

AN INTRODUCTION TO  
**SOCIALISM**  
vs.  
**CAPITALISM**

James R. Otteson



REALITIES OF  
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### **Date of Issue**

April 2023

### **Media**

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### **Acknowledgments**

The Fraser Institute thanks the Lotte and John Hecht Memorial Foundation and the John Templeton Foundation for generously supporting this project. The author also wishes to thank Jason Clemens, Steve Globerman, and an anonymous reviewer for helpful comments and feedback on a previous draft of this essay, which he has silently incorporated or addressed. He also thanks Kristin McCahon for sound editorial advice. All remaining errors are his. As the author has worked independently, the views and conclusions expressed in this study do not necessarily reflect those of the Board of Directors of the Fraser Institute, the staff, or supporters.

## Introduction

We certainly live in interesting times. On the one hand, based on numerous criteria we are living in the best of times. Whether we measure longevity, literacy, lifesaving drugs and medical procedures, liberty, or a long list of other things that matter, we are now at levels never seen in human history.<sup>1</sup> There is more real wealth in the world now than there has ever been, and the proportion of humanity living in absolute poverty—which the United Nations defines as living on approximately US\$2 per person per day—has never been lower. In 1900, the proportion living in absolute poverty was approximately 90 percent; today, it stands at approximately 9 percent, and is falling. There is also less violence in the world, greater tolerance for diversity, more average attainment of formal education, less extraction of raw materials despite increasing demands for energy, and even, recently, more greening of the earth.<sup>2</sup>



So, why aren't we happier? Indeed, why aren't we all jumping for joy?

Well, on the other hand, there is income inequality and unequal enjoyment of the wealth and benefits of society. There is increasing production of carbon dioxide and growing concerns about climate change. There is human trafficking. There are people who can't get the medical treatments they need, who face employment insecurity, who suffer from loneliness and anxiety and depression, who have broken families, who have little social support or little connection to society, and who are trapped in poverty—if not “absolute” poverty, then in circumstances far more challenging and difficult than the circumstances of the rich. A seemingly increasing proportion of people, both rich and poor, are having trouble finding meaning and purpose in life. These are not causes for joy.

A growing consensus holds that capitalism is behind both the good and the bad. The dawn of capitalism in the late eighteenth century led to an explosion of material prosperity, which continues to this day. And yet, at the same time, capitalism is alleged to have torn asunder the social and communal bonds humans have enjoyed and from which they derived their identities throughout their history; divvied up the world's natural bounty,

concentrating the lion's share in the hands of a lucky, rapacious, or greedy few; inflamed our appetites, titillated our lowest sensibilities, triggered a restive insatiability, and, in the end, reduced humanity in all its dignity and preciousness and nobility to factors of material production—descending from *Imago Dei* to “human capital.”

**“One recent poll found that fully half of all ‘Gen Z’ Americans—those born between the late 1990s and the early 2010s—approve of socialism.”**

Perhaps it is not surprising, then, that so many are searching for an alternative to capitalism, and that socialism, in one guise or another, is gaining favour. One recent poll, among many similar polls, found that fully half of all “Gen Z” Americans—those born between the late 1990s and the early 2010s—approve of socialism (Johnson, 2020, October 23). Another recent survey found that half of graduating college students are pessimistic about the future of the world; over half of them do not believe humanity will make significant

progress on climate change in their lifetimes, and fully 60 percent of them believe that in their lifetimes the world will not make significant progress on poverty (Routledge, 2022).

One could multiply such examples, but their point is clear: increasingly many people, especially younger people, believe that capitalism has either allowed or caused diminishments in the quality of human life, rewarded and thus encouraged vice and misery, and perhaps now poses an existential threat to democratic governments (the rich have undue influence) and even to all life on earth (climate change).

Now, do those who are asked whether they support socialism or capitalism have clear or consistent ideas about what those terms mean? Are they aware of the empirical results of historical experiments in socialism and capitalism? Perhaps not. And framing makes a tremendous difference. Consider this: suppose you were asked whether you supported a system that championed equality, fairness, and care for the poor; *or* a system that championed profit, greed, and callousness toward the poor. Who would support the latter, whatever it is called? Or suppose you were asked whether you supported a system that empowered governments to dictate all aspects of citizens' lives; *or* a system that respected and protected citizens' liberty and opportunity? Who would support the former, whatever it is called?

