

RESEARCH ARTICLE

Property, predation and socialist reality

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Abstract

Economics as a social science is about exchange and the institutions within which exchange relationships are formed and transactions are executed. Yoram Barzel's contribution to economics and political economy reflect this focus on exchange and institutions. In this paper, I will sketch a theory of real-existing socialist economies from a property rights/public choice perspective. Then I present the puzzles in political economy that such a system confronted in attempting to create a prosperous, regenerating and competitive economic system. I then conclude with a short discussion of the future for a progressive research program in political economy that takes institutional *change* seriously.

Keywords: Yoram Barzel; socialism; property rights

The claim that private property has been abolished in communist states and that all property there belongs to the state seems to me to be an attempt to divert attention from who the true owners of the property are. It seems that these owners also own the right to the terminology.

Yoram Barzel (1989: 104n)

1. Introduction

It is a distinct honor to recognize Yoram Barzel for his fundamental contributions to economics and political economy. Barzel was a critical part of the University of Washington approach to research in the economic analysis of property rights and institutional analysis and its application to shed light on significant events in economic history. This approach is grounded in a recognition of the almost infinite creativity and cleverness of individuals to resolve social problems and escape social dilemmas through exchange and institutional craftsmanship. Critical to this scholarly enterprise is an analytical focus on the exchange and enforcement of property rights.

I have stressed the creativity and clearness of individuals, as well as exchange and institutional craftsmanship, because I would argue in general that the rhetoric of maximization and equilibrium does not do full intellectual justice to the subtlety in Barzel's analysis. There is no doubt that individuals strive to do the best that they can, given their situation. They must choose against a set of constraints, and they do so not in a flawless way, but also not in a persistently stupid way. There are errors of judgment, errors of perception, and errors of execution, but the flip side of that is that there are creative and clever ways they attempt to change the constraints, to lower the costs of realizing the gains from productive specialization and peaceful social cooperation. The University of Washington mantra of "where are the deals" should not be intellectually trapped by a form of pure functionalism when discussing institutions. Yes, as Doug Allen writes in *The Institutional Revolution* (2011: 219), human history and the experience of everyday life demonstrate that there are numerous examples of "institutions that get the job done." And the analysis of behavior within

any given set of institutions does identify systematic incentives that impact the “scope and ability of decision making.” But Allen also recognizes that “Not all societies are successful at achieving this end [of a prosperous, regenerating, and competitive economic system] and often institutions are chosen that fail to meet the regularity of behavior that is desired.”¹

But of course, perceived dissatisfaction is a prerequisite for the pursuit of mutually beneficial exchange and entrepreneurial efforts at institutional craftsmanship (Boettke and Candela, 2015). When all the gains from exchange have not yet been exploited, the marginal benefit of an additional act of choice still outweighs the marginal cost of that act. Transaction cost-reducing innovations in institutional craftsmanship are similarly initiated by a frustration with the existing arrangements that must be blocking simple Pareto-improving moves from taking place, and thus creative and clever individuals are propelled to engage in institutional craftsmanship. There simply is an intellectual tension between the persistent and consistent application of maximization and equilibrium *within* any given institutional setting and choice *against* constraints fully identified, and a focus on the almost infinite creativity and cleverness of individuals to pursue mutually beneficial exchange and the institutional craftsmanship required to realize the gains from productive specialization and peaceful social cooperation. To give a classic example, those Beekeepers and Orchards farmers had to face a frustrating social dilemma first before they creatively found a contractual way out of that dilemma (Cheung, 1973). Institutional *change* is not compatible in a fundamental sense with maximizing and equilibrium modeling. But one might reasonably argue that the thought experiment of figuring out the functional explanation for an existing institutional arrangement does pursue this logic of maximizing and equilibrium and is a prerequisite for a theory of institutional change.

I do not propose to resolve this tension in this paper. That is not my purpose. I am more or less content to rely on the distinction made by my colleague Richard Wagner’s *Mind, Society and Human Action* (2010) between the foreground and background in economic analysis and argue that *both* a focus on maximizing and equilibrium *and* creativity, clearness and craftsmanship are vital to progress in economics and political economy. And Barzel’s contributions in works such as *Economic Analysis of Property Rights* (1989) and *A Theory of the State* (2002), as well as his work on “The Origins of Democracy in England” (Kiser and Barzel, 1991) or his paper on “Property Rights and the Evolution of the State” (2000), to name but a few of his numerous contributions, all exhibit his ability to live with this tension and to work toward an explanation of the “evolution towards a solution” that is the prime mover of progress in human history.² This is particularly valuable when it comes to analyzing the post-socialist political and economic history we have lived through since 1989.

