

BOOK REVIEW

CAPITALISM, SOCIALISM AND PROPERTY RIGHTS: WHY MARKET SOCIALISM CANNOT SUBSTITUTE THE MARKET

MATEUSZ MACHAJ

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PAUL F. CWIK*

The idea of socialism has a long history that can be traced back to the earliest writings on political economy. Over time, the idea of socialism and its applications have changed. In the 20th century, the world witnessed several types of socialism: the communist socialism of Russia, the nationalist socialism of Italy and Germany, and the democratic socialism in the post-World War II western nations. Despite the many manifestations of socialism, they all have a common root—one that was identified by Karl Marx. This commonality is the abolition of private property, at least in the means of production.

In the aftermath of the First World War, many intellectuals argued communism was the path to follow, and the new government in

* Paul F. Cwik (pcwik@umo.edu) is BB&T Professor of Economics and Finance at the University of Mount Olive.



Russia was leading the way. In 1920, Mises challenged this emerging orthodoxy and explained that without the ownership of the means of production, there would be no markets. Without markets, there are no prices. Without prices, there is no mechanism by which to calculate what is economically efficient. Mises expanded his “Economic Calculation Argument” in his 1922 book *Socialism*.

While acknowledging Mises’s insight for the need to rationally allocate resources through a system that at least resembled prices, most economists disagreed with Mises’s conclusion that such a problem was insurmountable. They rejected the idea that private property and markets were necessary for a rational economic order. The professional economists believed that their expertise would solve the calculation problem. Interestingly, their solutions were not consistent. Some thought that a central planning bureau alone would lead society to prosperity. Other economists admitted that the limited use of markets was necessary, but only in consumer goods. The criticism of Mises’s argument lasted throughout the 20th century until the Communist bloc collapsed. When the Berlin Wall fell and the USSR imploded, the economics profession was woefully unprepared to help the former communist countries transition to free market capitalism.

It is here that Machaj’s book, *Capitalism, Socialism and Property Rights*, takes center stage. Published in 2018, and at 173 pages (plus extensive footnotes and index), the book is straightforward. The English translation from the original Polish, by Kacper Potocki, flowed smoothly.

It is appropriate that this book comes from a former communist country. The author’s direct experience with a centrally planned economy and the subsequent transition to a market-based economy yields insights that other economists would never consider. For example, Machaj makes an important observation about something very simple—how inventories are dealt with in a centrally planned system. Economists, like US economist Fred Taylor and the communist Polish economist Oskar Lange (both are covered in the book), agreed that, under socialism, consumer goods markets were necessary to obtain consumers’ preferences. Shortages and surpluses of consumers’ goods would signal to the central planners the direction of production. Once it was

discovered what consumers wanted, they asserted that central planning would produce superior outcomes. However, under socialism, only empty shelves constitute a situation where there is no surplus. How are inventories factored into the plan? Suppose that a shop sells hammers. Hammers are durable goods and can sit on the shelf for quite a while before being sold. *How* will a shop manager know if there is a surplus of hammers? Should the manager lower the price to clear the shelves? As Machaj states, "We can see why socialism creates an economy of shortages. If the central planners assume that everything has to be used up immediately, lest it be considered a surplus, all goods will be swiftly consumed. A material approach based on counting the amount of goods in storage leads to economic catastrophe. The result is empty shelves, as the history of real socialism amply shows." (p. 32.) Production under socialism must either be for immediate use, or if there is a level of inventory, it would be completely arbitrary and wastefully uneconomic. Having lived through the era of central planning, Machaj is able to provide practical insights that Western economists simply overlooked.

In addition to such a gem, Machaj's book makes three important points. The first centers on the discussion on how the socialist economists, who thought that a market could be mimicked or limited to only consumer goods, were wrong. The second is that the neoclassical economists, who used the model of perfect competition and thought solving the right set of equations could produce equilibrium, were also wrong. And the third, and most important, point is Machaj's claim that Mises's approach was too narrowly focused on economics and not broad enough for the legal and ethical implications of property rights. As a consequence, Mises's argument was an insufficient guide for the former communist countries to reestablish market economies.

