
Commentary: Reconstructing Keynes' position in the economic calculation debate: a reply to Lopes and Almeida (2019)

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Abstract: In this reply to Lopes and Almeida (2019), I argue that in trying to discover Keynes' position in the economic calculation debate, the authors made him much more sympathetic towards the socialist side that he actually was. From a technical point of view, Keynes wanted the state to control the size of total output, but not its composition. This does not imply that the calculation problem is transferred from the individual to the state, as the authors seem to consider. Moreover, the highly abstract, equilibrium-dependent nature of the reply formulated by the socialists to Mises' original problem would probably not have impressed Keynes, given his position on using mathematics and equilibrium theory in economics. There are insufficient arguments presented in the Lopes and Almeida article to justify that Keynes was even mildly sympathetic towards the socialist side from a technical point of view.

Keywords: economic calculation debate; J.M. Keynes; L. von Mises; equilibrium theory; economic planning; *The General Theory*; output composition; aggregate monetary demand.

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1 Introduction

In an article published in the *IJPEE*, Lopes and Almeida (L&A, 2019) brought the socialist calculation debate of the 1920s and 1930s back to life, but with an interesting twist: in spite of its importance for the economics profession, J.M. Keynes made no claim regarding it. This is somewhat intriguing since Keynes was one the most renown (if not

the most renown) figure in the field of economics at the time. This led the authors to raise the following fascinating, although unhistorical, question: *If Keynes would have participated in the debate, what would his position have been?*

The importance of the calculation debate cannot be underestimated, given that today it is taught to economics students around the world, despite that both (antagonistic!) schools of thought (Austrians and socialists) have proclaimed themselves as victors.¹ It is indeed likely that a pluralist approach is needed in order to promote communication between schools of thought, otherwise economics as a science risks turning into a set of airtight silos which have little in common with each other.

The work by L&A (2019) is qualitative in nature. They offer a three-fold answer, with two arguments political and one economical/technical. The first two boil down to the fact that Keynes did not join the debate given that:

- 1 the debate was abstract and it would have distracted his attention from contemporary policymaking
- 2 the debate required the combatants to take a firm position either for or against socialism and Keynes was not adept of firm positions.

These statements are, I believe, perfectly sound.

However, regarding the third argument, i.e., the technical one, the authors maintain that Keynes would have taken a sort of middle ground between the Austrians and the socialists. They state that:

“In a sense, he would be on both sides: on the Austrian side because of his political position against communism and by recognising the importance of entrepreneurship and on the socialist’s side because of firm belief in the benefits of economic planning.” [L&A, (2019), p.235]

In this case, I fear that the authors have erred in pushing Keynes’ position on planning much closer to the socialist camp than it actually was. The source of this seems to be a misinterpretation of Keynes’ technical economics. Moreover, there are two additional reasons which can be mentioned here that would position Keynes against central planning in the socialist calculation debate; although not mentioned by the authors they are essential:

- 1 Keynes wanted the state to control only total output, but not its composition
- 2 Keynes’ contempt regarding economic equilibrium and mathematics.

The first is a technical/economic argument and the second is methodological.

At this point of the discussion, I need to emphasise that the main question is not whether or not Keynes considered state intervention in the economy necessary², as L&A (2019, pp.232–234) seem to suggest, but whether or not Keynes would consider state ownership over *all* the means of production a preferable option.

2 Keynes wanted the state to control total output, but not its composition

The problem raised by Mises (1935) in the socialist calculation debate was that if prices were removed in a socialist system, the government would then have no way to rationally allocate resources. The planning board would not be able to know what goods to produce,

what combination of factors to use, when and what technical innovations to implement or where to locate production facilities [Mises, (1949), pp.698–715]. Mises (1935) believed that the problem was essentially not with the production of consumption goods, where consumer feedback could be gained, but with *capital goods*. This problem was repeatedly stressed by Austrians.³ The extreme heterogeneity coupled with the fact that in a socialist system the producer market would be characterised by a bilateral monopoly (one buyer, one seller) with no information flow between participants meant for Mises that the economic system would cease to function. There would be a breakdown in the structure of production, and society would progressively consume its capital stock until general poverty would occur.