In this paper, I will first sketch out a theory of the functioning of real-existing socialist economies from a property rights/public choice perspective. I will then present what I consider to be the puzzles in political economy that such a system confronted in attempting to create a prosperous, regenerating, and competitive economic system. Then I will conclude with some closing remarks about the future, as I see it, for a progressive research program in political economy that takes institutional *change* seriously.

2. The socialist system

It has probably become a cliché to begin any analysis of 20th-century economic history with the claim that the greatest social experiment of that century was the effort to construct a socialist system in Eastern and Central Europe and the former Soviet Union, in China, in India, and throughout various

¹I have emphasized these three aspects of institutions “getting the job done” in Allen’s presentation precisely because I believe it forces us to focus our attention not just on the functional significance of any institutions within a specific historical epoch, but also on whether those institutions can function in a way that enables economic growth and development. Thus we can have institutions that are failing to “get the job done” even though they are serving a particular function within the existing set of arrangements.

²See also Benson (1999), whose economic theory regarding the emergence of the state and the evolution of governance complements that of Barzel.

parts of Africa, Latin America, and Asia. When I started studying economics in the late 1970s and early 1980s, it could legitimately be claimed that three-quarters of the world's population lived in a socialist system. And the history of this experiment, I have recently argued on the occasion of the 100th anniversary of the Bolshevik Revolution, is one of "A Legacy of Lies and Lost Souls" (Boettke, 2017). Economic deprivation and political tyranny followed from pursuit of this administered command economy and one-party rule, and the horrific examples of Stalin's "collectivization" and Mao's "Great Leap Forward" should never be forgotten in any discussion of political and economic systems. But strictly speaking, political economy analysis is not about the moral condemnation of any system, and so the primary task for the political economist is never ethical evaluation or historical judgment, but *understanding* the functioning of the system and its internal operating principles.

Charlie Plott (1991) has given us the fundamental equation of political economy:

$$\text{Preferences} + \text{Institutions} \Rightarrow \text{Outcomes}$$

Or, simply stated, "same players, different rules" produces different outcomes in the social games we play. We explain the variation in pattern of outcomes in the social game by the variation in the institutions under which the game is played, not in the variation of the preferences of the players.

No doubt, one could reasonably claim that "different players, same rules" produces different games. Watching LeBron James play basketball would be different than watching Pete Boettke play, even if we are constrained by the same rules, just as explaining the division of labor by reference to unique personal characteristics is no doubt true. Shaquille O'Neal probably could not have won the Kentucky Derby as a jockey any more than Willie Shoemaker could have played center in the NBA finals. But such "explanations" are basically "empty" in the economic way of thinking. Saying I drink coffee because I like coffee tells me little by way of explanation for my coffee consumption decisions. On the other hand, if I take preferences as given and look into the relevant constraints and the relative prices faced in making my choices and explain why in some instances I might choose tea instead then I have started to offer an explanation rather than a description. This is a theme to which I will come back at the end of this paper, but if our theories in political economy ultimately completely turn on initial conditions to determine the equilibrium exhibited, then I would argue that we haven't offered an explanation at all, just a description of the situation (Boettke and Candela, 2019).

Socialism didn't operate the way it did because of Russian characteristics, or Chinese characteristics, of the populations within which socialist institutions were instituted. In any detailed history of socialism in these countries, the history and cultural of the people matters as background. However, I would argue that the most important element in any serious analysis of the experience is one grounded in the logic of choice, the logic of the situation, and the organizational logic. Individuals are not persistently stupid, and they will strive to pursue the best strategy responses to the constraints they face and the social situations they find themselves grappling with. Russians and Chinese workers and peasants are just as clever and creative as their counterparts in England during the rise of liberal government, or Americans during the evolution of the constitutional project after 1787. Political, economic, and social actors all strive to do the best that they can given their situation. Elinor Ostrom (1990: 25–26) explained clearly why this must be the way we pursue our studies:

As an institutionalist studying empirical phenomena, I presume that individuals try to solve problems as effectively as they can. That assumption imposes a discipline on me. Instead of presuming that some individuals are incompetent, evil, or irrational, and others are omniscient, I presume that individuals have very similar limited capabilities to reason and figure out the structure of complex environments. It is my responsibility as a scientist to ascertain what problems individuals are trying to solve and what factors help or hinder them in these efforts. When the problems that I observe involve lack of predictability, information, and trust, as well as high levels of complexity and transactional difficulties, then my efforts to explain must take these problems overtly into account rather than assuming them away.

And as she had argued earlier in *Governing the Commons*, she was not content to let the standard modeling exercises lead her to see actors in the social world get trapped in situations they are hopeless to change. “The prisoners in the famous dilemma,” she states, “cannot change the constraints imposed on them by the district attorney; they are in jail.” Ostrom continues, “As long as individuals are viewed as prisoners, policy prescriptions will address this metaphor. I would rather address the question of how to enhance the capabilities of those involved to change the constraining rules of the game to lead to outcomes other than remorseless tragedies” (Ostrom 1990: 7). The actors we are studying are more creative and clever than the theorist studying them in finding ways to craft the necessary institutional changes to realize the gains from social cooperation – just remember those beekeepers and orchard farmers and the mantras “where are the deals?” and “let’s bargain.”