Because people have differing views about what “socialism” and “capitalism” are, they often find themselves talking past one another. A supporter of socialism might claim that capitalism is principally about enriching oneself regardless of the consequences for others or for the environment, while a supporter of capitalism might claim that socialism is about empowering authoritarian government agents to invade the rights of citizens and enrich themselves and their cronies at others' expense. If those are their starting points, neither of them may have the mental space to agree that the other's position could have arguments worth considering.

If we wish to enter into this debate in good faith, then, we first need to get our definitions straight. What exactly do we mean by “capitalism,” and what do we mean by

“socialism”? We also need to understand what the goals are that our system of political economy should champion, and what the ranking is of those goals. And then we need to understand what means we really have available to us to achieve those goals, or at least make progress toward them, how likely the various means are to make that progress, and the costs or tradeoffs, including moral costs and tradeoffs, that those means entail.

To enable some progress in the discussion, or at least the hope of some progress, perhaps we might begin with some relatively uncontroversial points of agreement. Perhaps there might be three such points of wide agreement—the first two, descriptive; the third, normative. First, we live in a world of *scarcity*, meaning that however much we have, we still want more and there will always remain unmet needs and desires. Even if we had unlimited material resources, we would still be limited by our time to use them. Second, human beings tend to be *locally self-interested*, meaning that they tend to prioritize the needs and desires of themselves and of their own families, friends, and communities before those of others. And third, human beings are *equal moral agents*, which means we should respect their lives and choices, and treat them with dignity, regardless of where they are, who they are, and whether they agree with us.

If we view those three starting points as relatively fixed constraints for political-economic policy, then perhaps at that point empirical investigation can help us determine which policies tend to promote our goals and which tend to inhibit them. All sides want human beings to flourish, and to have increasing opportunity to meet their needs so that they can progressively turn ever more of their attention to matters that can fill out a life of meaning and purpose—and, ultimately, happiness. Empirical investigation can then help us decide which available alternatives stand a relatively better chance of achieving those ends, given the three constraints above.

One final assumption is that no system of political economy is or can be perfect. Because our resources are always scarce relative to our needs and desires, and because human beings are imperfect both in their knowledge and in their virtue, heaven on earth will remain a dream and not become a reality. But what we can perhaps hope for is improvement. If not all needs and desires can be met, perhaps progressively more of them can be. If no life will ever be without hardship, perhaps we can address incrementally more of them to improve people’s lives, even if there will remain hardships to address. If injustice will continue to recur, perhaps we can reduce its frequency or its damage.

We might, then, restate the goal of an economically and morally attractive system of political economy as the striving for the conditions that enable human improvement by reducing scarcity or increasing prosperity, by channeling self-interest in mutually beneficial and productive directions, and by constructing public institutions that respect the liberty and dignity of all human beings, and do so equally, favouring or disfavouring none.

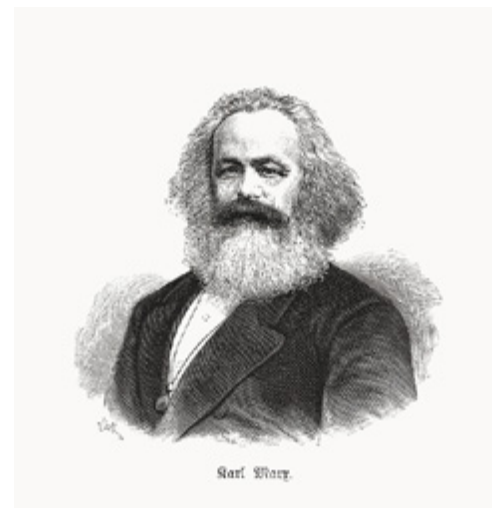
What would those political-economic institutions be? What purposes and scope of government activity would they encourage? To what extent should they protect private property rights? What should be their position on trade, taxation, or wealth redistribution? Should

they encourage more centralized economic decision-making, by government agents or experts, or more decentralized economic decision-making, by individuals themselves? More generally: What would be, if not the perfect, then perhaps the relatively better—or, indeed, perhaps the least bad—institutions that, if we endorse the goals of prosperity, progress, liberty, and dignity, we should support? On those grounds, we might be able to make some headway, and empirical investigation might help. The reports presented in this series aim to help us do just that.

