

GEORGE SOROS

THE
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LECTURES

AT THE CENTRAL EUROPEAN UNIVERSITY



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LECTURE THREE



OPEN SOCIETY

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TODAY I SHALL INTRODUCE the third pillar of my conceptual framework, namely, open society. In the previous lectures I was summarizing the conclusions of a lifetime of study and experimentation. Here I will be breaking new ground because my views on open society have changed over time and they are still evolving. As a result, the next two lectures will be much more exploratory in character.

The connection between open society and reflexivity is far from obvious. On a personal level they are closely connected. As

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you will recall, I was studying economic theory and at the same time I was reading Karl Popper's *Open Society and Its Enemies*. It was Popper's insistence on our inherent fallibility that led me to question the basic assumptions of economic theory and develop the concept of reflexivity.

But on a conceptual level the connection is only indirect. It is the first pillar, fallibility, that connects the other two. Fallibility in this context means not only that our view of the world is always incomplete and distorted but also that in our effort to simplify an extremely complex reality, we often misconstrue it. And our misconceptions play an important role in shaping the course of history.

If there is anything really original in my thinking it is this emphasis on misconceptions. It provides a strong argument in favor of critical thinking and open society.

POPPER DID NOT GIVE an exact definition of open society because he considered exact definitions incompatible with our imperfect understanding. He preferred to approach things from the opposite direction, by first describing them and then giving them a label. The form of social organization he named "open society" bore a close resemblance to democracy.

The net effect of his approach was to justify democracy by an epistemological argument. Since perfect knowledge is beyond the scope of the human intellect, a society characterized by the freedom

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of speech and thought and free elections is preferable to a society that imposes its ideology by force. Having been exposed to Nazi persecution and Communist oppression, I found this argument very persuasive.

Popper's philosophy made me more sensitive to the role of misconceptions in financial markets, and the concept of reflexivity allowed me to develop my theory of bubbles. This gave me a leg up as a market participant.

After a successful run as a hedge fund manager I went through a kind of midlife crisis. I was approaching fifty. My hedge fund had grown to \$100 million, of which about \$40 million belonged to me personally. I felt that I had made more than enough money for myself and my family, and running a hedge fund was extremely stressful and depleting. What would make it worthwhile to continue?

I thought long and hard and finally I decided to set up a foundation devoted to the promotion of open society. I defined its mission as opening up closed societies, correcting the deficiencies of open societies, and promoting a critical mode of thinking.

As time went by, I became increasingly involved in philanthropy. I established a foundation in Hungary in 1984 when it was still under Communist rule, in China in 1986, and in Poland and the Soviet Union in 1987. And as the Soviet Union and Yugoslavia disintegrated, I set up a network of foundations that covered almost the entire former Communist world.

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In this way I acquired some practical experience in building open societies. I learned a lot. I discovered things that I should have known in the first place—for instance, the disintegration of closed societies does not necessarily lead to the birth of open societies; it may just result in a continuing disintegration until a new regime emerges that bears more resemblance to the regime that had collapsed than to an open society.

THE EVENT THAT FORCED me to thoroughly reconsider the concept of open society was the reelection of George W. Bush in the United States in 2004. Here was the oldest and most successful democracy in the world violating the principles for which it was supposed to stand by engaging in human rights violations in the name of fighting a war on terror and invading Iraq on false pretenses. Yet, he was reelected. How was that possible? I had to ask myself: what was wrong with America? I wrote a couple of books trying to answer that question. I blamed the Bush administration for misleading the people and I blamed the people for allowing the Bush administration to mislead them.

As I probed deeper, I started to question my own conceptual framework. I discovered a flaw in the concept of open society. Popper was mainly concerned with the problems of understanding of reality. He put forward an epistemological rather than a political argument in favor of open society. He argued that “only democ-

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racy provides an institutional framework that permits reform without violence, and so the use of reason in politics matters.”

But his approach was based on a hidden assumption, namely, that the main purpose of thinking is to gain a better understanding of reality. And that was not necessarily the case. The manipulative function could take precedence over the cognitive function. Indeed, in a democracy, the primary objective of politicians is to get elected and then stay in power.

This rather obvious insight raised some additional questions about the concept of open society. How could Popper take it for granted that free political discourse is aimed at understanding reality? And even more intriguingly, how could I, who gave the manipulative function pride of place in the concept of reflexivity, follow him so blindly?

BOOTH QUESTIONS LED ME to the same conclusion: our view of the world is deeply rooted in an intellectual tradition that either ignores the manipulative function or treats it as subservient to the cognitive function.

