BOTOS KATALIN: WHERE IS THE FLAGSHIP GOING?

If somebody raises the question what the greatest change was in the world in the 1990s, nine out of ten persons in Middle Europe will answer it like this: It was the collapse of communism.

Fifteen years ago the processes which disrupted the Soviet empire and replaced the socialist system with restored capitalism began to emerge. Through democratic elections the political systems became multiparty democracies; private property was declared to be the basis of economy. However, actually, most of the means of production were state-owned in East-Central Europe. Therefore, a grand-scale of privatization process was launched in the formerly Soviet-dominated territories. Those who might hesitate were criticized and were accused of the intent to restore socialism.

The moderately progressive experts who did not want to eliminate the state's role-taking entirely were denounced retrograde. The owners of political power were accused that they wanted to have a hold on a part of the means of production and the large systems of redistribution in order that they would be able to intervene in economic affairs, probably, for the benefit of their own political supporters. You could hardly hear of the fact that those who urged on changes were not uninterested in the latter either and economic liberalism favoured definite groups of interest, i.e. people with inside knowledge and foreign owners.

The transition - as this period usually has been called - absorbed all intellectual energy. We hardly paid attention *where we had been going to*.

Anyhow, capitalism is not a uniform system at all. We are inclined to regard the events which have taken place in our hemisphere and region as being of great importance in world history - *as they are,* *indeed* - but we forget about the fact that *it is not only we that have changed.* There have been enormous changes in the world over the past half-a-century. And what is more important, there was another radical change just before the millenium.

The impact of the Great Depression

The standpoints of the classics of marxism almost proved to be true. In the early 1930s the economy of Europe was in ruins. Italians established the large state holding, IRI for financing the bankrupt companies what, eventually, led to the nationalization of a significant part of Italian economy. The English and French carried out nationalization to a greater extent after World War II and most of the colonies liberated sought to catch up with the help of state property and the state role-taking in economy. In the leading industrial great power of the world, too, the contradictions became so accentuated and the crisis of overproduction resulted in such a recession that tension in society had reached fever heat. As a contemporary, László Cs. Szabó said in his work on Franklin Delano Roosevelt what a great shock it had been for American citizens when *the democratic power*, the social system of which had been an example for the world, *gave order to fire at veteran protesters.* Americans came into conflict with themselves. Solution had to be found to the growing deterioration of social morals which had been induced by the unbridled speculation on the Exchange. (Even the President of the U.S. Exchange who was a Harvard graduate became involved in a fishy business!!!) Samuel Insull, the talented manager of the Edison Works built a pyramid-like empire of companies which ruined hundreds of thousands of small shareholders after the 'exchange fever' dropped. The way out of this crisis was setting-up the institutions of state regulation and the use of budgetary policy. In forms of diversity state ownership, state regulation and boom regulation became general in the developed world. The German economy followed a special way with the establishment of a social market economy in which the nationalization of the competitive sector did not take place but the state role-taking became immense in infrastructure, social policy and regulation. The new economic theories which emphasized a more vital role of the state seemed to conquer the leading capitalist economies and societies, as President Nixon said in a quarter of a century later: 'We all are Keynesians.' But by the time he uttered it, the period had been over. The monetarism of Friedman and liberalism of Hayek were on the way to conquer the 'heights of management'. Truly, the adherents of welfare capitalism shared the successes half and half with the liberals in 1974 because Gunnar Myrdal, the socially sensisitve Swedish economist and Alfred Hayek, the Austrian social scientist who stood for unconstrained freedom shared the Nobel Prize in economics. But Hannibal was 'ante portas'. Soon there came Thatcher's take-over of power in Great Britain and Ronald Reagan won presidency in the USA. The pushing back of the state became the target of formal economic policy since state intervention of a significant degree seemed not to be the guarantor of welfare anymore but the source of stagflation.

Privatization, deregulation and liberalization started everywhere. The 'left-over' of the Great Depression was intended to be swept out and people wished to return to the principles of classical capitalism: the full freedom of undertaking and the unrestricted flow of production factors.

It was not extraordinary at all that Eastern Europe took this way, too, after 1989. Truly, here there were much deeper changes since not only the democratization of economy but that of the whole social system was aimed at.

It can be stated that in the turbulent 1990s there were parallel economic revolutions in the eastern and western parts of the world the resultant of which showed to the same direction even if causes were somewhat different. Both wanted to push the state back and make private economy more competitive. The difference was that the institutional background of all this had to be established again in Eastern Europe that was lagging behind in competition to a great extent because the communist planned economy made the institutions of the market wither. And if we copy a system, let us copy the best one, i.e. the structure of the highly successful American economy.