The purpose of this introductory essay is to help set the terms of the debate and thus to enable readers of the country reports to assess them empirically and morally. We first define capitalism and socialism by looking at both the traditional and contemporary uses of the terms. Next, we consider the predicted outcomes from each system, which will give us something concrete against which we can judge what has resulted from what are essentially numerous experiments that have attempted to instantiate versions or approximations of these competing systems of political economy. And then, finally, we look at some of the evidence and see where that leads us.

### **Definitions**

The traditional definition of socialism is the public ownership of the means of production. Under Karl Marx's (1818–1883) recommendations, capitalism is a necessary but unhappy societal stage on the road to socialism and ultimately communism. As Marx put it in his 1848 *Manifesto of the Communist Party*, under the societal stage of capitalism, private property rights are introduced and lead to resolving human relations into a “cash nexus,” where the only value people constitute for one another is the extent to which each can profit from the other. Marx claims that this system thus dehumanizes us by reducing us to mere means to others' ends: not only what we make or produce becomes commodities that are bought and sold without regard for the human beings who made or produced them, but even people themselves become mere commodities, as their labour, skills, and abilities are also merely bought and sold. For Marx, capitalism is thus slavery by another name: “wage slavery.”



Marx claims that eventually workers, or “proletarians,” will waken to the dehumanized state to which capitalism inevitably reduces them, at which time they will reject the system based on private property that constructed their shackles and revolt. When they do so, they will seize the property of the owning class, or “bourgeoisie”; they will transfer ownership of all means of production to the people, and then will distribute the fruits of production according to need and the common good, not according to privilege or title.

Marx claims that this revolution will require violence. Because the bourgeoisie will not willingly give up their property and privilege, the proletariat's "ends can be attained only by the forcible overthrow of all existing social conditions." Once the violence of the revolution subsides, the hard work of comprehensively administering a state and its economy will then require a centrally organized authority. The state will then be administered by people Marx calls "Communists," who he claims are distinguished by their devotion to the good of all rather than merely themselves or one class opposed to another, and by their ability to perceive the social good that is often hard to identify for much of the proletariat: the Communists "always and everywhere represent the interests of the movement as a whole," and they alone "point out and bring to the front the common interests of the entire proletariat." These Communists will be "practically, the most advanced and resolute section of the working-class parties" and "theoretically, they have over the great mass of the proletariat the advantage of clearly understanding the line of march, the conditions, and the ultimate general results of the proletarian movement."

During this stage of "socialism," economic decisions will be made by the central state authorities, and they will be enforced coercively. Socialism therefore requires an expansive state; all property is owned in the name of the people and it is distributed, used, produced, and so on according to the directives of the state. Eventually, however, Marx believed that people would shed the capitalist "ideology" into which they had been enculturated in the prior phase of society's development, and so they will no longer require a state to administer their activities. They would themselves come to identify their own good with that of society, united in a common project of freedom and harmony. At that point, coercion is no longer required, and the state, as Marx's coauthor Friedrich Engels (1820–1895) would later put it, simply "withers away." Then, finally, we have society's ultimate and highest stage: communism.

Among those who claim to be socialists today, few endorse the complete abolition of private property and the state taking possession and claiming ownership of all means of production. Most today advocate state regulation of property, extensive welfare benefits, and redistribution of wealth intended to mitigate the alleged excesses and vices of capitalism and to spread the benefits of wealth. But reflecting on the original meaning of socialism can enable us to construct a spectrum on which we might be able to evaluate various programs, policies, and political-economic institutions that would be acceptable to proponents of competing systems today.

I propose this criterion for such a spectrum: Who is making the economic decisions in question? If a proposed program or policy empowers government authorities to make the decisions in question, then its tendency is toward *centralized* decision-making; if, on the other hand, it allows individuals to make their own decisions, then its tendency is toward *decentralized* decision-making. The former we might call "socialist-inclined"; the latter, "capitalist-inclined." This criterion has a correlated implication regarding the consequences of such decisions: "socialist-inclined" policies tend to distribute the



consequences of centralized decisions among all citizens, or large groups of citizens, while “capitalist-inclined” policies tend to let individuals themselves bear the consequences, good or bad, of their own decisions.

