In Janos Kornai's memory

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Janos Kornai, emeritus professor of Harvard University and Corvinus University Budapest, passed away in his sleep at home on Monday evening, October 18, 2021, at the age of 93. Bearing the departure of his beloved wife, Zsuzsa Dániel, a Hungarian economist (see her short autobiography in Dániel, 2015), a few years earlier was not easy for Janos. While he continued to write and publish until the last hours of his life, his deteriorating state of health could not let him to do as much as he wished.

His last body of work particularly focused on China's 'monstrous' U-turn, and the autocratic U-turn in Hungary under Victor Oban, and many other ex-Soviet type economies. He wrote a pair of articles on China, first in the *Financial Times* (Kornai, 2019a) and then a long complementary article titled 'Frankenstein's moral responsibility' (Kornai, 2019b). In those last papers, he was warning against the rise of 'autocracy', which he defined as a political regime between democracy and dictatorship. The subtitle of his paper on China was: "Western intellectuals must now seek to contain Beijing". Earlier, he had written about Hungary's U-turn away from democracy: "Hungary is turning away from the great achievements of the 1989–1990 change of regime—democracy, rule of law, free-working civil society, pluralism in intellectual life—and is attacking private property and the mechanisms of the free market before the eyes of the whole world" (Kornai, 2015).

Kornai (1990b) was an advocate of private property and market-based economies since he concluded that democracy could survive only under such economic conditions. In other words, his fundamental moral value rested on *democratic principles*, particularly the rule of law, a free civil-society, and pluralism in political and intellectual life. In his opinion, the socialist system characterized by the Communist Party's monopoly of power, the preponderance of state property and bureaucratic coordination were antinomic to democracy.

When *Public Choice* decided to devote a special issue "In honor of Janos Kornai" (published in April 2021, vol. 187, nos. 1–2), and invited me to act as a guest editor, I contacted Janos to learn if he would like to contribute to this volume. He decided to submit his personal memoir, "1956 in Hungary: as I saw then and I see it now" (Kornai, 2021). The choice was symbolic and particularly meaningful. He concluded the paper by citing the closing words of Péter Nádas's autobiography, published in 2017: "I can say without any overtone of pathos or sadness that all my life I have felt as if I was doubly bleeding. I have always detested autocracy, but at the same time I have been unable to ignore

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the difficulties, the cheap melodrama and the self-destructive partiality of the republic and democracy. I am truly sorry.”

Janos likewise was ‘truly sorry’ and considered himself to have been *intellectually* responsible both for the Chinese Frankenstein and the Hungarian U-turn. He too was disillusioned about his expectations in 1989–1990 and expressed it in a footnote in the same paper: “Now I see that my expectations about the benefits to come from capitalism and democracy were unrealistic. More than six decades later, the image formed in me is much more sober. I know how much injustice and inordinate income-inequality is born of capitalism. The institutions of democracy are unable to prevent the abuse of power and corruption, albeit to different degrees in different countries” (Kornai, 2021).

One of Kornai’s idiosyncratic personal qualities was intellectual honesty. He often looked backward critically to assess his theoretical predictions and questioned them boldly if he would find them incorrect. I just cited two cases of his self-criticism regarding China and his expectations in 1989–1990. His moral attachment to democracy, shaped by his bitter personal experiences with fascism and communism. The evidence is provided in his autobiography *By Force of Thought* (Kornai, 2006).

Born into a Jewish family on January 21, 1928, Kornai was the son of an attorney, Dr Pal Kornhauser, and a loving mother, Aranka Schatz, (called Munyo by her children), to whom Kornai dedicated his autobiography. It was in 1945 that Kornai decided of his own accord to take the name Kornai.