However, we did not know much about what changes took place in the flagship of capitalism, i.e. in the USA in the 1990s, *what capitalism was brought about by the processes occurring parallel with our ones in the U.S. economic and social system which we wished to resemble* since its success seemed to be obvious. What is today's capitalism like, indeed? What is the USA to which we would intend to approach like?

Chatting on the surface

What is the modern USA like? With one word we may say: it is *successful*. From bird's eye view, from a great distance it seems to be like that and this can be proven by measurable indicators, without any doubt. The USA faced new technological challenges with success. It is in the forefront of framing the new economic structure: 14% of the total of manpower works in processing industry. The proportion of services - and within this, that of the up-to-date science-based services - is the highest in the sectorial structure. Its per capita GDP is one-and-a half times as high as those of Europe and Japan. Its employment indices are far more favourable than those of Europe; the state share in GDP is considerably lower than those in the other two power centres. The burdens of taxes and contributions which are so important from the aspect of competitiveness are smaller. The USA succeeded in overcoming the recession phenomena of the 1980s and had a continuous growth almost over two decades. The nature of capitalism seemed to change: cyclical fluctuations had come to end. Truly enough, U.S. economy had some seamy sides as well, namely: significant budgetary deficits, accumulated debts and chronic deficiency of the balance of payments. But since difficulties of financing did not hamper sustainable growth - there were a great many of dollars outside the USA which ought to find secure investments - the outsider was inclined to forget the aforesaid seamy sides. However, these questions were also on the agenda in domestic economic policy. It is no wonder that the Clinton administration aimed at the reduction of budgetary deficit and achieved that goal, too. It is also true that this melted away in a second during the Bush administration and a great many of macroeconomists are concerned with the problem of deficit again today.

The development of fantastic nineties stopped short and the illusions based on them vanished due to the slackening of the momentum of 'IT business'. The hope that there would not be crises anymore since more up-to-date monitoring of stocks would be rendered possible by modern technology and thus, cyclical overproduction could be hampered faded away. U.S. economy fell into deep recession accompanied by scandals.

Silence in depth

Technologial development caused a historical turning in the world: the fundamentally labour-based economy became capital and labour-based. After the New Deal the USA moved to a greater degree of equality in property and income. In one of his papers published in 1935 J.A. Ryan traced three major deficiencies of U.S. capitalism, namely, wages were insufficient to make a living; there were great differences in property between the poor and the rich and there was a high concentration of capital. He considered the latter the greatest problem, stating that it would jeopardize the stability of the whole system. (Alford-Naughton, p. 277). In 1936 Hilaire Belloc pointed out if economic freedom was accepted, the aim should be the restoration of property. Political and economic reforms which disperse property increasingly to the extent while the number of owners in possession of proper quantities of the means of production are high enough to determine the image of society should be elaborated. (Alford-Naughton, p. 285). Only a person with property may state that he is relatively free since he has certain financial background which makes it possible for him not to 'sell himself' under any and dictated conditions. Otherwise, the bargaining position of capital will be stronger and exploitation will be increasing, i.e. the distribution of new value will always occur to the benefit of the capital. But from the 1970s on there have been significant changes. Incomes began to differentiate. This process slowed down a little in the Clinton era but later it continued. From the economic growth of the past decade, practially, only the upper 5% of families have had a share - stated Robert Freeman in 2004. Since the early 1970s the income of the richest 1% has doubled while the family and household incomes of the 80% of the population have been stagnant or decreased. According to the figures of the Office of Labour the average hourly wage, taking inflation into account, shrank from $ 8 and 3 cents to $ 7 and 40 cents between 1970 and 1994. In the 1990s productivity increased by 7% but wages and benefits did only by 1%. According to J. Annable, the economist of the First National Bank of Chicago, they witnessed it that the field of income redistribution shifted from labour to capital. (Alford, Naughton, pp.276-278). Since 1973 the U.S. poor have become poorer. Here the income differences are not so great as they are in Latin America but much greater than in East-Asia or in European democracies. (Stiglitz, 2004. p. 34) Who is poor in the rich USA is poorer due to the differentiation of incomes than those in the group of European countries which have a GDP 50% lower on the average than the USA. The cause and explanation of this can be attributed, among others, to the relative underdevelopment of American social network and the insufficient structure of social securities and health care which fail to cover the whole population. Between 1973 and 1994 the proportion of those covered by pension funds dropped from 62% to 46%... According to the international comparative studies of the Pázmány Péter Catholic University the efficiency of the system of U.S. health institutions leaves much to be desired. It is really shocking *how low the efficiency of health care* is in the most advanced economy of the world: the expenses spent on this are nearly the one-seventh of GDP, however, this system produces a state of health worse on the average than the systems of countries which spend half or one-third proportionately to their GDP on this purpose. What is remarkable, this sphere has been organized by the partial or full participation of the state in the other developed countries, while in the USA it has been organized on market basis decisively.