To illustrate, suppose a country is considering a reform of its health care system. If the proposal would allocate relatively more decision-making control to the government, or to government authorities, then we would classify it as “socialist-inclined” (if not fully “socialist”). If, on the other hand, it proposes to allocate relatively more decision-making control to individuals, then we would classify it as “capitalist-inclined” (if not fully “capitalist”). Similarly for educational policy, business policy, environmental policy, and a range of other issues. Income redistribution, for example, would typically be motivated by a “socialist-inclined” principle because it would act to rearrange decentrally negotiated or generated income based on centralized judgments about where income should go. On the basis of this criterion, then, we could form a relative judgment about an entire country’s economic system: if relatively more of its economic decisions are made centrally, then the country’s system would tend to be “socialist-inclined”; if relatively more of its economic decisions are made decentrally by individuals themselves, then the country’s system would tend to be “capitalist-inclined.”



Consider a recent proponent of socialism, G.A. Cohen (1941–2009), and his last book, *Why Not Socialism?* (2009). Cohen describes a camping trip with several families, and he argues that the campers would endorse socialist principles of equality and community: everything would be shared, with the “common aim” that “each of us should have a good time,” and we would avail ourselves of the various “facilities” we brought to the trip—including “pots and pans, oil, coffee, fishing rods, canoes, a

soccer ball, decks of cards, and so forth”—according to “collective control” organized communally so that “everybody has a roughly similar opportunity to flourish.” Cohen claims that we would endorse “collective control” in the camping trip both because it would enable everyone to flourish equally and because it would foster community rather than competition or the “greed and fear” he associates with capitalism. Cohen then goes on to argue that what we would endorse in a small social context like a camping trip we should also endorse on a larger national or even international scale.

The “collective control” Cohen describes would, especially as we move from small-scale to larger-scale groups, require centralized coordination and control. If individuals were to make their own decisions about how to allocate their time and resources, and about how to allow their possessions (or “facilities”) to be used, then this would lead to changing patterns of allocations that would inevitably fail to line up with the overall signature of

distribution that Cohen claims socialism requires. Thus, Cohen’s socialism would require centralized control to effectuate the equality and community he argues socialism champions (on Cohen’s assumption that centralized control would in fact lead to more equal distribution), which would make his proposal “socialist-inclined.”

At the other end of this political-economic spectrum, consider the 1945 essay by Nobel laureate Friedrich Hayek (1899–1992), “The Use of Knowledge in Society.” There, Hayek argues that to have a chance at constructing a “rational economic order”—that is, one in which our scarce resources are allocated first to their most important uses, then second to their second most important uses, and so on down the line of our priorities—we must draw on specific “relevant information,” including people’s “given system of preferences” and our “knowledge of available means” to satisfy people’s preferences. The problem, however, according to Hayek, is that such information is “never for the whole society ‘given’ to a single mind which could work out the implications and can never be so given.” Why not? Because the relevant knowledge is contained in discrete “dispersed bits” scattered across billions of brains. You have some of it, I have some of it, and everyone else has some of it; but no single person, and no single group of persons, has all of it—especially as it continually changes in response to “changes in the particular circumstances of time and place.”

The only chance we have at approximating a rational economic order, Hayek argues, is by relying on prices that emerge from the choices people make in their particular circumstances, based on their localized knowledge of their own (changing) values, opportunities, and resources. If prices are allowed to move freely, Hayek argues that they will contain just the needed information—about people’s preferences, their available means, and so on—required to make suggestions about where our scarce resources should go first, then second, and so on. Key for Hayek’s argument is that the price mechanism can contain this needed information only if people are allowed to make decisions for themselves decentrally, based on their own assessments of their situations and drawing on their own unique possession of localized knowledge. Hayek’s argument thus calls for more economic decisions to be made by individuals than by centralized authorities, which would make his argument “capitalist-inclined” based on our taxonomy.

**“Hayek’s argument calls for more economic decisions to be made by individuals than by centralized authorities, which would make his argument ‘capitalist-inclined’ based on our taxonomy.”**

### ***Predictions regarding socialist- vs. capitalist-inclined policy***

Would centralized control of economic decisions in a country lead to the flourishing that Marx, Cohen, and other supporters of socialism claim? Or would decentralized economic decision-making foster the “rational economic order”—and increasing prosperity—as Hayek and other supporters of capitalism maintain? Alternatively, would a “middle way” set of institutions that allows some protection of private decision-making coupled

with some measure of centralized redistribution or decision-making—as, for example, one might find in Scandinavian countries—lead to greater flourishing than would either of the ends of the decision-making spectrum? Most countries fall somewhere on the scale between fully centralized and fully decentralized. Perhaps there is some point on the spectrum that is optimal? Perhaps, that is, neither the socialist model nor the capitalist model engenders the most prosperity, but somewhere between does?