Specializing in the Hungarian business affairs of German companies, his father was a prosperous man of law and culture until the ascent of Hitler to power and the transformation of Nazism into a totalitarian system. He then lost all his German clients gradually and finally met his end in Auschwitz after the occupation of Hungary by Germany on March 19, 1944. Kornai’s older brother, Bandi, also punished for being a Jew and enduring forced labor under Hungarian military command eventually died of exposure or illness. Kornai himself, wearing the compulsory yellow star and working as a manual laborer at the Bricks works, finally escaped to Pest in the Swedish squad¹ and then hid in a Jesuit monastery before being liberated by the Russian Red Army, just a few days short of his 17th birthday.

The trauma of March 1944, the Horthy regime, and the search for a guarantee against the resurgence of fascism, caused Janos to sympathize with the Hungarian Communist Party. But his ‘unconditional belief’ in the Soviet Union and the Communist Party could not be reduced entirely to psychology.

Reading Marx’s *Capital* affected his way of thinking forever, even when he called himself “anti-Marxist” (Kornai, 2009). From a theoretical point of view, his two principal sources of inspiration were Marx and Hayek (Leeson, 2008; Vahabi, 2021a, 2021b). In fact, he was influenced so greatly by *Capital* that he decided to become an economist (Sen 2020). But Kornai did not believe in what he called Marx’s dogma, namely dictatorship of the proletariat and the labor theory of value. He had rejected Marx’s labor theory in 1955–1956 when he was defending his Ph.D. thesis on *Overcentralization* (Kornai, 1959/1994). In his opinion, Marx bore the ‘intellectual responsibility’ for the political and economic system created by Lenin and Stalin in Russia and other ex-Socialist countries. When Amartya Sen’s (2020) excellent contribution to the special issue, titled “Marx after

¹ The Swedish squad was created by Raoul Walenberg, the heroic Swedish diplomat, who tried to carry out a rescue campaign all over Budapest by issuing protective documents to non-Swedish citizens in Hungary. The young Janos obtained a “letter of safe conduct” from the Swedish Embassy in Budapest; the document was decisive in organizing his trip (see Kornai 2006, p. 18).

Kornai”, was published, Janos criticized Sen’s views on Marx and advocated ‘anti-Marxism’ because of Marx’s “intellectual responsibility”. The exchange between the two long-time friends and eminent economists is rich with insights for understanding Janos’s complex relationship with Marx (see Vahabi, 2021c).

Again, the ground for Kornai’s rupture with Marxism and Communism was prepared by psychological dissonance and disillusionment. Kornai’s wakeup call putting an end to his ‘unconditional faith’ in the Soviet Union and the Communist Party came after the death of Stalin on March 5, 1953. The post-Stalin period in Hungary, resulting in the replacement of Rakosi by Imre Nagy as prime minister and the inception of the “New Course”, opened the doors of secret files documenting tortures and forced confessions of ‘non-loyal’ communists.² That trauma broke the ethical foundations of Kornai’s beliefs in the summer 1954. Kornai also started to grasp that many official economic figures were based on unrealistic plan targets detrimental to people’s daily lives. Kornai’s first insubordination as a journalist for *Szabad Nep* was to decline writing an article in 1954 attributing the ‘electricity shortage’ to ‘objective conditions’ instead of erroneous assessments of the country’s electricity needs by the planning authorities. While the “New Course” was a wakeup call, the 1956 Hungarian Revolution turned the page for Kornai (2021), who abandoned the Communist Party forever.

Kornai’s true intellectual journey as an autodidact economist started with his PhD dissertation. The originality of that work, noticed both in the East and the West (Gregory 2021), was its positive analysis of the economic conditions under socialism.

There are, of course, dozens of textbooks and collection of notes for use at universities which describe our methods of economic administration and planning, our pricing and wage systems, etc. However, all of these have a serious fault in common: instead of telling us how our economic mechanisms works *in reality*, they merely describe how it would work if it worked as their authors would wish... A coherent description of how the mechanism of our economy really does work represents a new task, not hitherto performed in the economic literature of our country. (Kornai, 1959/1994, pp. viii–ix)

The book was not about normative or doctrinal ‘laws’ and ‘principles of socialism; it contained only one quotation from Marx on shortages in a chapter devoted to a problem that later became a central issue of Kornai’s (1980) writings, *The Economics of Shortage*. *Overcentralization* showed how close a relation exists between shortage and centralization, how shortage increased the tendency to centralization and centralization in turn induced shortage. Kornai’s (1959/1994, p. 215) main message was that “excessive centralization is a coherent, unified mechanism, which has its own inner logic and several tendencies and regularities peculiar to itself.” While Marx’s labor theory was absent, Kornai’s systemic method was at work.