The analysis of socialist systems in practice is not any different. The actors inside the system were not passively responding, but strategic and entrepreneurial. But the rules in operation in the system, as well as the constraints the actors faced, meant that their strategic and entrepreneurial actions were directed toward certain behavioral patterns in exchange and production. This was true for consumption decisions and production decisions both within and outside of the official planned economy. Early work in my career was focused on the origin, practice, collapse, and transition from this set of arrangements in the former Soviet Union (see Boettke 1990, 1993, and 2001). In *Why Perestroika Failed* (1993), I even had back-to-back chapters on how the system was supposed to work in theory and how it actually operated in practice. The point that is vital to get across is that in understanding the socialist system and its transition, we must first get a good understanding of its internal logic within a given set of institutions, and that gives us our start state, and clearly identify the social problems that arrangement systematically generates. It is from that point that we can begin to explore the possibilities of institutional craftsmanship to realize Pareto improvements. Such institutional craftsmanship itself proposes identifying incentive-compatible institutional solutions to the existing social dilemma, and incentive-compatible strategies for the adoption of that proposed solution.³

One of the defining characteristics of the socialist economy was shortages, as explored by Janos Kornai (1992) among others. Barzel in *Economic Analysis of Property Rights* has two very important discussions that are relevant for developing an analysis of the socialist economy, though he only indirectly touches upon the subject: Chapter 8 on non-market allocation and Chapter 2 on price controls and rationing by waiting. I mention them in reverse order because I think the essential point is to first understand the setting on non-market decision making and then the application to settings where relative prices do not guide adjustment and adaptation. Pecuniary benefits certainly still play a role in these non-market settings, but so do other factors, such as power and privilege to those in unique positions.⁴

³However it is important to point out that I follow Buchanan (1959) in my view of the role of the economist in this process of institutional craftsmanship. The priority is given to the actors within the system, not the theorist outside the system, for the reforms. Economics is best seen as a tool of social understanding, not as a set of techniques applicable to social control. From this perspective of Buchanan’s, the economist, as economist, has no privileged position in the public discourse.

⁴There is a fundamental point to be made about the difference between the analysis of socialism that is associated with Mises and Kornai, which sees the system as operating under bureaucratic rules, and that of Barzel and my presentation here as operating as a distorted market economy. These issues are too subtle and complicated to adequately address in this paper as they would take me too far afield. As a result, I will gloss over differences between these thinkers for this paper and instead work with a synthesis of their works. They are, however, very important issues that deserve serious consideration. In a paper with Chris Coyne and Peter Leeson, I address the problems with “Quasi-Markets” (Boettke, Coyne and Leeson, 2011), and in my SEA Presidential address (Boettke, 2018) I discuss the problems of public administration and bureaucratic decision-making outside the realm of the price system and the process of economic calculation. But in studying real-existing socialist economies, I have been influenced by Rothbard’s claim that the existence of underground markets, the use of world market prices, and the constant renegotiating that is internal to the planning process, meant that “markets” were more prevalent in the Soviet system, which was usually discussed in textbook depictions of “central planning” (see Boettke and Coyne, 2010). My position was also influenced by the earlier work of Paul Craig Roberts (1969, 1971) – under the influence of G. Warren Nutter and Michael Polanyi – on the polycentric nature of the Soviet economic system.

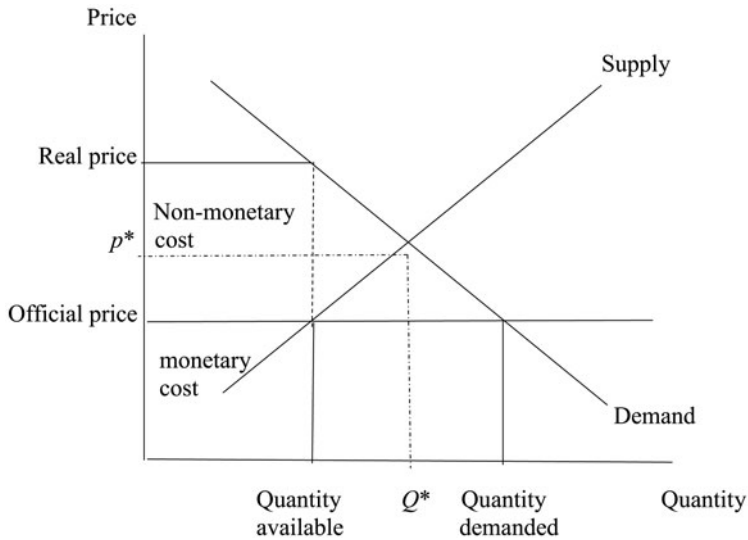


Figure 1. Supply and demand in a shortage economy
Source: Boettke (2001: 3).

