction of economic agents. The contributors bring contemporary microeconomic theory to bear on a range of related issues, including the relationship between democratic firms and efficiency in market economies; incentives and the relative merits of various forms of internal democratic decision-making; and the effects of democratically accountable firms on innovation, saving, investment, and on the informational and disciplining aspects of markets. Various approaches to the study of economic interaction (game theory, transactions' cost analysis, social choice theory, rent-seeking, etc.) are considered in an attempt to understand the relationship between power and efficiency in market economies.

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Markets and democracy: participation, accountability and efficiency

Edited by

SAMUEL BOWLES

Department of Economics,
University of Massachusetts, Amherst

HERBERT GINTIS

Department of Economics,
University of Massachusetts, Amherst

and

BO GUSTAFSSON

Department of Economic History, University of Uppsala
and Director, Swedish Collegium for Advanced Studies in Social Sciences

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Preface

If it were not for the hope that a scientific study of men's social actions may lead, not necessarily directly or immediately, but at some time and in some way, to practical results in social improvement, not a few students of these actions would regard the time devoted to their study as time misspent. (A. C. Pigou, *The Economics of Welfare*, 1932)

The contributions to this volume encompass a wide range of subjects pertaining to the analysis, understanding and evaluation of economic systems in regard to their structural as well as to their behavioral and evolutionary aspects: capitalism, socialism, institutions, rules, ownership, power, participation, agency, incentives, conflict, cooperation, productivity, and investment behavior. But it seems to me that the underlying common denominator is somehow related to the quest for an economic régime that is able to bring about an acceptable trade-off between efficiency and participation (democracy) in modern society. It may be held that this quest has seemingly been removed from the agenda as a consequence of the decline and fall of socialism in the world. But such a conclusion would certainly be premature, and for several reasons. In the first place, it is debatable whether the socioeconomic system in Eastern Europe had anything more in common with traditional images of socialism than collective ownership of the means of production and planning. Even these two attributes were very peculiarly designed in so far as the collective ownership implied, on the one hand, an almost total absence of links between individual effort and individual reward and, on the other, the rewards of collective effort were, to a great extent, appropriated by a totalitarian élite; while planning in effect had abolished all horizontal (market) relations between economic agents and was excessively centralized. Secondly, the historical conditions (economic development level, political culture, etc.) were so unfavorable for success that the attempt to skip capitalism and democracy was doomed to fail from the very start, a point which was made abundantly clear by prominent critics of Bolshevism even before the Revolution (by Plekhanov and others). Still, the demise of dictatorial state socialism in Eastern Europe has exposed socialist ambitions in general, and certain Marxist tenets in particular, to a rough test that hopefully has prepared the ground for a thorough reconsideration of the conditions for a viable modern economic system. One of those conditions is certainly the existence of markets for labor as well as for means of production and consumption, not only because of the information carrying capacity of markets but also, and more important, because of markets' capacity to structure incentives and cater for social needs

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(two points which were underestimated or even neglected in the early market-socialist tradition). Another condition is the existence of well-functioning property rights (private, cooperative and social) that permit economic agents to capture rewards from their efforts and thus give them incentives to make rational decisions and permit long-run time horizons in economic action. A third condition is that a viable modern economic system needs not only enterprises but also entrepreneurs, who are willing, capable and motivated to create new combinations (innovations) and not just react "correctly" to given information; without such entrepreneurs any economic system will at best remain stationary. A fourth condition is that a collectivism that goes too far and encroaches on fundamental individual interests is self-defeating and gives rise to extreme ego-centered behavior; from which it seems to follow that there must always be some appropriate mix of individual and collective decision-making in an efficient economic system. A final condition is that if collectivism (socialism) has a future, it must have some tangible positive importance in the everyday life of the individual members of society.

These considerations, as well as other, more far-reaching ones, have motivated some people to conclude that modern capitalism does after all represent the best possible option, particularly with regard to efficiency and participation. Since capitalism is outcompeting alternative economic régimes it must, so one argument goes, surely meet fundamental human requirements better than those alternative régimes. In this social-Darwinist argument, existence is taken as an indication of superiority. This may be true as far as it goes, but it does not go very far. It does not demonstrate any necessary and sufficient conditions for the assumed superiority; it implicitly assumes that capitalism as an economic system represents not only an *optimum optimorum* but also the final stage of human economic performance; and it sidesteps those problematic aspects of the capitalist system which now and again give rise to criticism as well as plans to reform it: first and foremost persistent unemployment; inequalities of wealth, income and power; a deficient supply of basic social services; and promotion of competitive as opposed to cooperative motives in the operation of society. If the argument includes a plea for some form of far-reaching welfare capitalism, which modifies negative effects and supplements what is missing, it carries much more force and cannot easily be disposed of. Still, even the most advanced cases of welfare capitalism, such as the Scandinavian varieties, have not solved the problems generated by ownership and control of firms leading to differences in capacities and opportunities for participating in those firms as well as in society (wealth, status, control over information, etc.). Furthermore, the experiences of the 1980s seem to show that the achievements of the welfare society are not permanent.