These are ultimately empirical questions, and what could help us decide them is if we had data across various measures of human well-being for countries, territories, states, and so on that fell along various points on the spectrum. If we studied various countries' political-economic institutions and could list them on a scale from most “socialist-inclined” to most “capitalist-inclined,” we could then compare that ordered list to their attainments on various measures of well-being. In that way, we might be able to draw some conclusions about what kinds of institutions seem to lead to increases in human flourishing and what kinds seem to lead to decreases, and we could thus make recommendations based on empirical evidence rather than on intuitions or guesses.

That is precisely what numerous investigations have sought to determine,<sup>3</sup> with the Fraser Institute's annual *Economic Freedom of the World* report most prominent among them (Gwartney, Lawson, Hall, and Murphy, 2021). The reports contained herein provide further evidence.

If we consider the centralized vs. decentralized decision-making criterion, and the scale or spectrum that falls between those two poles, we might also be able to make some theoretical predictions that empirical findings could corroborate or falsify. Let us consider two such theoretical predictions, the Local Knowledge Argument and the Day Two Problem.

### ***The Local Knowledge Argument***

The first prediction derives from what I call the “Local Knowledge Argument,” articulated by Adam Smith (1723–1790) and elaborated by Frédéric Bastiat (1801–1850), Hayek, and others. In his 1776 *Wealth of Nations*, Smith writes, “What is the species of domestic industry which his capital can employ, and of which the produce is likely to be of the greatest value, every individual, it is evident, can, in his local situation, judge much better than any statesman or lawgiver can do for him” (1776/1981: 456). Smith's Local Knowledge Argument proceeds as a three-step syllogism:

- Premise 1: People's individual situations, along with their values, purposes, and opportunities, are known best by individuals themselves.
- Premise 2: To be made wisely, decisions about allocating resources must exploit knowledge of situation, value, purpose, and opportunity.
- Conclusion: Therefore, the person best positioned to make such decisions is the individual.

Smith's argument is not that individuals are infallible, only that they are in possession of more information about their own situations than are distant others, and thus that they are in a relatively better position to make wise decisions about allocating their own resources than are people who know their situations little or not at all. His Local Knowledge Argument thus recommends decentralized economic decision-making, and it makes the empirically testable prediction that countries that allow relatively more decentralized decision-making will prosper more than will countries that instead engage in relatively more centralized decision-making.

Similarly, Bastiat's 1850 "What Is Seen and What Is Not Seen" points out that for every allocation of resources, there is an "unseen" opportunity cost—what is given up when we allocate scarce resources to one end rather than to any of the indefinitely many alternative ends to which we might have dedicated them. Bastiat's argument implies that finding a beneficial end toward which to dedicate scarce resources does not yet by itself mean that we should do so: before deciding, we must compare the potential good results from other possible allocations. Perhaps dedicating resources here leads to beneficial results, but dedicating those same resources there could lead to even more benefit. So *good*, by itself, is not yet *good enough*; it must instead be *better than*.

Estimating opportunity cost is difficult, however, because it involves imagining what might have been but was not; yet it is even more difficult—perhaps indeed impossible—to do from afar. So, it is challenging for me to estimate the opportunity cost of, say, dedicating my time to write this essay; but it would be extremely difficult, perhaps impossible, for me to estimate the opportunity cost to you of the time you will spend reading it. I would have to know what your resources are, what your values and goals are, and what your other opportunities are—all in real time. This is information I simply do not possess. What might reveal your opportunity cost, however, is your behaviour: for example, how much you or other potential readers would pay for this essay if it were sold in a competitive market. As Hayek argued, prices are generated on the basis of people's decentralized choices about how to allocate their scarce resources; as such, they contain real information about people's values and goals, opportunities, resources, etc. that third parties, including government planners, would have no other way to assess.