This is of course nothing new, given that Mises' view is relatively well represented in the economic literature. However, the main point that I would like to stress is that Mises' objection referred not only to the size of the output in a socialist state, but also to its *composition*.⁴ I would go as far as claiming that for Mises, the monetary value of the total production carries little significance, if any.

If we now take a look at Keynes' technical economics, we will easily reach the conclusion that he was not the most consistent economist. This is of course not news, given that he was known to change his opinion with lightning speed.⁵ However, *The General Theory* (1936) was undoubtedly his most influential book in technical economics⁶, so when trying to find Keynes' view on an issue, that would probably be the best place to start. By the time he wrote his *magnum opus*, Keynes' (1936) problem with the working of the capitalist system was not the composition of output, but that in a monetary economy aggregate demand could lag behind aggregate supply. In this case, instead of allowing a general decrease in prices, businesspeople would keep prices relatively rigid and adjust the quantity produced. This would lead to fewer factors employed, especially labour. Keynes' solution to this problem was that the state should use the means at its disposal (especially fiscal ones) to boost aggregate demand in order to prevent unemployment.

In L&A (2019), rather strange is Section 4, *the elimination of calculation in Keynes and the 'information problem'*. If my reading is correct, the authors seem to claim that by following Keynes' prescriptions, the calculation problem would be transferred from the individual to the state: "In this sense, we can notice that the calculation problem in Keynes does not belong to the individual, but to the state" [L&A, (2019), p.233]. The same idea appears a few paragraphs later: "And it is from this point that one can build a concept of socialization of investments in Keynes: a coordinated capitalism, in which the calculation problem would necessarily disappear for the individual producer." But this is of course false. Firstly, the calculation problem does not disappear in the Keynesian scenario, and second, it is really doubtful that this is what Keynes actually had in mind.

As explained above, Mises's calculation problem was mainly a problem of the composition of output. The problem continues to exist even in the Keynesian scenario. Even if the state would stimulate investment in economic downturns (say by fiscal or monetary policy), as Keynes argued, would investors not still have to decide what to produce, with what combinations of factors or what techniques to use? Keynes did not want the state to decide what to produce. He knew that businesspeople would be more capable.⁷ He just wanted to ensure that in periods of economic turmoil, the state would boost aggregate demand so it does not lag behind supply, thus eliminating unemployment (in his understanding).

This is also probably the reason for which Keynes (1936, pp.378–379) explicitly mentions in *The General Theory* that he was not arguing for state control of the means of production:

“I conceive, therefore, that a somewhat comprehensive socialisation of investment will prove the only means of securing an approximation to full employment [...] *But beyond this no obvious case is made out for a system of state socialism which would embrace most of the economic life of the community. It is not the ownership of the instruments of production which it is important for the state to assume.* If the state is able to determine the aggregate amount of resources devoted to augmenting the instruments and the basic rate of reward to those who own them, it will have accomplished all that is necessary [...]. But if our central controls succeed in establishing an aggregate volume of output corresponding to full employment as nearly as is practicable, the classical theory comes into its own again from this point onwards. If we suppose the volume of output to be given, i.e. to be determined by forces outside the classical scheme of thought, *then there is no objection to be raised against the classical analysis of the manner in which private self-interest will determine what in particular is produced, in what proportions the factors of production will be combined to produce it, and how the value of the final product will be distributed between them.* [...] Thus, apart from the necessity of central controls to bring about an adjustment between the propensity to consume and the inducement to invest, *there is no more reason to socialise economic life than there was before.* To put the point concretely, *I see no reason to suppose that the existing system seriously misemploys the factors of production which are in use.* There are, of course, errors of foresight; but these would not be avoided by centralising decisions. When 9,000,000 men are employed out of 10,000,000 willing and able to work, there is no evidence that the labour of these 9,000,000 men is misdirected. The complaint against the present system is not that these 9,000,000 men ought to be employed on different tasks, but that tasks should be available for the remaining 1,000,000 men. *It is in determining the volume, not the direction, of actual employment that the existing system has broken down.*”

The reader will have to excuse the long quote, but it is extremely relevant to my research question. Keynes clearly points out that “no obvious case is made out for a system of state socialism” and that “there is no objection to be raised against the classical analysis of the manner in which private self-interest will determine what in particular is produced, in what proportions the factors of production will be combined to produce it, and how the value of the final product will be distributed between them.”

