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CAPITALISM, SO LONELY (REVIEW OF CAPITALISM ALONE, BY BRANKO MILANOVIC)¹

CAPITALISMO, SOLO: EL FUTURO DEL SISTEMA QUE RIGE EL MUNDO

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Pablo Javier Mira*

Capitalism is now alone. A condition that should not be confused with success, triumph, or hegemony. Capitalism did not defeat an opponent, its main challenger just gave up. Seventy years ago, the fight between capitalism and socialism was not even close to end, and ten years before the fall of the Berlin Wall everyone would have predicted many more rounds to come. But then, all of a sudden, socialism threw in the towel and that was, according to the famous claim of Francis Fukuyama, the end of history.

Since the dissolution of the Soviet Union, however, the absence of competition made western capitalism relax in its duties. European developed economies, the so-called East Asia Tigers and the United States, all suffered crisis of unexpected magnitude. Meanwhile, some Latin American countries are still trapped in a middle-income nebula, and many African economies do not find the key to escape poverty. Globally, the capitalist world is growing at a much slower pace than in all three decades after the WWII.

It's true that some of these developments have been tolerated, but lately some tensions have been mounting up. Liberal advocates insist that lower growth rates are not to be imputed to the system itself but to the poor qual-

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ity of institutions and spreading government corruption. According to this view we need more, not less capitalism, and so reforms are needed to take full advantage of the system competences.

Yet there is a problem that capitalism can't get rid of, and that is inequality. Although this is hardly a controversial idea, its interpretation needs some discussion. The negative relationship between income distribution and growth and has been upheld by many capitalism supporters, for whom inequality is an early cost we need to assume in order to get rich. Indeed, modern views claim that a non-egalitarian distribution could be the natural result of different skills and personalities (even genetic disparities) that we do not want to alter. But *Capitalism Alone* Branko Milanovic wrote bearing in mind what is clear to the naked eye: that inequality is a consequence of the inner workings of the capitalist system, perhaps a necessary evil for the system to run efficiently.

Surname: Capitalism

In earlier books, Milanovic has done a wonderful job on how to understand inequality, its properties and consequences. Those are more technical than conceptual works. *Capitalism Alone* explores the relationship between capitalism and inequality from a new and fresh perspective.

To grasp the author's thesis, let's say that Capitalism is a father raising two descendants that happened to be rivals, because they will dispute his throne. On the blue corner we have Liberal Meritocratic Capitalism, which is quite a name if I must say. "Liberalism" refers to social mobility, where everyone is provided with some tools (for instance, public education) in order to be able to climb the stairs of success. The middle name, "Meritocratic", is to be understood in the spirit of Rawls' Theory of Justice, meaning a system where individual talent is welcomed and accepted as **the right way** to prosper. Finally, the surname "Capitalism" addresses how goods and services are produced and exchanged; in our metaphor the lineage the children will have to honor. Liberal Meritocratic Capitalism, naturally, is well represented by United States of America.

On the red corner we have the challenging, Political Capitalism. It has no middle name (a feature of his personality, perhaps), and that makes

its definition more nuanced. Political Capitalism may be understood as a mere description of China, but then its economic logic is much less known than that of his brother. The first characteristic of the Chinese system is that bureaucracy plays a huge role in implementing policies and taking responsibility for achieving high economic growth, usually established as an explicit goal. The second feature is that in order to do their job effectively, officials cannot be constrained by rules that are too strict—they need a lot of discretion to meet their goals. The final property of Political Capitalism is the deprivation of capitalists' interests as the supreme benefactor of society. The state retains significant autonomy to follow national interest policies and will not hesitate to run over the private sector to meet its objectives.

Political capitalism is the nightmare of many western academic economists, and Milanovic's book suggests that dawn will not arrive soon. In their book *Why Nations Fail?*, Daron Acemoglu and James Robinson claimed that having the right institutions is all that matters, and admit that if China continues to grow at the last thirty-year's pace, that would prove their theory wrong. At present these analysts may well be losing their bet, but the key issue pointed out by Milanovic is that China does not fit into Acemoglu's framework at all. According to the author, allowing China to be more democratic or less corrupt could be a hurdle rather than a blessing to keep growing.

For sure, each system delivers its own benefits. Although the United States has been proud of endorsing and protecting individual freedom, the connection between free economic policies and growth has lately proved to be more elusive than expected. On the other hand, China takes a lot of arbitrary actions against private agents, but in exchange it provides rapid and sustained growth.