Is it sure this is the example to be followed by all countries of the world?

From the macroeconomic data it can be seen that people in the USA work more than in Europe. In 1992 an average American worked one month more in a year than a European, although in 1973 their work burdens were approximately the same. Thus, we can say that we need not long for the average U.S. living standard here, 'East to Eden', but our activity rate should be raised and we must work more intensively. (By the way, in the USA this is also compelled by the fact that can be experienced with social security: if somebody loses his job, practically, he is unable to pay for the expensive private insurance and thus, he will not have any benefits or allowances). It is true that the lower burden of contributions - what may be smaller than in Europe due to the lower level of compulsory contribution of social security - is favourable for American entrepreneurs; it makes them more competitive - but is it good for employees, esp. if they have lost their jobs? American people achieve higher average living standard but a lower quality of life. Is it an objective for Europe, too? Or probably, is it a constraint owing to globalization?

However, let us consider the widening differences of wages more thoroughly. Here not only the differences themselves are in question, since the salaries of top managers jumped to incredible peaks. According to the Wall Steet Journal 1996. No. April ll. the salaries of managers grew four times as much as did the average wages but their growth was even treble as fast as that of company profits.

Here there is something new, something more what is worth considering.

Whose is the USA?

W. Greider said it would be time to pose the question what had always be unanswered by modern liberalism: Whose is the USA? (Alford-Naughton, p. 278.)

The endeavour to make an ever greater number of U.S. citizens a proprietor became reality by the turn of the century: more than 50% of the population had acquired shares. The 'people's capitalism was realized through various institutional forms: employee's program for part-ownership, pensions funds investing in shares and, perhaps, direct purchase of shares. There are estimates according to which shareholdings cover not more than 30% of the population. Anyhow, it is true that the scope of owners has been enlarged, but it does not mean that each of the owners may exert the same influence on his property since small shareholders only endure or enjoy the value change of their shares. Moreover, the developments of the 1990s just strengthened what the outstanding economist Schumpeter referred to in the 1930s and so did Galbraith in the

1950s and 1960s, namely: the real owners of modern age are managers. At least, they exercise the strategic rights of disposal that are the very essence of ownership. Naturally, in the modern form of a joint-stock company to exercising the aforesaid rights the approval of the community of owners, i.e. the general assembly is necessitated but in a significant part of the cases the general assembly gives a nod of assent to the proposals of management. As long as the value of shares is proper or perhaps is increasing, management need not worry: in the boom on the Exchange owners were generous at the general assembly and approved the high payment of the CEO, the top-managers. When the option of shares was introduced, it was emphasized that everybody would benefit from the strengthening of ownership feeling; the old shareholders would benefit more because the managers who turned to be owners would be more interested in the success of the company what is, let us add to it, does not depend only on them but on a team work as well. Yet, the company management had it approved that the payments of top-managers could be *even four or five hundred times higher than the average income*! American managers get multiple the sum of their European or Japanese counterparts. In Japan the salary of a managing diretor is 10-fold the average wage, in Great Britain it is 25-fold, in the USA it has climbed from 85-fold to 500-fold over the past decade.

And what made it possible? Practically, the external circumstances did it, namely: the economic boom and the rise of the quotation of shares assisted by several factors. They were as follows: the interestedness of the financial sector, the spread of the socalled creative book-keeping and the short-sighted approach of co-owners who thought that the growth of the 'bubble' was infinite and the boom would be an endless process, too. It did not disturbe them that managers became co-owners since they profited from that,too, owing to the rising quotations. However, since everything must come to an end once, the great American miracle was also finished spectacularly. The quotations of IT shares began to drop, the investments in information technology proved to be excessive. Even the most developed technology was unable to safeguard the gready human species from cyclical fluctuations. Many people lost much. *But the ownership structure of the company changed. Managers remained inside.* The value of a company may be stabilized at a realistic level but, in the meantime, the managers have aquired or have been able to acquire a significant influencing participation; it can be said - all this happened to the detriment of the small shareholders since, obviously, the value of the company will or can be maintained but that of the individual shares may decline as now it is spread among several owners.