Machaj deals with the first two points in his second and third chapters. The rest of the book, and this review, centers on this the third point. Machaj argues that Mises's calculation argument was too narrowly focused on economic theory. He does not dispute the validity of Mises's position. What he is arguing is that if the calculation argument was a subset of the larger argument on the necessity of private property, then the countries transitioning to market-based economies would have had more success. Machaj

explicitly argues that the ownership of property is the foundation of a free economy, the law, and ultimately a prosperous society.

Machaj's foundation is the idea of self-ownership, which is not a unique starting point. Self-ownership is foundational for philosophers such as John Locke and Ayn Rand, as well as Austrian economists such as Murray Rothbard and Hans-Hermann Hoppe. Self-ownership means that the individual has rights that are superior to the collective and the state. The individual is sovereign and, as long as one does not aggress upon another, these rights must be respected. The idea of self-ownership can be extended to ownership over material items, thereby deriving the idea of property rights. The analysis can be further extended to the interaction between individuals, as such determining that just and legal activities are those generated through freely agreed upon contracts. Thus starting with the individual, Machaj is able to build his concept of a free and just society.

As Mises points out, property rights lead to markets, prices, and economic calculation. However, property rights are able to do much more. Machaj emphasizes that a key feature of a right to property is the ability to exclude. As Machaj states, "The most important point in our inquiries is the following: property laws essentially define relations between the owner and other people, not relations between people and things." (p. 8.) Excluding others from using a good means the non-use of a resource. The non-use of a resource is the basis for savings and economic growth. A tree becomes more useful as it grows. If the tree is unowned, then anyone can come along and chop it down. Preventing others from using the tree allows the tree to grow and become more useful in the future. Private property rights exclude non-owners from cutting down the tree.

For a nation seeking freedom, Machaj contends that the economic calculation argument is too narrow. If the question were merely one of ownership, then why not allow the workers to collectively own the businesses? Why should the government not intervene in the economy to redress economic iniquities? Why should politicians not regulate the market to achieve politically desired goals? The answers of economic efficiency is not something that sways the minds of many people, and because it is an abstract concept, it does not yield a strong adherence by the general population. Machaj shows that

economic efficiency is only one benefit to a nation with a legal code based on a foundation of strong property rights. By casting the goal of a free society as one with strong property rights, and not as a society with efficient economic calculation, he argues that the adherence to a free society will be more deeply and robustly entrenched.

One of the key features of a centrally planned economy is that society is organized through a bureaucracy. Machaj's book compares the bureaucrat with the entrepreneur. It explores the nature of socialism, imperialism, monopolization (all stemming from systems that reject or curtail private property rights) and contrasts them with the dynamics of the market process. Following Mises's lead, Machaj shows that "Calculation is the driving force behind the economy and leads to changes in the structure of ownership and in the entrepreneurial division of labour. The distribution of ownership, the entrepreneurial division of labour and calculation are three inseparable fundamental elements of monetary economy." (p. 110.) Machaj builds upon Mises's analysis and rightly emphasizes the social function of bankruptcy. As Machaj states, "Bankruptcy means the reallocation of the resources from the entrepreneur who made mistakes to more effective entrepreneurs." (p. 110.)

As with all scholarly works, there are points to debate and discuss. For example, I disagree with Machaj's theory of interest. To me it seems that he is positing a variant of Turgot's fructification theory. Nevertheless, this point is not central to his argument and does not detract from any other issue presented.

Overall, the book provides a unique contribution to economics in that it argues that Mises was too narrowly focused upon items of economic theory rather than a broader appeal to a system of property rights. By broadening the perspective beyond the economic and into the legal and moral realms, one sets the foundations for policies of nations transitioning away from socialism in any of its forms.