Despite its systemic approach, *Overcentralization* stopped at a critical point in its causal analysis. It established that among the causes of the problems of planning are the command economy, extreme centralization, and exclusion of market coordination. But it did not go deeper: “it does not recognise the basic contribution to dysfunctional operation of the economy made by political oppression, ideological monopoly, and state ownership

² Kornai (2006, p. 61) truly was appalled by the numbers of imprisonments and internments: “One figure I remember was more than 40,000 political prisoners in Hungary at the time of Stalin’s death, out of a population of less than 10 million.”

squeezing out private property.... [T]he maturation process took me longer. I still believed the Socialist economy could be reformed. I was still a *naïve reformer*, as I described my 1956 state of mind in a later piece of writing” (Kornai, 2006, p. 93).

The maturation process went through three major phases, each divisible into subperiods. The first phase began with Kornai’s Ph.D. thesis and ended with his masterpiece *The Economics of Shortage* in 1980. During that phase Kornai insisted on the primary role of *economic factors in explaining institutions*. He developed a specific type of comparative economic study of socialism and capitalism in terms of ‘sellers’ markets’ versus ‘buyers’ markets’ that he called ‘pressure’ and ‘suction’. The first phase can be separated in two subperiods.

The first subperiod covers Kornai’s works from *Overcentralization* to *Anti-Equilibrium* (1971). At the start, Kornai was an advocate of market socialism; he even improved upon Oscar Lange’s model in his paper with Liptak on a “Two-level Planning”, published in 1965 in *Econometrica* (Andreff, 2021). At the end of that subperiod, Kornai became a critic of the Walrasian general equilibrium. He started keeping distance from Lange and approaching von Mises and Hayek (Boettke & Candela, 2021). Kornai also mobilized the Marshallian concept of ‘normal state’ (Vahabi, 1998) to argue that each economic system should be characterized by its specific *chronic disequilibria* rather than by its equilibrium states. Accordingly, capitalism was grasped as a ‘surplus’ economy³ in sharp contrast to socialism as a ‘shortage’ economy.

The second subperiod runs from *Anti-Equilibrium* to *The Economics of Shortage* (1980). During that time, Kornai formulated the original concept of *soft budget constraint* (SBC) versus *hard budget constraint* (HBC). SBC described an *empirical* fact regarding the behavioral regularities of a socialist plant director who could spend more than his revenue expecting a bailout of the socialist enterprise in case of grave financial difficulties. By contrast, HBC applied to the behavioral regularities of a capitalist enterprise within a competitive market economy. SBC was a heretical concept not only for mainstream economics then, but also for the neo-Keynesian economics advocated by Clower, Leijonhufvud, Portes, and many others. Kornai defined a budget constraint not as an *accounting identity* or a *rational postulate* but as an *empirical fact* (Vahabi, 2001). The concept could be interpreted as a rediscovery of the Austrian criticism of Lange’s position (Streissler, 1991). Boettke and Candela also reformulated an original Austrian version, according to which soft budget constraints are a *consequence* of competition between firms in a non-profit setting.

The second phase started with *The Economics of Shortage* and ended with his classical textbook *The Political Economy of Communism* (Kornai, 1992) taught at Harvard. In the same period, Kornai criticized his previous approach and argued for the primary role of *institutional* factors in economic performance. He argued specifically that institutional coordination mechanisms determine economic factors. For example, SBCs are created by bureaucratic rules adopted to implement *State paternalism*. He also formulated an ‘affinity thesis’ (Kornai, 1990a) in explaining the relationship between coordination mechanisms and property relationships. Janos distinguished between ‘weak’ and ‘strong’ linkages. Private property and market coordination forged ‘strong’ linkages, whereas state property and market coordination maintained weak linkages. During his

³ Kornai (2013) later published a book in which capitalism’s dynamism and rivalry are explained in terms of the ‘surplus’ economy.

second phase, Janos avoided analyses of political systems, focusing instead on coordination mechanisms and property relationships.