At first sight, this contention could be interpreted as a "social utility function" where economies may choose between more freedom or more growth. But the function is hardly continuous for the rest of the world. Many developing countries are already suffering low growth rates **and** inequality. Choosing the proper system to develop, then, should not be easy. From the perspective of the medium or high class in rich Europe, Political

Capitalism may seem an aberration. But for Latin American median or lower classes, losing some freedom to do business in exchange for getting some essential needs may be worth it.

Reproducing inequality

In *Capitalism Alone*, the growth-equality tradeoff is the appropriate framework to clarify the pros and cons of the two systems, and Milanovic proceeds to explain what happened to inequality in each case. Clearly, the economic logic of each arrangement implies a specific stance on the distribution of income and wealth. Liberal Meritocratic Capitalism inequality is not only naturally conveyed by its own logic, this system also **reproduces** it. In one of the most important parts of the book, Milanovic masterly describes the channels through which this process takes place and shows convincing data to support his claim. Rich people used to have just capital, but now capital owners are also very well paid as workers. Elite families keep their wealth safe by paying low bequest taxes, or evading them. And millionaires marry each other because they frequent the same places. Milanovic warns that, if politics do nothing to correct this problem, in the future (or in the present, as the recent Chilean riots seem to show) this could bring social unrest, and eventually lower growth. In one interview, Milanovic looks convinced enough and declares: *“Let me just say it again, I think (inequality) it is bad for growth. It is bad for social stability, and it is bad for equality of chances, or equality of opportunity”*.

Political Capitalism is hardly a contrasting case. Milanovic shows that although China brought hundreds of millions of people out of poverty, inequality rose sharply from 1980 to 2005, mainly in urban areas. However, from 2005 on the trend seems to be receding slowly, resembling the famous U-inverted shape curve due to Kuznets. So the family name (Capitalism) seems to matter after all, since none of the two brothers are guaranteeing an egalitarian distribution.

Although *Capitalism Alone* is about inequality, it is not meant to compete with Thomas Piketty’s *“Capital in the Twenty-First Century”*, the other top-class analyst of global inequality. On the contrary, Milanovic stands up for the French economist rejecting what he considers an unfair

critique of the famous Piketty's expression $r > g$, meaning that inequality happens because the rate of return on capital (r) is greater than the economy's growth rate (g).

Moral Brothers

Since bad publicity for inequality comes mostly from moral reasons, Milanovic dedicates many pages to address the issue of economic integrity in detail.

In a world permeated with random events, the chance of being rich just because it is deserved is considerably small. Milanovic notes that being born in a wealthy country instead of a poor one assures individuals a huge "income premium", hard to vindicate as the result of pure effort or talent. The moral topic that needs to be handled here is immigration, since free movement of people could smooth this rent. The author dumps any political correctness and notes that, in an era of globalization, immigration to highly developed welfare states may lead to the perverse effect of attracting less skilled or less ambitious migrants, as empirical data seem to show.

Another moral topic chosen to be dissected is corruption, present in both systems but in different circumstances. As explained, in Political Capitalism corruption is endemic and constitutes a **feature** of the system. Arbitrary decisions thrive, but in the end, bribery and power are vehicles for the benefit of society as a whole. Sometimes it is argued that excessive control leads to corruption, but this statement is meaningless in the case of China, where corruption is almost a necessary condition to exert adequate control and coordination of public policies. In Liberal Meritocratic Capitalism, however, corruption is an **unintended** consequence of the market system. Too much freedom may give rich capitalists the opportunity to (cleverly) avoid the law, as in the case of tax havens. Milanovic then revisits corruption labelling this behavior as morally unethical in both systems. The liberal brother justifies tax havens in the name of efficiency and good incentives embedded in transparent property rights, yet brother political backs his arbitrariness and discretionary policies in the name of growth for everyone.

There is an important asymmetry about the morals of corruption, though. Financial international institutions usually condemn political,

rather than economic dishonesty, mainly because political corruption makes the rules of the game uncertain for capitalists. Since the ones classifying countries according to their “transparency” in doing business are themselves capitalists, economies like China are usually labelled as strongly corrupt and not suitable to invest, which is a weird judgement for the most successful story of investment and development in the history of humanity. This is why Milanovic engages in no less than fifteen pages to explain in every detail the awkward and unethical features of worldwide corruption. Globalization enabled illegal practices in both systems as never seen before, and the trend seems to be unstoppable in a world where inequality continues to rise and economic power to concentrate. It looks like father capitalism is not going to fix this problem alone.