Although it is worth while mentioning that the separation of the legal structures of actual management and control, too, plays a role in the realization of the above-mentioned possibilities, esp. if moral motives are pushed into the background by strong financial interests, because joint stock companies have board of directors, boards of supervision or socalled external directors responsible for control - but how do they get among the members of these boards? Generally, the management themselves make a proposal to these persons. In addition to prestige, these jobs are concomitant with significant benefits which would not be missed by the lucky nominee at all. Thus, they 'shut one of their eyes' not to see when, in extreme cases, the management have not only advantageous options of shares but special credits for themselves approved. The supervisors, external directors protect not the interests of shareholders but those of the managers and their own ones. Naturally, this is not always so spectacular like that, and in most of the cases - in the phase of the booming business cycle - it seems not to be in conflict with the shareholders' interests. Truth comes to light when the market position is deteriorating. But one may pose the question: How can this happen as joint stock companies have to have themselves audited? But, the independent auditors are also elected by the general assembly - on somebody's recommendations. And on whose ones? You may have 'three guesses'... Also, the auditors could not afford these highly profitable businesses to be passed until the audited data get very far from real facts - while, so to say, they are in no collision with professional aspetcs. Of course, departure from facts has already occurred long before but truth does not come to light until a downward trend in quotation of shares presents itself.

Conclusions

If we want to make a pointed remark, we may say that traditional capitalism in which there were employees and capitalists - may the theory have justified the existent conditions by the 'returns' of the production factors - was based on the exploitation of workers. This is why such a shortage of income that, finally, led to the crisis and overproduction in the 1930s emerged due to the wages reduced at microlevel. This is why since the publication of the Encyclic Rerum Novarum the message of the Catholic Church had taken, several times, a definite stand on a fair wage which should take into consideration the dignitiy of workers and his family circumstances; it should make possible for him to educate himself and to sustain his family. It has emphasized that this is why workers have the right to struggle through the organizations which safeguard their interests, and the state is obliged to give market participants an 'economic constitution' which would guarantee the fair distribution of incomes.

However, modern capitalism is not based on the only contradiction between the capitalist and the worker anymore. Under present conditions employees themselves may be shareholders in their own 'company' since there are such programs, too, or they keep their savings in other companies.

A great number of today's citizens are capitalists - even if to a lesser extent - and they are persons who earn wages or salaries at the same time. Thus *they are often deprived of the fair part of the value produced by them through a double channel.* If not the shares of their own company drop, they will lose through the decline of the value of shares owned by their pension funds. Millions of Americans invested their savings in shares with confidence in the 1990s and, at the turn of the millennium, $ 8500 billion 'disappeared' from the accounts of individual savings!!! This sum is one-third of the value saved in this type of form!!!

It can be said that the drops of exchange rate make only the paper profits blown up disappear and this is right and desirable, indeed. There will not be either more or less value than it has really been produced. Actually, every owner loses something but only that which he/she has never had.

This argumentation may be quoted but it is not the full truth. Besides losers *there are always winners, too, and they are typically the managers* who got bonuses by a fluke. Undoubtedly, the value of bonuses decreased, but still, it can be attributed to luck that, based on favourable trends, they obtained the co-owners' right from the other owners (from the general assembly) at all. Obviously, 'they have worked hard for it.' But a competent person knows well that the conditions of regulation, the concerted managerial, banking and auditorial interests and, the short-sighted approach of shareholders are the sources of the wealth of company managers which they acquired in the aforesaid way.

Before accusing me of the fact that this argumentation is a mere speculation, I would like to begin admitting that, basically, I relied on the latest book by J. Stiglitz entitled 'The Roaring Nighties' (2004). J. Stiglitz, the ex-vice president of the World

Bank, the ex-president of the Economic Advisory Body of the Clinton administration, professor of Stanford University and a Nobel Prize winner outlined the above-mentioned relationships - which can be observed even in our domestic circumstances as well.

Nobody is envious of the benefits of a manager's work - not at all, if there is a real work in the background. If trickery, the lack of regulation or the utter degeneration of morals can be traced behind managerial benefits, criticism should not be hidden under a bushel. We are responsible for our environment and our value orders transmitted to future generations. We may not stand for Wall Street as opposed to Silicon Valley - in order to cite Stiglitz again.

Society needs a more righteous and brotherly world. This is true for the U.S. society, so is it for the Hungarian one to a greater extent. We long for a capitalism of more human face - perhaps, it would not be called like that either - in which not cruel laws but labour and respect towards well-earned property prevail; in which the possession of property means to have responsibility for the common good; in which we make use of and not misuse our rights.

References

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