There is nothing here suggesting that if Keynes would have been required to participate in the economic calculation debate, he would have been even mildly sympathetic towards the socialist side from a technical point of view. If this was not so, why did he explicitly state numerous times in *The General Theory* that he was not arguing for the socialisation of the means of production? Keynes considered that “authoritarian state systems of to-day seem to solve the problem of unemployment at the expense of efficiency and of freedom” [Keynes, (1936), p.381]. I am rather intrigued that L&A (2019, pp.231–232) do not mention these paragraphs at all, especially in their section *brief exposition of Keynes’s view on planning*. They use instead quotes from rather obscure sources like radio broadcasts⁸ and letters, even though *The General Theory* was Keynes’ most renown technical economics book.

3 Keynes' contempt for economic equilibrium and pseudo mathematics

I have grouped these two arguments under the same umbrella because they are interrelated (but not necessarily identical):

- 1 Keynes' contempt for economic equilibrium and the way it was used in classical economics
- 2 his position on the use of mathematics within economics.

Let us first concentrate on the former.

A fundamental difference in Keynes's thinking between the *Treatise* (1930) and *The General Theory* (1936) was that he adopted the idea that the economy can adjust to a decrease in aggregate demand through an adjustment in output and employment (not prices!) (Leijonhufvud, 1976). This basically means that the market either completely lacks any automatic adjustment mechanism or that these forces are extremely sluggish. Thus, for Keynes, the market either never reaches equilibrium, or if it does, it is by pure chance and represents an extremely unlikely event.⁹ This is essentially why he stressed that his theory is the general one and the theory exposed by the 'classics' only a particular case.¹⁰

For the second argument, on the one hand, we have the 'classical' approach represented by Skidelsky (1983), Stone (1978) and Carabelli (1985), who claimed that Keynes was rather antithetic to using mathematics, statistics or econometrics and that he attacked such practices. On the other hand, others contest this somewhat conventional view arguing that Keynes's attitude is highly ambivalent and/or that his objections do not refer to employing mathematics *per se*, but to the misapplication/illegitimate use of mathematics (e.g., Patinkin, 1982; Brady, 1988; O'Donnell, 1990).

Let us choose the weakest position between the two, i.e., that Keynes was not opposed to the application of mathematics *per se* but to the misapplication of mathematics or to "the elevation of mathematics to the highest form of economics reasoning" [O'Donnell, (1990), p.29]. Going back to the economic calculation debate, the way in which the socialists allegedly¹¹ won the debate was by showing that socialism is compatible with general equilibrium theory. They argued that in equilibrium, the Pareto-Barone equations could be used to determine optimum quantities in absence of market prices (Rothbard, 1991). It is generally considered that Oskar Lange delivered in 1936 the final socialist answer to Mises (L&A, 2019).

Now, let us for the moment disregard the question concerning which camp was essentially right regarding the calculation debate and focus on another which in this context is more important: *what would have Keynes thought about Lange's solution?* Assuming consistency in the case of Keynes (and I freely admit this is a bold assumption) the only thing Keynes could have felt regarding Lange's argument was contempt. Firstly, it is based on equilibrium economics and, if there is one area where Keynes was consistent was that the classical equilibrium¹² is only a very specific case which can basically never be found in real life situations. Moreover, Lange's equations would have probably fallen under Keynes' pseudo mathematics category, given that they are based on premises which do not describe the real world. For a pragmatist like Keynes, these would be ample reasons to reject the socialist counterargument altogether. It is even possible that this was the main reason for which Keynes did not officially join the debate, which was strange for someone of Keynes' calibre.