The third phase started in 1992 and continued until his last works. It was a period during which Janos insisted on *political economy*, particularly on politics as one among the institutional factors determining economic performance. In his opinion, three fundamental institutional blocs, namely political system, property ownership and coordination mechanisms, are decisive.

The April 2021 special issue of *Public Choice* “In Honor of Janos Kornai” covers all three phases of his intellectual life. Each of the 15 papers comprising the volume summarizes one aspect of Kornai’s contributions or discusses the relevance of his concepts, such as the ‘soft budget constraint’, in addressing new economic problems (Leeson et al. 2020; Maurel and Pernet 2020; Xu et al. 2020) or his political economy approach to autocracy in China, Hungary and Turkey (Gorodnichenko & Roland, 2021; Mihályi & Szelényi, 2020; Rosta & Tóth, 2021; Hénin & Insel, 2021). While Kornai’s works were received warmly both in the Western and Eastern countries and the issue’s contributors wrote of the benefits of his comparative economic approach, each emphasized one specific strand of his intellectual life.

According to Olivier Blanchard (1999) in his interview with Kornai, the conceptualization of soft budget constraints was Kornai’s main contribution to our discipline. It is true that a soft budget constraint was accepted by mainstream economists and ultimately led to a formal (game theoretical) strand of literature probing it. But was that idea Kornai’s main contribution in the eyes of people living in the East under the socialist system? According to Kornai (1999, p. 439), “The concept of soft budget constraint had a much stronger impact on the profession in the West than in the East. It presents something that fits in with neo-classical thinking, but at the same time, steps out of it a bit, and brings some improvement on it. I think that’s why it was and has remained influential.” However, the SBC idea has not been regarded as Kornai’s main contribution in the East.

For the Chinese, Russian, and virtually all Eastern European readers of *Economics of Shortage*, Kornai’s principal message was that the dysfunctional properties of socialism were endemic, systemic, and could not be reformed. Kornai’s maturation process traversed the same three phases. He was first a *naïve reformer* in 1956, but transformed into a critic of market socialism in 1971. His critical assessment of market socialism prompted him to adopt the Austrian position on the socialist calculation debate and market rivalry (Kornai, 1980, 1986). He finally and explicitly advocated private property rights as indispensable in achieving a full-fledged market economy (Kornai, 1990a, 1990b). He abandoned reformism in favor of transformism.

As I wrote in my contribution to the special issue,

In a sense, Kornai’s role was similar to that of the French Encyclopedists in preparing the ground for France’s 1789 revolution. Kornai’s intellectual contribution was to formulate a revolutionary discourse emphasizing the sterility of half-measure, cosmetic changes, and reform packages. Kornai’s revolutionary discourse on the non-reformability of the socialist system rests on two foundations: (1) the unity or what Kornai calls the coherence of socialism as a system, and (2) rejection of so-called market socialism. Accordingly, reforms could only introduce inconsistencies without solving the system’s chronic problems. Moreover, the inconsistencies of the half-measures would erode socialist systems, inevitably leading to revolution. (Vahabi, 2021a, 2021b, 2021c)

Kornai was both a true scholar and a committed public intellectual. He never lost his strong sense of observation and remained uninfluenced by doctrinal biases despite his moral commitment to democratic values. For him, economics served as a source of fundamental knowledge of society and of social change.

I would like to finish this note by saying that Janos will be missed by many: not only by his daughter and two sons, his grandchildren and all his family, but also by his numerous friends, colleagues, and students all over the world. Our profession lost one of its most brilliant minds; I lost a mentor and a friend.

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