**"As Hayek argued, prices are generated on the basis of people's decentralized choices about how to allocate their scarce resources."**

The Local Knowledge Argument holds that the person who possesses this relevant information about any given individual, and likely more of it than anyone else, is the individual; hence, it concludes that it is the individual who should make decisions about how to allocate his or her resources, not third parties or distant government agents. The prices that arise from such decisions would reflect individuals' localized knowledge, which cannot otherwise be known by such centralized parties. Hence, the empirically testable implication would again be that countries that allow people relatively more authority over making their own decisions about allocating resources—in other words, allowing

for decentralized decision-making—will tend to use their resources more productively and with less waste than will countries with the opposite policies—and in so doing will achieve better outcomes.

Finally, Hayek claims that the knowledge required to enable the price mechanism to perform the “marvel” (his word) of coordinating the economic decisions of indefinitely many disparate individuals in their varied, unique circumstances can arise only if people are allowed to make such decisions for themselves. This part of Hayek’s argument



is based on two critical assumptions: first, that individuals possess the private property rights required to enable them to make their own decisions about how to allocate their resources; and second, that the consequences of the decisions they make, whether good or bad, accrue principally to them. If I do not possess rights over my property, then I cannot make my own decisions about how to use or allocate it; in that case, prices with their real information do not arise. And to whatever extent others bear the consequences of my decisions, the feedback I require

to improve my judgment or make better decisions is diminished, and I do not have the incentive to search for more efficient or productive use of my time, talent, or treasure. Both these assumptions are sensitive to degree. That is, if I bear some proportion of decision-making authority over my own resources, and if I receive some proportion of the consequences of my decisions, then the prediction would be that as the proportion allotted to me decreases, so does the value of the information from the price signal and hence so does the potentially beneficial effects of capitalizing on localized knowledge.

This part of Hayek’s argument could thus also shed light on contemporary advocacy of “mixed” economies, “social democracy” (instead of “socialism”), Scandinavian “third way” systems, and so on. As these countries substitute, to varying extents, centralized decision-making for decentralized decision-making, the Hayekian argument would predict that those relative proportions should indicate where such countries fall on efficient and productive uses of resources and thus ultimately on indices of human well-being. Here, then, is another empirically testable prediction: those countries that allow more decentralized decision-making will see progressively more efficient and productive uses of their resources and thus improved human well-being than countries that instead increase the proportion of such decisions made by centralized authorities.

### ***The Day Two Problem***

One central motivation behind socialist-inclined proposals is to remedy what are perceived as problematic distributions of wealth or resources. Perhaps people believe that there is too much wealth or income inequality in society, or perhaps some worthy causes

go wanting for lack of resources, while some unworthy causes receive funding or are otherwise profitable. In such cases, one might argue that a centralized redistribution of resources can remedy either, or both, of these inequities. Such concerns motivate much socialist-inclined policy, including everything from progressive taxation to inheritance taxes to luxury taxes to taxation to support public education and provide aid to the poor.

A challenge facing such redistribution, however, is what I call the Day Two Problem, so-called because the problems redistribution addresses on Day One recur, and perhaps even worsen, on Day Two, thus diminishing redistribution's effectiveness. The Day Two Problem has, in fact, two parts, both empirically testable. The first part of the Day Two Problem is that once we have determined what the proper distribution of wealth should be and have effectuated that proper distribution (putting aside difficulties associated with determining what the proper distribution is or should be, implementation, and so on), by the next day things would no longer conform to the pattern we wanted. The reason is that human beings are unpredictable. They have their own ideas; their values, desires, goals, and circumstances change; and thus there is little reason to believe they will—if allowed any freedom to make decisions for themselves—continue to behave and choose in accordance with our preferred pattern of distribution. In fact, the Local Knowledge Argument gives us reason to expect they will not comport with our pattern: if people know their own situations better than centralized planners do or can, and if their behaviour and choices will reflect knowledge of their situations that centralized planners do not possess and thus cannot anticipate, the prediction is that they will indeed deviate from our preferred pattern.

That prediction leads to the second part of the Day Two Problem. To remedy the departures from our initial preferred distribution, we would have to redistribute again. But then people will again deviate, which will necessitate a re-redistribution; and so on, indefinitely. There would be no stopping point. And at each stage we would face increasing costs associated with the process of redistribution itself (monitoring, resource aggregation and collection, resource (re-)redistribution, (re-)assessment, and so on). Hence, we would face increasingly diminishing returns from redistribution. We might additionally create an increasing disincentive for people to produce wealth in the first place—which requires effort, after all—if they know that some antecedently unspecified portion of it can or will be taken from them and redistributed elsewhere.