If we take a very long view, it may be maintained that modern history has been characterized by the parallel growth of democracy and efficient capitalism and this observation is not entirely wrong. In comparison with earlier modes of production capitalism did indeed foster a mobilization of initiative and participation on a mass scale and notwithstanding setbacks, democracy has

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increasingly gained ground since it was ushered in by the French and the American Revolutions. From this some people have concluded that democracy is caused by capitalism and that democracy cannot exist without a capitalist economic system. But correlation is not causation. It may well be that democracy has been victorious not because of but in spite of capitalism (defined as a market economy combined with wage labor) and that democracy and capitalism in fact are essentially incompatible. This was the traditional conservative view as expressed by Justice Story in the early nineteenth-century and almost echoed verbatim in the twentieth-century by the socialist Wigforss, Minister of Finance and architect of the Swedish welfare state, who wrote:

> General suffrage is incompatible with a society divided into a small class of property owners and a large class of non-owners. Either the rich and the property owners will abolish the general suffrage; or the poor, by means of the suffrage, will appropriate a share of the wealth.

The fact that capitalist economic régimes have coexisted with very many different kinds of non-democratic political régimes should also make us careful in hypothesizing any necessary link between capitalism and democracy.

Ideally we are in search of an economic system, which combines the flexibility and vitality of modern capitalism with full employment, extensive participation in decision-making, a more egalitarian distribution of income and wealth in firms, and promotion of values oriented toward cooperation and solidarity between people. It may be argued that it is impossible to devise an economic system capable of meeting these requirements simultaneously, either because the goals are inherently contradictory (competition and innovative activity versus cooperation and solidarity, flexibility and change versus full employment, etc.); because some of them are contrary to "human nature as we know it" (Frank Knight, 1921); or because self-interest is the only reliable motivation in mass cooperation (Mandeville's dichotomy of "private vices–public benefits"). At the same time it is clear that different sub-sets of the social system do interact and that, in this interaction, the economic system occupies a crucial role. A society based on big private corporations owned by an élite fosters sets of behavior and values that differ from those found in a society based on some kind of generalized and collective property ownership. With this in mind, the task of devising an economic system capable of meeting several contradictory requirements remains. But at the same time it reduces itself to more manageable proportions and opens up a possibility of alternative solutions depending upon what precisely we want to achieve and what we want to take as constraints on the solution. It may well be, as suggested by several contributions to this volume, that labor-managed firms could become the core structure in the search for a superior solution to the trade-off between democracy and efficiency in the economic system. At the same time these contributions make abundantly clear that this institution does not represent a "magic wand" capable of solving all problems. On the one hand such firms may transform the relationship between labor and capital to the benefit of labor; they may extend democracy to one of the most important spheres of

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human existence – the working life; they may make income and wealth more egalitarian; they may foster values of cooperation and solidarity; and they may even be more productive than capitalist firms. On the other hand, they may be more reluctant to innovate and more resistant to structural change; they may be less inclined to make risky and long-term investments; and they may be less flexible in their reactions to market signals than capitalist firms. Other aspects of a labor-managed economy are still not much discussed. Will there be big differences in income and wealth levels between firms? Can we take for granted that the transformation of large sections of the working population into competitive entrepreneurs will not extend rather than diminish values focused on competition? And we know next to nothing about the stability properties of such a system.

Nonetheless, the contributions to this volume shed new and important light on many key aspects of labor-managed firms. Other contributions provide frames of reference for analyzing not only such firms but also economic systems in general. On the basis of this, Samuel Bowles and Herbert Gintis have made a bold attempt to outline the elements of a post-Walrasian political economy, which not only represents a challenge to the substance of the standard neoclassical model but also "appears likely to foster some fundamental rethinking about the structure of economic theory itself and its relationship to empirical studies and to neighboring disciplines."

It is up to the readers of this volume to judge if, how and to what extent its contributors have succeeded in this attempt. For my part it is quite clear that the thrust of argument in this volume is wholly in line with the objective of SCASSS, namely to promote advanced interdisciplinary study in new and progressing areas of social science research.

This volume has been made possible thanks to the generous financial support afforded the SCASSS research program, "Property Rights, Organizational Forms and Economic Behavior," by the Tercenary Fund of the National Bank of Sweden.

BO GUSTAFSSON
Director of the Swedish Collegium for Advanced Study in Social Sciences (SCASSS)

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