Within real-existing socialist economies, there was no alternative supply chain for goods other than the state production process, which meant that theft was an integral part of the operation. There were small-scale private plots in agriculture, but durable goods from toasters to cars were all products of state enterprise. The international “trade” that was officially in operation was through Comecon, which were basically internal barter arrangements predominately for natural resources, such as oil, or quasi-public goods such as trains and airplanes. Consumer frustrations were eased in the black market, and production frustrations were eased through backroom deals between state enterprises. Property rights existed throughout the system, but they were attenuated. Individuals had control rights (i.e. the ability to exclude non-users), but not explicit cash flow rights (i.e. the ability to exchange). Barzel follows Armen Alchian and William Allen (1972) in arguing that a property right sets an expectation that the owner will be able to enjoy the fruits of that asset. But if you cannot officially possess cash flow rights, but have *de facto* control rights, all the incentives are aligned for economic actors to attempt to convert those control rights into cash flow rights as quickly as possible. Those waiting in the queue will face a real price, rather than the official price. See Figure 1.

This shortage situation will set in motion competitive processes on a multitude of margins. The area between the real price and the official price at the available quantity is the real comparison, not merely the official price and the would-be equilibrium P_* and Q_* . This comparison matters significantly not only in the welfare economics of transition from a shortage economy, but in the political economy of winners and losers in the transition. First, the standard of living is not accurately measured by looking at the competitive equilibrium price versus the controlled price and pointing out that since the market price is higher the average person is now worse off. The goods and services at the controlled price were not available at that price, they were available only at the black market price (the real price, or the queuing “price”) and thus the move to an open market is actually a reduction on the cost of acquiring the good or service. Second, we must ask: why did these regimes systematically price goods and services below the open market price? Here, work by David Levy (1990) and Andrei

A full analysis of real-existing socialism requires recognition of the differences between the *de jure* and the *de facto*, as well as the difference between the form an institution takes and the function it serves. Also see Richard Wagner’s *Politics as a Peculiar Business* (2017) for a discussion of an “entangled political economy” as well as Murtazashvili and Murtazashvili (2019) on the political economy of legal titling.

Shleifer and Robert Vishny (1992) augments the earlier work of Kornai on bureaucratic coordination problems in the over-administered state, and shows that in a system of attenuated rights as the socialist economy in practice was, pricing below the market to create shortages was in the interest of those in positions of power and privilege in the planning system. Thus this analysis provides the micro foundations for a theory of the shortage economy within real-existing socialist systems.

The socialist economy was, in this sense, merely a modern manifestation of the rent-seeking society of older style mercantilism, as described by Ekelund and Tollison (1981) and then developed in work by Anderson and Boettke (1997). And thus, this shortage economy where the official price is set below the market clearing price, means that transactions are going to be supply constrained and competition among buyers in the underground market will be bid up black market prices till they equate to the queue price for waiting. The status quo is one in which there is simply no alternative supply chain, a situation from which bargaining must take place if there is any hope of establishing an institutional regime that can “get the job done,” as Allen puts it, and produce prosperity, regenerate itself, and establish a competitive and vibrant economy as well as an open political system.

When socialist governments began to collapse in 1989 and then in 1991, when the Soviet Union ceased to exist and transitional political economy was set in motion, it was often remarked that this monumental task was unique in human history. The magnitude of the changes required and the number of people impacted was huge (and we shouldn't forget China, though they started earlier). However, what I want to suggest is that when we strip away the rhetoric, the puzzles in political economy were actually age-old puzzles and not something unique. This is why I have belabored this last section because correctly identifying the start state is one-third of the battle in a clear-headed political economy of transition, while another third is understanding the end state goal even if in some very abstract sense. And of course, the third stage of drawing a road map from here to there is actually correctly identifying the best route given the existing state of human capital and technology available.

3. Timeless puzzles in political economy

There are timeless puzzles in political economy that the property rights/public choice perspective provides us with tools for analyzing. There are two meta-puzzles that date back as far as one can remember. The first of these is what Acemoglu and Robinson recently dubbed “the Gilgamesh problem” after the ancient tale of an all-powerful ruler. It is a tale as old as time, and inspiration could have been found in 1 Samuel of the Old Testament as well. The key issue is the development of countervailing power used to check the abuse of power by the rulers. Who will guard the guardians is a classic puzzle and led to the first fundamental paradox of government.