It is easy to see how this view of the world became so ingrained. The aim of the cognitive function is to produce knowledge. Knowledge is expressed by statements that correspond to the facts. To establish correspondence, statements and facts have to be separate and distinct. Hence, the pursuit of knowledge requires that

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thoughts should be distinguished from their subject matter. This requirement led philosophers, whose primary preoccupation is with thinking, to the belief that reason and reality are separate. This dualism had its roots in Greek philosophy, and it came to dominate our view of the world during the Enlightenment.

The philosophers of the Enlightenment put their faith in reason. Reason was supposed to work like a searchlight, illuminating a reality that lay there, passively awaiting discovery. The active role that reason can play in shaping reality was largely left out of the account. In other words, the Enlightenment failed to recognize reflexivity. This resulted in a distorted view of reality, but one that was appropriate to the age when it was formulated.

At the time of the Enlightenment humankind had as yet relatively little knowledge of or control over the forces of nature, and scientific method held out infinite promise. It was appropriate to think of reality as something out there, something waiting passively to be discovered, and to think of reason as actively engaged in exploring it. After all, at that time not even the earth had been fully explored. Gathering facts and establishing relationships among them was richly rewarding. Knowledge was being acquired in so many different ways and from so many different directions that the possibilities seemed unlimited. Reason was sweeping away centuries of traditional relationships and religious dogma and generating a triumphant sense of progress.

The difficulties that reflexivity poses to a proper understanding of human affairs went largely unnoticed. The leaders of the

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French Revolution believed that reason could help reconstruct society from the ground up, but their faith in reason was excessive. Society failed to follow the dictates of reason, and the euphoria of 1789 deteriorated into the terror of 1794.

The Enlightenment misinterpreted reality by introducing a dichotomy between thinking and reality that would enable reason to attain perfect knowledge. The dichotomy was not inherent in the subject matter but introduced by the philosophers of the Enlightenment in their attempt to make sense of reality.

The mistake made by the Enlightenment philosophers has been given a name; postmodernists call it the “Enlightenment fallacy.” I shall adopt that term here, but I want to make it clear that I am talking about a fertile fallacy, one that contains a valuable kernel of truth.

Let me explain more precisely what I mean by “fertile fallacy.” We are capable of acquiring knowledge, but we can never have enough knowledge to allow us to base all our decisions on knowledge. It follows that if a piece of knowledge has proved useful, we are liable to overexploit it and extend it to areas where it no longer applies, so that it becomes a fallacy.

That is what happened to the Enlightenment. The dichotomy between reason and reality worked very well for the study of natural phenomena, but it was misleading in the study of human affairs. Fertile fallacies are, in other branches of history, the equivalent of bubbles in financial markets.

The Enlightenment fallacy is deeply rooted in our view of the

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world. It led Popper to proclaim that the same standards and criteria apply in both the natural and social sciences, and it led economic theory to model itself on Newtonian physics. Neither Popper's elegant model of scientific method nor economic theory recognized reflexivity. What is worse, even I, who discovered—or invented—reflexivity in financial markets, failed to recognize that Popper's concept of open society was based on the hidden assumption that the cognitive function takes precedence over the manipulative function—that we are pursuing the truth and not simply trying to manipulate people into believing what we want them to believe.

The Enlightenment fallacy is also at the root of the efficient market hypothesis and its political derivative, market fundamentalism. The fallacy in these two intellectual constructs was exposed in a spectacular fashion by the collapse of the financial system. My discovery of a flaw in open society was less spectacular because the concept is less widely accepted, but on a personal level it was equally earthshaking. It forced me to rethink the concept of open society.

I HAVE NOT ABANDONED my belief in the merits of open society, but I realize that it needs stronger arguments to buttress it. Popper took it for granted that in an open society the cognitive function takes precedence over the manipulative function; I now believe that this has to be introduced as an explicit requirement for

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an open society to flourish. Let me explain how I reached that conclusion.

In a democracy political discourse is aimed not at discovering reality (the cognitive function) but getting elected and staying in power (the manipulative function). Consequently, free political discourse does not necessarily produce more far-sighted policies than an authoritarian regime that suppresses dissent.

To make matters worse, in the political battle to manipulate reality, a commitment to abide by the truth has become a handicap. The Bush administration had at its disposal a powerful right-wing propaganda machine working for it that did not feel any need to respect the facts. This gave it a decided competitive advantage over more old-fashioned political practitioners who were still under the influence of the Enlightenment fallacy and felt constrained by the facts.