The most appealing ethical notion that Milanovic brings in is what he calls “outsourced morality”. In some societies, morality has been safeguarded by religion. In others, the Smithian “tacit social contract” promised that the baker would deliver tasty bread because he would be monitored by the market. In today’s globalized capitalism, however, these ethical self-enhancement mechanisms are mostly missing. The boundary between what is acceptable and what is not will not be defined by morality, but by the law, which is meant to be external to the system. In globalized capitalism only law clear-cuts good from evil. Outsourced law is the suitable mechanism to ensure that the playing field is the same for every competitor, who then fights in the globalized arena for survival using the same means and the same tools as everyone else. Outsourced law is king, and so if you score a goal with your hand in a football game and the referee does not notice and awards it, that is all that counts.

Globalized capitalism has also sociological consequences. Not only the system but also technology is changing the way humans interact, by extending what Milanovic calls **atomization** and **commodification**. Atomization means demanding markets to do basic tasks that used to be performed at home, like every day cooking. If this trend continues, the nuclear family and individual privacy may fade away in the next decades. Commodification, the reverse of atomization, is the tendency of non-capitalists to offer personal services to other individuals, with no salary

relationship. Uber and bike delivery are the best examples. So we are all welcoming markets to our life and becoming marketable ourselves.

The Crown

So which brother will finally get crowned? Milanovic thinks that the up-take of one system by the other is not going to happen anytime soon. Political Capitalism must deliver permanent productivity growth in order to overcome freedom restrictions, and Liberal Capitalism does not seem to be growing enough to avoid being economically surmounted by its brother. Spreading these systems to intermediate countries is another matter: Liberal capitalism does not appear to be an automatic path to development, especially for countries that do not accept their offered place in the global value chain. Political Capitalism, on the other hand, may be hard to implement in western societies with entrenched cultural values. Given the modern absence of revolutions in midway countries, path dependence may define which future type of capitalism is going to be adopted.

Since Capitalism is alone and is responsible for its own future, Milanovic provide some help on how to promote more equality where is needed most—that is, in Meritocratic Liberalism. The dream of Meritocratic Liberalism is to achieve, in the end, a more egalitarian society where opportunities for all would deliver social mobility, perhaps converting everyone into a small capitalist competing nicely in transparent markets, and thus lowering interpersonal income disparity. But in practice the elite and its opposites do not seem to be exchanging their places.

The unexpected and dismal outlook for Meritocratic Liberalism, according to Milanovic, is that its own logic will force itself to adopt features of his brother Political. This would leave us with a wealthy but not as much decent family. In his own blog review of the book, Milanovic gives his account of that potential bleak future: “...*the contrast between acceptable behavior in hyper-commercialized world and traditional concepts of justice, ethics, shame, honor, and loss of face, creates a chasm which is filled with hypocrisy; one cannot openly accept that one has sold for a sum of money his/her right to free speech or ability to disagree with one’s boss, and thus arises the need to cover up these facts with lies or misrepresentation of reality*”.

All you can read (alone)

As you may have already noticed, *Capitalism Alone* is a book about global ideas. Every important topic about production systems, its properties and consequences, is discussed on it. Besides the ideas presented in this review, Milanovic handles technological fears, universal basic income, climate change, war threats, geopolitical issues, and many others.

Milanovic restrains academic ostentation by avoiding to fill up pages with references and communicates refreshing ways of exploring and understanding the world of capitalism and its future. The informative style can be recognized in the brief boxes that notify the reader where to find the key arguments.

Along the book, Milanovic gives his own opinions, but he is also ready to admit what he does not know. There are policy recommendations to deal with inequality, and reasons are provided for the options he thinks will not work. In these days, careful analysis of policies at such a systemic scale are infrequent, but Milanovic does it splendidly, never endorsing a course of action without enough justification. I wonder if his own experience living in a socialist system gave him a useful perspective (that is, a not-so-western ideology) to write with a clear and open mind about those important issues.

Surprisingly enough, *Capitalism Alone* does not discuss in detail western world's higher hope: Scandinavian countries. Milanovic barely notes that capital concentration in Norway has been rising, but does not present these countries as an alternative for future capitalism. For a naïve, western economist like me, this would have to be the most natural option, but I will be awaiting for the author's opinion on the matter.

So Father Capitalism is now Alone, but in charge. His older son, the Liberal brother, has been waiting for its virtues to materialize by themselves, but then little happened. Meanwhile, the young Political brother achieved the most impressive growth revolution in history, razing laws, rights and freedom in its endeavor. Milanovic has the rare talent to understand both histories in perspective and provides useful advice to help both better cope with their own future. Our future.