Barry Weingast has suggested that this is:

[the] *fundamental political dilemma of an economic system*: Any government strong enough to provide the minimal institutional requirements of markets – for example, a secure system of property rights, an objective judicial system, a stable monetary system – is also strong enough to extract the wealth of its citizens. (1997: 43; emphasis original)

This problem of binding the hands of the ruler will recur throughout our discussion.

The second meta-puzzle deals with the fundamental dilemma that results whenever we are choosing in groups, and that is namely the problem that Rousseau put his finger on: how can an individual be free while subject to wills other than their own? The decision calculus of the group must respect the rights of those who are in the minority in any case. The ability of collective decision-making processes to impose costs on individuals that are not of their choosing is a fundamental puzzle. This is a normative question with positive analytical answers, whereas the Gilgamesh puzzle is almost purely an analytical one. Though they arise in the theory of liberal political economy from Adam Smith to John Stuart Mill to F. A. Hayek to James Buchanan, these two fundamental problems in political economy merge into variants of the constitutional project. Or, as Buchanan (1975) might have

summed it up: can you find that set of constitutional principles and institutional structure that empowers the protective state (courts, law and order, and defense) and the productive state (the variety of public goods from roads to education) without unleashing the predatory state (confiscatory taxation, rewarding of privileges, and abuse of the rights of citizens)? If we take this meta-puzzle as described and relate it to the post-socialist period, we can appreciate as David Weimer (1997: 1) put it, that:

Property rights, the relations among people concerning the use of things, lie at the nexus of economics and politics. Property rights systems, which include the rights themselves and the formal and informal institutions that create them, structure economic transactions, including decisions concerning the exchange and accumulation of physical, human and intellectual capital, and the preservation of natural resources. The state, as maker and enforcer of formal rules, plays a fundamental role in shaping the property rights system.

But in the difficult moment of post-socialist transformation, establishing credible property rights will be critical to the government. “A difficult task for any government,” Weimer adds (1997: 12), “it is all the more difficult for them because of their legacy of institutions with low levels of economic legality and their need to alter radically their formal property rights system.” The puzzles in political economy that I see are all nested inside the meta-puzzle of the constitutional project, and moreover nested within each other so that a proper institutional solution can be found only if all the puzzles are satisfactorily solved simultaneously. Let me list them with a short explanation for each.

Rational choice and reform

Envision a basic Edgeworth Box depicting a contract curve between two representative agents in our economy. Our axis on the diagram is personal command over financial resources and personal command over the ability to exercise power over others. The problem with the socialist reality was that too much command over financial resources and too much ability to exercise power over others resided with the representative governmental actor relative to the citizen. That is our problem, but that also defines our status quo that must be bargained from. There is no normative weight to this position, it just is what it is. And it is where we must begin.

To puzzle #1 – how do you get on the contract curve so that the representative government actor will exchange and end up in a position that grants more command over financial resources, and more power over their own lives to the representative citizen? In the basic Edgeworth Box framework you can only get trades inside of the eye of the status quo sets of indifference curves, so the answer would be that you cannot. If the rational choice logic is indeed a “harsh mistress,” then perhaps that only way to get the re-contracting phase would be an exogenous shock. This is one way to read the message in Mancur Olson’s *Rise and Decline of Nations* (1982). But Yoram Barzel argues that a ruler may choose to tie their own hands as a consequence of the calculations about the trade-off between wealth and security. As he says, while his argument is Hobbesian in spirit, he turns Hobbes on his head because the ruler will give up some of their power voluntarily in order to earn the trust of their subjects (2000: 27). Due to the constant threat of their security both from internal and external friends and foes, rulers stumble upon an evolution toward a solution to the optimal institutional configuration that maximizes wealth while providing security from overthrow. In short, by beginning at the onset of the process, rather than studying the situation once that process has worked itself out and settled on the new equilibrium arrangement, we can study the evolving institutions that lead to the slow and steady shift in arrangements from dictatorship to the rule of law and democracy. It is a process that takes time, but we are neither trapped by initial conditions (endowment), nor able to ignore where we came from (those initial conditions). There is hope in constitutional re-contracting, but we must admit that history seems to point to cautious rather than enthusiastic hope. As I am suggesting, that is because this puzzle cannot be solved in isolation from the others.

Transitional gains trap and the rent-seeking society

Gordon Tullock (1967) famously challenged the traditional welfare loss argument about monopoly by pointing out that the empirical measures of the deadweight loss were in fact minuscule. Yet despite this, economists were still preoccupied with the problem of monopoly and its deleterious effect on the economic system. How could one square these two facts? Well, Tullock explained, the deadweight loss measures of monopoly were not the accurate measures and in fact systematically understated the costs, and once the process by which individuals expend resources in the race to obtain the monopoly privilege to be a sole seller of a good or service was taken into account, then the full extent of the costs would be known and the magnitude of that use of resources in unproductive transfer activity would justify the economists' concern with the phenomena. It is not monopoly rent *per se* that is so deleterious to economic performance through time, but the activity required to *seek* and *acquire* those rents from monopoly privileges.