Frank Luntz, one of the most successful right-wing propagandists in the United States, openly admitted that he used George Orwell's *1984* as his textbook in devising his slogans. As a believer in the open society, I found this shocking. How could Orwellian Newspeak be as successful in an open society as in a totalitarian state with its Ministry of Truth, which could use Stalinist methods to keep people in line?

This line of enquiry provided me with a clue to the question: what is wrong with America? People are not particularly concerned with the pursuit of truth. They have been conditioned by

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ever more sophisticated techniques of manipulation to the point where they do not mind being deceived; indeed, they seem to positively invite it.

People have become used to receiving information in prepackaged messages; hence the influence of paid political advertising. They are more interested in being entertained than informed; hence the influence of populist commentators like Bill O'Reilly and Rush Limbaugh.

THE TECHNIQUES OF manipulation have developed gradually over time. They originated in the commercial arena toward the end of the nineteenth century when entrepreneurs discovered that they could improve their profit margins by differentiating their products through branding and advertising. This prompted research into the motivation of consumers, the testing of messages, and the use of focus groups, setting in motion a reflexive process that changed the behavior of the public. It led to the development of a consumer society and spread from there to politics and culture.

These trends undermined the hidden assumptions on which economics and politics were based. Economic theory has taken the conditions of demand and supply as given, and it has shown how free markets under the conditions of perfect competition would lead to the optimum allocation of resources. But the shape of the demand curve was *not* independently given; it was subject to manipulation

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by advertising. The theory of representative democracy assumed that candidates would present themselves and their programs, and that the electorate would choose the ones they preferred; it did not anticipate that the candidates would study public opinion and then tell the electorate what it wanted to hear. Both of these theories failed to take into account that reality can be manipulated.

The manipulation of reality also became a major theme in the arts. It was literary criticism that eventually led to the development of the postmodern worldview, which turned the Enlightenment upside down. It denied the existence of an objective reality that could be discovered by reason; instead it saw reality as a collection of often contradictory narratives.

I HAD DISMISSED THE postmodern worldview out of hand because it was in conflict with my profound respect for an objective reality. I did not realize the connection between the postmodern worldview and the Bush administration's propaganda machine until an article by Ron Suskind in *New York Times Magazine* opened my eyes. He quoted one of the operators of that machine as saying "when we act, we create our own reality. And while you're studying that reality—judiciously, as you will—we'll act again, creating other new realities."

This forced me to change my mind. I had to take the postmodern position more seriously and recognize it as a fertile fallacy,

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fully equal in its influence to the Enlightenment, and currently, perhaps, even more influential. But I still regard the postmodern fallacy as more of a fallacy and less fertile than the Enlightenment fallacy. By giving precedence to the manipulative function it ignores the hard core of objective reality that cannot be manipulated. This is more of a defect, in my eyes, than the Enlightenment's neglect of the manipulative function.

ACCORDING TO THE Enlightenment, reason and reality are separate and independent of each other. The only way people can turn reality to their advantage is by understanding the laws that determine the course of events. Under these conditions it could be taken for granted that discovering those laws has to come first. This led to the development of natural science, which is the greatest achievement of the human intellect. It is only in the study of human affairs that the fallacy crept in.

By contrast, the postmodern worldview is *thoroughly* misleading. It has spawned an amoral, pragmatic approach to politics. It can be summed up as follows: Now that we have discovered that reality can be manipulated, why should the cognitive function be given precedence? Why not engage directly in manipulation? Why not pursue power rather than truth?

There is an answer to that argument. While reality can be manipulated, the outcome is bound to diverge from the manipula-

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tor's intentions. The divergence needs to be kept to a minimum, and that can be done only through a better understanding of reality. It is this line of reasoning that led me to introduce a commitment to the pursuit of truth as an explicit requirement for open society.

THIS ABSTRACT ARGUMENT can be reinforced by a concrete example. Look at the Bush presidency. It was remarkably successful in manipulating reality. By declaring war on terror it managed to line up the nation behind the president and pave the way to the invasion of Iraq. The invasion was meant to establish the supremacy of the United States in the world, but it achieved the exact opposite result. America lost power and influence precipitously, and George W. Bush is widely considered the worst president the United States has ever had.

This example ought to be convincing. Yet now that the concept of reflexivity is gaining recognition, the danger is that it will be misinterpreted in favor of the postmodern fallacy. A reflexive reality is just too difficult to understand, and people are easily misled by simple answers. It takes a lifetime to understand the argument that a valid prediction does not necessarily prove that the *theory* on which it was based is also true, but a paid political announcement takes only thirty seconds.