4 Conclusions

In spite of writing an extremely interesting article¹³, I fear that Lopez and Almeida (2019) erred in presenting Keynes as much more sympathetic towards socialist planning than he actually was. Keynes' technical economics, which suggests that the state should support aggregate monetary demand in order for it to equalise supply, does not imply that the responsibility of economic planning is transferred from the individual to the state. Even in a Keynesian scenario, the individual producer would have to decide what to produce, what factor proportions to use, where to localise production and what innovations to implement. Mises's argument still has teeth even in a Keynesian framework. Moreover, it is highly doubtful that Keynes would have had a high opinion regarding the way Lange answered Mises' problem. Being too equilibrium dependent and highly abstract, the answer would not have impressed Keynes and would have probably fallen under his pseudo mathematics category.

Despite the excellent quality of the original article, the technical arguments presented by the authors are insufficient to argue that Keynes would have been even mildly sympathetic towards the socialist side from a technical point of view.

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Notes

- 1 This was once again shown recently when Lopes, one of the authors of the initial piece, published another article on the calculation debate. See the recent theoretical exchange in the *Cambridge Journal of Economics* between Lopes (2021, 2022) and Bylund et al. (2022).
- 2 If this would be the case, the problem becomes trivial. Of course, Keynes was pro-government intervention. However, using the same logic we may also argue that many members of the Austrian school tolerate, if not recommend, a certain degree of state interventionism. Probably, the most renown case here was Hayek, who actually favoured state welfare measures in a large number of areas (see for instance, Shearmur, (1997). There was even a rather well-known (admittedly mean) joke among Austrians circles that Hayek's 'libertarianism' in practice amounted for something close to Sweden's welfare state.
- 3 See for instance Rothbard (1991, pp.56–57): "The real problem, as Mises has insisted from the beginning, is in *all the intermediate markets for land and capital goods*. [...] And here is precisely where calculational chaos necessarily reigns, and there is no way for rationality to intrude on the immense number of decisions on the allocation of prices and factors of production in the structure of capital goods."
- 4 It would be safe to say that the socialist calculation debate is in essence a debate regarding the composition of output in a socialist state and not regarding the size of the aggregate (monetary) demand.
- 5 One of Keynes' more memorable quotes, "When my information changes, I alter my conclusions. What do you do, sir?" [Samuelson, (1983), p.19].
- 6 Here I say most influential, but not necessarily his best/most consistent. I argue, along with Leijonhufvud (1976), that the *Treatise* is Keynes' (1930) more fundamental work from a theoretical point of view.
- 7 To their credit, L&A (2019) note that Keynes would dislike socialism since it decreases efficiency and freedom. They also correctly pointed out [L&A, (2019), p.233] that Keynes' view on uncertainty and entrepreneurship brought him close to Hayek's position in the debate (in certain respects).
- 8 There is also a reference to 'Can Lloyd George do it?' in L&A (2019, p.231), but I fail to see how it is relevant since Keynes did not express his view on planning there; only that the general opinion at that time was in favour of planning.
- 9 My article (Patruti, 2018) explained that the main obstacle in the Keynes-Hayek debate was that Hayek, for the larger part of his life, believed that markets actually *do* tend to equilibrium or to a state which approximates it. By the time he wrote *The General Theory*, Keynes did not. Both economists claimed that these were not essentially ideologies, but empirical observations.
- 10 See Keynes (1936, p.3), "I shall argue that the postulates of the classical theory are applicable to a special case only and not to the general case..."
- 11 I say allegedly because there are still Austrians who believe that "Lange's famous response to Mises' challenge constitutes a rebuttal of a straw man" [Bylund et al., (2022), p.609].

- 12 I used the word classical equilibrium to distinguish it from Keynes' 'equilibrium' with unused resources.
- 13 I wish to take advantage of the opportunity here to mention that I am indebted to the authors for raising the question and doing the subsequent research on the issue.