John Wallis (2006) has made a very important distinction in economic history between venal corruption and systemic corruption. Venal corruption is the under-the-table payoffs in order to get around restrictions and ease the path toward realizing mutually beneficial transactions. But systemic corruption is when the government distorts the economic system through its doling out of privileges and command and control over the everyday economic life of its citizens. Venal corruption is consistent with economic growth and development, though obviously small changes in the rules would improve upon that situation. Systemic corruption has the ability to thwart economic growth and development.

This raises again the trade-offs that rulers are always making in their calculations, as Barzel lays out in his work – wealth, power, security, etc. The problem is that “selling” monopoly privileges has been one of the most effective revenue-raising strategies given technological limitations to metering and monitoring throughout history. But if those monopoly rights are transferable, the rent earned is capitalized quickly so that no super-normal returns will exist for the rent-holder. And thus we have puzzle #2, which is the transitional gains trap. In Figure 1, the shortage economy of the socialist system was depicted using a standard supply and demand diagram. In that picture there are costs to demanders that are not simultaneously benefits to the suppliers, but the suppliers have control rights and thus it is in their interest to transform those non-monetary costs to the demander (queuing) into monetary benefits for them (at the black market price, or bribe fee for access, etc.). In the 1950s it was a common Russia idiom to say “Blat [bribe fees] is higher than Stalin.” From top to bottom, there are parties that benefited from the administration of a shortage economy.

The transitional gain can be easily gleaned again by looking at Figure 1. The monopoly rent due to the artificial restriction of output and the privilege of being the exclusive seller of that good and/or service is far greater than the deadweight loss due to the artificial restriction. Opening up that market will eliminate the deadweight loss, but the cost of getting existing rent-holders to give up their current privileges will be greater. The costs of reform are greater than the benefits to be received from it in this simple depiction. As can be seen, puzzle #1 and puzzle #2 are in some sense variants of each other. And the answer is similar: how do I get those currently in positions of privilege willingly to give up some of their wealth and power in order to pursue Pareto-improving changes in the governing rules of the economic system?

Credible commitment and time inconsistency

An opportunistic government, whoever has the ability, as Weingast put it earlier, to confiscate the wealth of its citizens will be most successful if they can convince the citizens that they will not confiscate their wealth and thus encourage them to engage in productive specialization and peaceful cooperation, which enhances the wealth for the taking. Again, remember Weingast's point – a government strong enough to establish strong property rights is also strong enough to violate those property rights and confiscate the wealth produced in the economy.

The sequentially rational move of an opportunistic government would be to announce the opening up of the economy to entrepreneurial innovation, and then after the production of wealth to engage in confiscatory regulation and taxation to secure the fruits of the increase in economic output for themselves. So, puzzle #3 of political economy is how does one effectively establish a credible commitment so that even the most opportunistic government will be unable (or better yet unwilling) to play the confiscatory strategy in the remote rounds of the game? If they are unable to establish this credible commitment, then via the logic of backward induction the citizens in the economy will in fact not enter the above-ground economy to realize the gains from trade and from innovation. The economy will be poor, the rulers will have less revenue, and the citizens will exist in an ambiguous state of illegality in their everyday economic life unless such a credible commitment is established. And to compound matters, keep in mind Weimer's very useful insight that in the post-socialist environment we are expecting such a commitment from a government in an environment characterized by low trust of public institutions. Therefore, in addition to a credible commitment, strong signals that this commitment has been made will be required.

Roving and stationary bandits

Douglass North, Avner Grief, Daron Acemoglu, James Robinson, and many others have all explored the transition from personal to impersonal exchange and the pathway of institutional evolution that must be traveled for this to take place. Put aside the subtle and important difference in these different narratives, and instead strip down to the basic intuition and you get puzzle #4 as laid out by Mancur Olson (1993). The time horizon of the ruler matters in whether or not the ruler will engage in confiscatory policies or seek to establish the stability and security of persons and property so that individuals will engage in capital accumulation and productive investment in the economic future. The roving bandit will seek to exploit the situation quickly and move on, whereas the stationary bandit will seek to establish an institutional environment that is prosperous, regenerating, and competitive.