Of course, a market, or “capitalist-inclined,” system also continually redistributes resources and creates its own patterns of incentives. But if the consequences of decentralized decisions, whether good or bad, are experienced principally by those making the decisions, then those individuals have an incentive to pursue positive outcomes and avoid or abandon negative outcomes. By contrast, under centralized decision-making,

**“If the consequences of decentralized decisions, whether good or bad, are experienced principally by those making the decisions, then those individuals have an incentive to pursue positive outcomes and avoid or abandon negative outcomes”**

the consequences tend to be experienced by people other than the decision-makers (i.e., citizens, not the centralized planners), blunting the effectiveness of the feedback.

The Day Two Problem thus predicts that the would-be centralized planner would face the following dilemma: either give up altogether on the project of redistributing wealth to achieve a preferred distribution, thus reverting to the decentralized model recommended by Smith, Bastiat, and Hayek; or continue (re-)redistributing wealth, and redoubling the efforts indefinitely, with increasingly diminishing returns.

As in the case with the Local Knowledge Argument, the Day Two Problem leads to empirically testable predictions: countries that engage in continuous wealth redistribution will, depending on the extent to which they do so, experience either forgone prosperity (that is, less prosperity than they otherwise would have had) or even, if the redistribution is sufficiently extensive, diminishing prosperity. Moreover, once countries have enacted policies of wealth redistribution, they are unlikely to stop; instead, they will likely increase their redistributive activities progressively over time to correct for misalignments and mismatches between their preferred outcome patterns and the patterns that in fact arise.

### What does the evidence show?

The Local Knowledge Argument and the Day Two Problem predict that countries with relatively less centralized economic decision-making—that is, more “capitalist-inclined”



countries—would see citizens faring better on a broad range of elements of human well-being than countries with relatively more centralized decision-making—that is, more “socialist-inclined” countries. For several decades now, researchers have been generating and assessing data that might help us test these predictions. What has the evidence shown?

The reports contained in this series are some of the most recent attempts to assess new evidence as it bears on these questions. Evidence seems

to be converging on the thesis that the more “capitalist-inclined” a country’s policies are, the better its citizens tend to fare on a wide range of metrics, while the more “socialist-inclined” a country’s policies are, the worse its citizens tend to fare on those same metrics. These metrics include important aspects of human well-being: not just wealth, but longevity, education levels, access to health care, decreases in poverty rates, improving nutrition, decreasing rates of violence, increasing rates of inoculation, increasing access to the internet, and even increasing self-reported happiness. Although this evidence does not suggest that wealth cures all problems, much less that wealth is equivalent to happiness, what it does suggest is that the increasing wealth generated in relatively decentralized economies enables people to address their more pressing needs—such as food, clothing,

and shelter—and thus turn their attention incrementally but progressively to other things that can fill out flourishing lives of meaning and purpose.

### ***A Middle Way? The Case of Sweden***

The evidence also suggests that the so-called soft socialism advocated by “democratic socialists” such as U.S. Senator Bernie Sanders, or the mixture of market-based economies coupled with substantial welfare states and wealth redistribution in, for example, Scandinavian countries, turns out to follow the predicted pattern. That is, the relative proportion of centralized economic decision-making, including through governmental wealth redistribution, is inversely correlated with their material prosperity and with other measurements of well-being. Because many supporters of socialist-inclined policy point to Sweden as a model, its case is perhaps worth a few more words.



Free-market reforms in the 1860s allowed Sweden to begin enjoying the gains in productivity that were occurring elsewhere during the Industrial Revolution. These reforms led to an explosion of innovation and entrepreneurship, including the founding of iconic Swedish companies like IKEA, Volvo, and Ericsson. In the late 1930s, Sweden decided it could sustain its robust growth while at the same time creating a welfare state that included modest worker and retirement benefits, unemployment protections, and so on. Its previously ignited economic engine enabled it to continue growing into the 1950s, at which time Sweden decided to expand its centralizing efforts dramatically: government spending of the country’s gross domestic product went from averaging less than 10 percent from 1870 to 1938, to approximately 20 percent in 1950, and then to fully 50 percent in 1975.