It is tempting to adopt the postmodern view of the world, but

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it is very dangerous to disregard the existence of an objective reality. One way to bring home objective reality is to draw attention to death as a fact of life. The mind finds it difficult to accept the idea of ceasing to exist and all kinds of narratives and myths have sprung up around the idea of life after death. I have been struck by an Aztec ritual in which teams compete in a ball game and the winners are sacrificed to the gods. That is an extreme example of the power of such myths. Yet the fact is that the winning team died.

EVEN SO, I HAVE TO admit that the absence of life after death cannot be proven to those who believe in it. My insistence on the importance of the objective aspect of reality is a matter of personal belief. Indeed, it has a curious resemblance to a religious belief. The objective aspect of reality as I have construed it has many of the attributes of God as conceived in monotheistic religions: it is omnipresent and all-powerful, yet the ways of its working remain somewhat mysterious.

I hold the objective aspect of reality in very high regard, and I used to think that that was the norm. I have come to realize that my attitude is quite unusual and it has to do with my personal history.

The formative experience of my life was the German occupation of Hungary in 1944. Under the wise guidance of my father we not only survived but managed to help others in a situation full of

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dangers. This turned 1944 into a positive experience for me and gave me an appetite for confronting harsh reality.

This attitude was reinforced by my involvement in the financial markets. I was a risk taker, and I often pushed matters to their limits, though I avoided going over the brink. I learned to protect myself against unpleasant surprises by looking out for all the things that could go wrong. I chose investments that had risk-reward ratios that remained attractive even under the worst assumptions. This made me emphasize the dark side of every situation.

Then I became active with my foundations. Here, the fact that I could do something positive to alleviate injustice increased my willingness to recognize and confront harsh realities. A negative assessment became an invitation for positive involvement.

My foundation ended up devoting much of its resources to seemingly insoluble problems like drug policy and seemingly hopeless cases like Burma, Haiti, Liberia, Sierra Leone, and the Congo. Needless to say, fighting losing battles is not the preferred choice of most foundations.

My commitment to the objective aspect of reality plays the same role in my thinking as religion does in other people's. In the absence of perfect knowledge we need beliefs. I happen to believe in harsh reality, while other people believe in God.

Nevertheless I would argue that when society ignores the objective aspect of reality it does so at its own peril. If we try to avoid

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unpleasant realities by deceiving ourselves or the electorate, reality will punish us by failing to meet our expectations.

Yes, reality can be manipulated, but the results of our actions are governed not by our desires but by an external reality whose workings we cannot fully comprehend. The better we understand it, the closer the outcome will correspond to our intentions. Understanding reality is the cognitive function. That is why the cognitive function ought to take precedence over and guide the manipulative function. Ignoring an objective reality that cannot be fully understood leads to the postmodern fallacy.

THE FOREGOING DISCOURSE has shown that mankind has adopted two fallacies about the relationship between thinking and reality in recent history: the Enlightenment fallacy and the postmodern fallacy. They are related to each other. The Enlightenment failed to recognize the prevalence of manipulation in the human sphere, and the discovery of the manipulative function led to the postmodern fallacy. Each of them recognizes one half of a complicated relationship.

My conceptual framework, based on the twin principles of fallibility and reflexivity, combines the two halves. Both fallacies have been influential, but my framework has received little acceptance. This goes to show how easy it is to misinterpret reality—much easier than to gain a proper understanding.

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The postmodern fallacy is now in the ascendant. It guided the policies of the Bush administration and I note with alarm that it has surfaced in the Obama administration as well. I refer to a recent book by George Akerlof and Robert Shiller, which has been influential in shaping the policies of the Obama administration. That book extols the merits of what the authors call the “confidence multiplier.” In other words the authors believe that the ills of the economy can be cured by talking up the financial markets. That belief is half true: the stock market rally has allowed banks to raise capital and it has strengthened the economy in other ways as well. But the confidence multiplier disregards the other half of reflexivity: if reality fails to conform to expectations, confidence can turn into disappointment, boom can turn to bust. I am deeply worried that by deploying the confidence multiplier President Obama has taken ownership of the recession and that if there is a relapse he will be blamed for it.

This discussion should help to clarify my theory of reflexivity by putting it into the context of two false interpretations of reality. In particular, a point that may not have come through loud and clear needs to be emphasized: there is a hard core of objective reality that cannot be manipulated, such as the inevitability of death. It is this hard core that is ignored by the postmodern fallacy.