In many of these discussions, the answer seems to turn on the initial conditions within which the ruler finds themselves – whether that be the physical conditions that determine the harshest of life, the existing stock of human capital among the rulers and the ruled, or the given state of technological knowledge for metering, monitoring, and collecting revenue from productive economic activity. There is something very unsatisfactory in this, because an explanation that relies on initial conditions to do all the heavy lifting may in fact be little more than a description. We end up naming things, not explaining things, as the brilliant physicist Richard Feynman used to stress. So, for example, in North, Wallis and Weingast (2009), we have a Limited Access Order and an Open Access Order, and there are defining characteristics with respect to the way they attempt to deal with violence to produce social order. And in Acemoglu and Robinson (2012) we have extractive institutions and inclusive institutions, and the balance of these determines in some sense whether the society under investigation is an absent Leviathan, an unshackled Leviathan, or a shackled Leviathan. Only the shackled Leviathan can secure liberty, prosperity, and peace, but it does so because the existing stock of human capital and the technology available enable that society to achieve this – or, as Allen put it, institutions getting the job done. As my colleague Peter Leeson (2017: 3) likes to put it, rules might tell us what is permissible, but constraints tell us what is feasible. However true that might be, our task in comparative political economy and post-socialist transition studies cannot be limited to a description of initial conditions and the equilibrium pattern of behavior that falls out of such a description. Our task is one of studying the *transition* in the long process of economic development from a limited to an open access order, or the shift from extractive to inclusive institutions orchestrated by creative and clever actors within the system who are engaged in institutional craftsmanship. And that means the binding constraints on the predatory capacity exhibited first among private actors on one another, and then on the public actors whom we entrust to curb private predation, but who can therefore engage in the larger deleterious act of public predation.

Can the revenue-maximizing strategy for Leviathan be wealth maximizing for the economic system?

Geoffrey Brennan and James Buchanan published *The Power to Tax* in 1980, and it works throughout the model of a revenue-maximizing Leviathan in a consistent and persistent manner to great effect. The critical point to understand about their effort is that their use of this assumption was never meant as a description of real-existing governmental actors. Rather, its purpose was a modeling strategy to aid in the discovery of institutional rules that would guard against opportunistic behavior and thus work to enable individuals to engage in productive specialization, peaceful social cooperation, and wealth creation. Puzzle #5 is precisely to find that set of institutions that will equate the revenue-maximizing strategy with the wealth-maximizing set of public policies.⁵ If we can find an answer to puzzle #5, then even the most opportunistic ruler will agree to operate under this set of institutional constraints on their behavior.

As I said at the beginning of this discussion, these problems are nested. They are not identical, but are like the various pieces in a complex social jigsaw puzzle that must be put together for the full picture to come into view—in this case the picture of a growing, vibrant economic system. Think about this for a minute: the transitional gains trap must be resolved in a way that also credibly commits the ruler to tying their hands. But to overcome the transitional gains trap, one must pay the existing rent-holders the present value of their future income stream expected from maintaining their privileged position. In post-socialist Russia this sometimes meant insider deals in the early transition period, and this helped create the Oligarchs, who have been a target of criticism ever since for those frustrated with the Russian experience over the past two decades (see discussion in Aslund, 2013: 201ff). But how have countries that did not move quickly to privatize in East and Central Europe fared in the post-socialist environment? In those countries, many large enterprises remained state-owned and either have subsequently shut down, or sold to foreign investors and performed poorly because they were so late in making the necessary structural changes to compete effectively in a more open market environment. In Russia, on the other hand, many large enterprises remain successful businesses. But their tremendous wealth enabled the Oligarchs to become politically connected, if they were not already. So did mass privatization succeed in overcoming the transitional gains trap? History seems to suggest an affirmative answer to that question. But did they do so in a way that established a credible commitment to strictly constraining the government's active role in the economic life of its citizens?

There the answer is less optimistic to say the least. Russia may be a “normal” middle-income country, as Shleifer and Treisman (2005) have argued. That just means it is an economic and political system that suffers from systemic corruption, and remains in the language of North, Wallis and Weingast (2009) a “limited access” order. Russia has so much more potential in terms of human capital, and physical capital, so the inability to craft institutions that “can get the job done” means that large sums of “Big Bills” remain on the proverbial sidewalk. Pareto-improving changes in the rules are not made: the University of Washington mantra of “where are the deals?” and “what bargains can be struck?” simply cannot get off the ground in the public space if the puzzles continue to trip up the rulers and the ruled.

The long process of economic development is characterized by the accumulation of successful marginal adjustments and adaptations to fit the pieces of the puzzles together. History never moves in one giant leap, as Alfred Marshall taught some many years ago. Instead, as Hayek argued in *The Constitution of Liberty* (1960: 19), there is a slow laborious process of acquiring hard-earned

⁵Another point to also consider is the following: what if the objective function of the ruler is not to adopt institutions that “get the job done” but instead to adopt institutions that perpetuate their power, or allow them to extract rents as quickly and as thoroughly as possible? Of course, in that case, the ruler's behavior would be predictably different. As I have stressed, I take the meta-puzzle to be about development, following Allen's lead, and one of Barzel's unique contributions was precisely to demonstrate that the even a power-hungry ruler may pursue the institutional changes associated with wealth maximization in order to secure their own political future. Therefore, this puzzle about aligning wealth maximization with revenue maximization remains.