Despite its small and relatively homogeneous population, and despite its cultural consensus in favour of both income equality and hard work, this level of economic centralization eventually proved too much for Sweden to sustain. A series of economic shocks ensued, which led, over the next two decades, to currency devaluations, inflation, rising unemployment, stagnating production, and anemic growth. Matters came to a head when its fixed exchange rate policy collapsed in 1992. This led Sweden to rethink its priorities: it began privatizing state-owned companies, deregulating parts of the economy, and scaling back its welfare state.

This re-transition to its previous free-market success was bumpy and difficult, but Sweden’s economy began showing signs of returning to growth and vitality. Sweden eliminated its inheritance tax in 2005, its wealth tax in 2007, and its taxes on residential property in



2008; it cut taxes on labour and disallowed union membership dues from qualifying for tax relief; it installed a competitive voucher system for education and allowed a growing private health care system; and it made all its welfare benefits less generous. These reforms have led to a mild increase in material inequality in this country that formerly led the world in its material equality, but the tradeoff has been that now more people work, its economy is growing, and the country is reducing its debt. According to a recent study, “Sweden implemented a reform package that ignited a successful reorganization of a business sector that had faltered for decades”; the study continues that the “removal of barriers to growth for new and productive firms, as well as increased rewards for investment in human capital, were crucial to the success of Sweden’s reforms,” and concludes that “the Swedish experience can be a valuable case study for developing countries that are attempting to promote growth by developing their business sectors” (Heyman, Norbäck, and Persson 2019).<sup>4</sup>

## Conclusion

It bears repeating that countries with decentralized, “capitalist-inclined” economies do not flow only with milk and honey. There remain problems to solve, not least because it seems to be an endemic feature of the human condition that no matter how much we have, we still want more and needs still go unmet. Because the human condition is dynamic and ever changing, our needs also evolve over time. It is also the case that wealth itself can generate new kinds of problems, perhaps including the rising rates of anxiety, depression, drug (over)use, and suicide that seem particularly evident in many wealthier countries today. So, things are far from perfect and much remains to be done. Yet, as we noted at the outset, we should beware of falling prey to the tendency to compare our situation to an imagined state of utopian perfection, because perfection is not possible for imperfect creatures. All systems of political-economy—socialist, “socialist-inclined,” “capitalist-inclined,” capitalist, and everywhere in between—are imperfect. The proper standard is thus instead what is *comparatively better*. Among the available alternatives, and among the hundreds, or thousands, of experiments in social organization and institutions humans have and are experimenting with, in which do people seem to fare relatively better over time than in others? Assessing all the data we can, and reviewing it as objectively and dispassionately as we can, which sets of institutions seem to allow greater well-being, all things considered?

That, ultimately, is the question all such empirical investigation aims to address and is indeed the ultimate question the reports included in this series are meant to help assess. As you review these reports, I invite you to keep this question in mind: what do they suggest about the political-economic institutions that enable relatively greater well-being? Because human beings are so greatly affected by the institutions their countries adopt, and because human lives can even depend upon them, the answer to this question could not have more moral weight. These are, after all, not mere matters of historical curiosity: real human lives lie behind them. If we can generate and assess real data that can enable us to give credible answers to this question, then pursuing them, analyzing the data objectively,

and making the best even tentative recommendations we can on their basis is not merely an academic exercise: it is a moral responsibility.

## Endnotes

- 1 See, for example, Deaton (2013), Van Zanden et al. (2014), Goldin and Kutarna (2017), Tupy (2017; 2019), Davies (2019), and Bailey and Tupy (2020). See also “Sources and further reading” at the end.
- 2 See, for example, Maddison (2007), Pinker (2018), Rosling et al. (2018), and McAfee (2019).
- 3 See, for example, the United Nations Human Development Index. See also Phelps (2013); McCloskey (2016); Pinker (2018); Lawson, Murphy, and Powell (2020); and McCloskey and Carden (2020).
- 4 See also Otteson (2014), chap. 5. Other Scandinavian countries have also struggled in recent years to sustain their generous welfare and wealth redistribution programs. See, for example, Gronholt-Pedersen (2019).

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\*All links current as of June 7, 2022.

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