Economic systems theory and general equilibrium theory

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The present age has placed a new question before economics: how should economic systems be deliberately shaped and planned in detail, and their functional mechanism developed? The author states that economics is not yet capable of providing an answer based on a proven theory. This lack must be made up for by "economic systems theory". There has existed hitherto a single established school of economic systems: the general equilibrium theory. Here the author expounds some theorems that criticize this theory.

– The assumption that certain economic phenomena are constant over time prevents the examination of change, though this is a fundamental problem of life.

– "Optimality" and "maximization" are not good assumptions for describing the activity and actual behaviour of complex economic organizations, since they hide the diverse, real motive powers motivating enterprise activity.

– The assumption of convexity excludes the case of economies of scale, although this is a group of phenomena of fundamental importance to concentration.

– The general equilibrium theory builds on a simple system of control and signals because it neglects uncertainty. Yet uncertainty exists in reality, and so information must be multiple in the interest of reliable control.

– It is claimed that better conclusions would be reached if the creative efforts of whole generations of economists to develop a systems theory were more suited to describing the functioning of economic systems in a better and more realistic way.

Bureaucratic and market coordination

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Here the author has two goals. One is to raise some theoretical ideas and outline an analytical apparatus suited to this group of questions. The other is to address the problems of economic reform in terms of the subject-matter stated in the title. The study is a partial outcome of lengthy research. Restrictions on length mean the author must cover large, complex questions very briefly. More detailed expressions of these will appear in later publications.

In this inaugural lecture at the Hungarian Academy of Sciences the author distinguishes four mechanisms of coordination conceived as the regulatory basis for any kind of transformational and transactional process: bureucratic, market, ethical and

aggressive coordination. This classification is distinct from the usual one in literature in classifying the control procedures, not the individual organization(s), in the sense that direct control of every microprocess is performed by one of the four basic forms or by some combination of them.

From analysis of a few characteristic indicators the author reaches the conclusion that the scope of bureaucratic regulation in Hungary (despite the general stand against bureaucracy) is at best stagnating, rather than increasing. There are four causes behind this tenacity of bureaucracy: 1. Bureaucracy is inclined to complement the general regulations with ever more concrete and detailed rules. 2. While bureaucracy is confronted in one area, the point of emphasis of its activity shifts frequently to other areas. 3. If there is a shortage, and insofar as market coordination does not fulfil its task of adjusting supply and demand to each other, bureaucratic coordination becomes inevitable. 4. Those with power within the bureaucratic system and those enjoying its advantages fight to retain their positions.

The author challenges the view that in Hungary's society and economy both market and bureaucratic coordination should be relegated and the role of ethical norms increased. For the latter is unsuited to becoming the main road to coordination in modern societies. The author takes an unambiguous stand for expanding the scope of market coordination – and in doing so urges the development of the Hungarian system of control towards more indirect, "more market" directions. But he sees that externalities, transaction costs and problems related to just income distribution and to monopolies, make the survival of bureaucratic regulation inescapable in some areas, of course with far smaller scope than is the case today.

The principles of privatisation in Eastern Europe

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The paper reviews values and decision criteria to be used in privatisation. The main dimensions are 1. sociological, the long-term historical perspective, 2. economic, and within it requirements calling for incentives to efficient production, security of ownership, and fiscal and monetary considerations, 3. political, and 4. distributive-ethical. Under the last is treated the principle of restitution and justice, and also equality and equity.

The paper covers the role of government and the evolutionary character of the privatisation process, and reviews the forms of property. It stresses the importance of private persons as proprietors and touches on the types included. It deals with employee property and the various forms of institutional property, including the role of anonymous share ownership. It analyses alternatives to free distribution of state property and the problems of ownership by foreigners. Finally the author presents his view on the speed of the privatisation process.

The system paradigm

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The notion of a paradigm stems originally from T. S. Kuhn and was inspired by the history of the natural sciences. The article begins by explaining the

interpretation of the notion as used in the social sciences. Here a new paradigm need not necessarily replace an earlier one: several paradigms can apply side by side. The milestones in the concept are the works of Marx, Mises, Hayek, Polányi, Schumpeter and Eucken. Although the list is somewhat varied in the philosophies and political stands of its authors, what they share is the "systemic approach". They discuss not some detail of the economy, but the system as a whole; not just the economy, but the political, ideological and societal dimensions, paying particular heed to interactions among all the spheres. It is a great examination task for the system paradigm to research the post-socialist transition. It is indispensable to it in its explanatory power and cannot be replaced by any other paradigm. Yet its users have frequently made grave errors in their forecasts (as have those using other paradigms). The predictive power of the system paradigm is restricted, which warns its users to be cautious.

The soft budget constraint I–II
With co-authors Eric Maskin and Gérard Roland

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The authors set out to clarify the notion of a soft budget constraint, which is widely used in analysing socialist, transitional and market economies alike. The interpretation in the study is broad enough to embrace most existing approaches to soft budget-constraint phenomena and classifies the causes and consequences of these (Part I). In the light of this, the study then reviews the theoretical literature on the subject and compares it with work in other dynamic commitment problems in economics (Part II).

Innovation and dynamism
The reciprocal effect between systems and technical advance

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Literature on post-socialist transformation usually deals with its political, economic and social sides, despite the important changes in the field of technical advance in the last twenty years. One of capitalism's main virtues is the strong incentive it gives to dynamism, enterprise and the innovation process. Every revolutionary new product for civilian use has arisen from the capitalist system. The socialist system managed at most to develop new military products. The article gauges how far this radical difference can be explained by the innate tendencies and underlying attributes of the two systems. These new products, for instance, the sphere of information and communications deriving from the computer, the mobile phone and the internet, have transformed our daily lives. While many see all these as favourable changes, fewer discern the causal relation between the capitalist system and rapid technical progress. Nor does the usual syllabus of microeconomics enlighten students on this important virtue of capitalism, which is also emphasized inadequately in the statements of leading politicians.