institutional changes that yields different liberties, which accumulate until a tipping point is reached and a regime of liberty is established with constitutional democracy and the rule of law (Boettke and Candela, 2017). But note that each step along the way, our explanations of this evolutionary process must be disciplined by the logic of choice, the logic of the situation, and the organizational logic so that we do not rely in our explanations on wishful thinking, fortunate circumstances, or magical leaders. Instead, we ground our explanations in ordinary human beings acting creatively and cleverly in their effort to improve their situation. We must, as James Buchanan stressed, recognize the two levels of analysis – both within the rules, and over the rules. And a genuine institutional economics follows when the economist is no longer content to postulate the institutional framework within which economic activity takes place, but turns their attention to the derivation of that institutional framework from the behavioral postulates consistent with the economic way of thinking (Buchanan, 1999: 5).

Piecing together these different puzzle pieces provides the mechanism by which we also solve our meta-puzzles that was the basis of this discussion. And there is a certain content in the institutional structure that provides security to person and property from predatory exploitation by strong private and powerful public actors that must be embedded in the evolution toward a solution if the institutional framework is to *get the job done of establishing a regime that is prosperous, regenerating, and competitive*.

4. Conclusion

Yoram Barzel (2000) has argued that individuals created institutions throughout history in order to ward off the confiscatory threats, and simultaneously built in various competitive checks and balances, to enhance the functioning of these institutions. If you think about this in light of the puzzles I laid out, and in particular the nested nature of the puzzles and their solution, such institutional innovation represents the extreme cleverness and creativity of human actors. As Barzel (2002: 250–266) later argued, the different regimes that are established along this historical path have different capacities to cope with the shocks, large and small, that history thrust upon them in studying human affairs. He argues that regimes that approximate the rule of law will be able to sustain themselves even in the wake of significant shocks, whereas regimes that did not move so far along the historical path from their dictatorial roots will be vulnerable in the face of even small shocks.

The Soviet and post-Soviet cases are particularly illuminated by looking through Barzel's lens of property rights and institutional evolution. As Barzel (2000: 35) stresses, it is the ability to make credible commitments to protect persons and property that also enables the ruler to establish institutions that will provide checks and balances independently. In the United Kingdom and the United States, at least to a reasonable extent, the protective state and the productive state could be empowered while keeping the predatory state in check, at least for a reasonable period of time. Economic growth and development, as well as political freedom, followed. When the regime is unable to do this, the result is not a prosperous, regenerating, and competitive system, but a poor, degenerating, and monopolistic system. In 1921, for example, the Soviet regime confronted a situation where the very survival of their ruling coalition was in question as the economy completely collapsed under "War Communism" (see Boettke, 1990, 2001). Lenin *et al.* made the faithful decision to give citizens relatively more economic autonomy and introduced the New Economic Policy (NEP). The Bolsheviks traded some of their command and control to citizens in exchange for their retention of ruling power. In fact, they consolidated their political power while making these economic concessions, and effectively not only established a one-party state, but eliminated all dissent within the party as well. The NEP originally had strongly positive effects on the Soviet economic situation relative to the preceding period. But the regime could not credibly commit to the reforms in terms of the content that would constrain the confiscatory practices of accumulated wealth. So the Nepman (those who prospered from the relative opening up of economic life) lived in constant fear and had an ambiguous legal status. Less than a decade later their fears were realized, and the Soviet regime beginning in 1928 began in earnest to violate the property rights of individuals in the name of industrialization and collectivization.

This also set the Soviet system on a treadmill of economic reforms that it would never get off until the system collapsed. The system had its own internal logic and functioned according to those operating principles in a predictable manner. But it was also obvious to anyone given the human capital and state of technological knowledge that Big Bills were constantly being left on the table due to the failure to make the Pareto-improving changes in the rules. The Soviet reform efforts could never solve the puzzle as long as the Soviet Union remained intact. This was played out in Perestroika (see Boettke, 1993; 2001), as the regime was never able to signal the establishment of a credible commitment to economic liberalization. Unfortunately, this inability continued in the post-Soviet era and perhaps the best evidence in both the Perestroika period and the post-Soviet period is that extensive underground markets continued to operate and in fact expand at a time when a supposedly more open economy was being established.

None of these peculiarities in the everyday political economy of socialist and post-socialist countries is understandable unless institutions, and in particular the vital role that property rights play in economic, social, and political existence, are front and center in our analysis. And Yoram Barzel has done as much as any thinker in the second half of the 20th century to rejuvenate and refine our analytical and historical understanding of the relations among people and “the rights, or the powers, to consume, obtain income from, and alienate” the assets that individuals are recognized formally and informally to possess (Barzel, 1989: 2).

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