Emboldened by my recent successes, I will go so far as to claim that my conceptual framework provides the *correct* interpretation of reality. That is a bold claim, and at first sight it seems to be self-contradictory. How can a correct interpretation of

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reality be reconciled with the principle of inherently imperfect understanding? Easy. By pointing out that reflexivity introduces an element of uncertainty both into the participants' thinking and into the course of events. A framework that claims that the future is inherently uncertain cannot be accused of perfection. Yet it can provide important insights into reality; it can even anticipate the future within bounds, although the bounds themselves are uncertain and variable, as we have seen in the recent financial crisis. By recognizing uncertainty, my framework manages to be both self-consistent and consistent with reality. Yet, since it is less than perfect, it holds itself open to improvement.

ACTUALLY, I SEE a tremendous scope for further development. My original framework, formulated under the influence of Karl Popper, dealt only with the problems of understanding reality. But when I added the requirement that the electorate should cherish truthfulness and punish deception, I entered the realm of values. In that realm, uncertainty is even more prevalent than in the realm of cognition; therefore, a lot more thinking needs to be done.

As we have seen, the truth is difficult to establish and often hard to bear. The path of least resistance leads in the opposite direction, avoiding unpleasant realities and rewarding deception as long as it remains convincing. These tendencies need to be resisted for an open society to remain open and to flourish.

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This prescription is particularly relevant to the United States at the present time because that country is facing a particularly unpleasant set of realities in the aftermath of the financial crisis. It has been living beyond its means for the last quarter of a century and making ends meet by borrowing abroad. Now the housing bubble has burst, and consumers are overextended and need to rebuild their savings. The banking system has collapsed and needs to earn its way out of a hole.

The Bush administration had deliberately misled the electorate when it invaded Iraq on false pretenses. The Obama administration cannot be accused of deliberate deception; nevertheless, it has accepted that the country is unwilling to face harsh realities and deployed the confidence multiplier.

Unfortunately, objective reality is unlikely to fulfill the hopes raised by the confidence multiplier. At the same time, the political opposition is not constrained by facts in attacking the president. In these circumstances, the requirement that the electorate should be more committed to the pursuit of truth will be difficult to meet. It provides a good agenda for my foundation, but the current state of democracy in America does not strengthen the case for open society as a superior form of social organization. I need to find a stronger argument.

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A BETTER CASE CAN BE found by reverting to the Founding Fathers, who formed their views long before the concept of open society was introduced. The Founding Fathers built their case on the value of individual freedom. The epistemological argument they employed was flawed: the Declaration of Independence states that “We hold these truths to be self-evident,” but there is nothing self-evident about them. Self-evident or not, however, the value of individual freedom is enduring and, having been exposed to totalitarian regimes, I’m passionately devoted to it. And I am not alone.

Reverting to the Founding Fathers has another great advantage: it allows a discussion of power relations. The Constitution protected against tyranny by a division of powers. The division of powers recognizes that there are competing interests and different interpretations of reality within society that need to be reconciled by a political process. The constitutional checks and balances preclude the formation of absolute power that could claim to be in possession of the ultimate truth. The Constitution establishes a mechanism whereby different branches of government interact and control each other. But that is not sufficient.

Open society can prevail only when people can speak truth to power. It needs the rule of law that guarantees freedom of speech and press, freedom of association and assembly, and other rights and freedoms. They empower citizens to defend themselves against the abuse of power and to make use of the judicial branch for such defense. That is how the Founding Fathers created an open society.

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Let me spell out my conclusion more clearly. Open society is a desirable form of social organization both as a means to an end and as an end in itself. It enables a society to understand the problems confronting it and to deal with them more successfully than other forms of social organizations, *provided* it gives precedence to the cognitive function over the manipulative function and the people are willing to confront harsh realities.

In other words, the *instrumental* value of democracy is conditional on the electorate's commitment to the pursuit of truth, and in that regard the current performance of American democracy does not live up to its past achievements. We cannot rely on the inherent superiority of the American system and need to prove ourselves anew. But quite apart from its instrumental value, open society also has an intrinsic value, namely, the freedom of the individual, which applies whether open society flourishes or not. For instance, it applied in the Soviet Union.

Of course, the freedom of the individual must be made compatible with the public interest and the freedom of other individuals.

Moreover, the intrinsic value of individual freedom falls short of being self-evident. For instance, it is not generally recognized in China, where the interests of the collective take precedence over the interests of the individual. This was the clear message of the opening ceremony of the 2008 Olympic Games. The ceremony showed that by doing exactly what they are told at exactly

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the right time, a large collection of individuals can produce a superb spectacle.

With the changing power relations between the United States and China, the value of individual freedom is likely to assume increasing importance in the immediate future. I will address that subject in my last lecture.

Thank you.