

# “THE FORGOTTEN CONTRIBUTION: MURRAY ROTHBARD ON SOCIALISM IN THEORY AND IN PRACTICE” AND THE REINTERPRETATION OF THE SOCIALIST CALCULATION DEBATE: A COMMENT

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Peter J. Boettke and Christopher J. Coyne merit strong congratulations for their illuminating *Quarterly Journal of Austrian Economics* article “The Forgotten Contribution: Murray Rothbard on Socialism in Theory and in Practice” (2004). The article is a much needed and long overdue acknowledgement and appreciation of Rothbard’s contributions to the theory, including the calculation debate, and practice of socialism. Rothbard ranks as one of the foremost Austrian School economists of the twentieth century, and his contributions to these, as well as other topics, clearly deserve to be better recognized and understood. Boettke and Coyne have performed an important service in presenting and analyzing Rothbard’s contributions in these areas.<sup>1</sup>

My remarks regarding the Boettke and Coyne article are directed toward a relatively narrow topic, specifically, the reinterpretation of the socialist calculation debate by Rothbard and others. Boettke and Coyne perceptively and correctly note that Rothbard’s analysis and reinterpretation of the socialist calculation debate in *Man, Economy, and State* in 1962 anticipated developments concerning this issue by two decades:

However, it is important to report Rothbard’s interpretation of the socialist calculation debate because it anticipated the reinterpretation of that debate that gained currency in the writings of Karen Vaughn, Peter Murrell, and Don Lavoie in the 1980’s, concluding that the Austrians had

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<sup>1</sup>In addition to their acknowledgement and analysis of Rothbard’s contributions to the theory and practice of socialism, Boettke and Coyne are right on the mark in their evaluation of Ludwig von Mises’s thesis demonstrating the impossibility of calculation in a socialist economy when they state: “This insight of Ludwig von Mises is, in our opinion, the most significant contribution to political economy made in the twentieth century” (p. 74).

indeed won the calculation debate. We will quote Rothbard at length so the reader can see how his presentation in 1962 already implied the failure of equilibrium economics to adequately address the issues in the socialist calculation debate that was stressed in these later contributions by Vaughn, Murrell, and Lavoie. (Boettke and Coyne 2004, pp. 75-76)

The point I would like to convey is the following: While in no way attempting to lessen or marginalize the significance of their work, the “reinterpretation” of the socialist calculation debate by Rothbard, Vaughn, Murrell, and Lavoie would not have been necessary if the economics profession had fully acknowledged and comprehended Ludwig von Mises’s path-breaking thesis. Mises’s seminal article “Economic Calculation in the Socialist Commonwealth” contains textual evidence that he anticipated and refuted the arguments of the mathematical, general equilibrium socialists (Mises 1990, pp. 25-26) and, thus, effectively won the “debate” in 1920 with the initial publication of the article. Mises again addressed and refuted the mathematical, general equilibrium socialists, admittedly in an expanded manner, in 1938 with the publication of a French language paper. Mises wrote an English language version of this paper that was first published in the *Quarterly Journal of Austrian Economics* under the title “The Equations of Mathematical Economics and the Problem of Economic Calculation in a Socialist State” in 2000. His most comprehensive treatment of the topic occurred in 1949 with the publication of the first edition of *Human Action* (Mises 1966, pp. 710-15).<sup>2</sup> Importantly, Mises did not modify his initial thesis during the course of the debate, or his lifetime. If Mises did not strictly win the debate in 1920, and again there is textual evidence that he did, then he certainly emerged victorious in 1949, if not in 1938. In support of this conclusion, this Comment presents and documents Mises’s analysis and refutation of the mathematical, general equilibrium socialists. Joseph T. Salerno, in his “Postscript” to Mises’s 1920 article (Salerno 1990), has provided an outstanding summary, analysis, and elaboration of Mises’s calculation argument, and this Comment draws notably from Salerno’s discussion. Salerno concludes: “Mises’s original thesis stands on its own against all counterarguments and without any need for qualification or emendation” (Salerno 1990, p. 66).

The socialist calculation debate occurred because the large majority of economists (mainstream and otherwise) were unable and/or unwilling to fully grasp the nature, scope, and implications of Mises’s thesis. Rothbard’s significant contribution to the debate was to resurrect and restate Mises’s analysis, and for this important achievement Rothbard, of course, deserves

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<sup>2</sup>In *Human Action*, Mises also systematically addressed and refuted other, non-general equilibrium based criticisms of his demonstration that calculation is not possible in a socialist economy (Mises 1966, pp. 698-710). These responses by Mises are not discussed here since the socialist calculation debate centered on the assertion that a socialist planner could utilize the equations of general equilibrium analysis to calculate.

high commendation.<sup>3</sup> Rothbard, in a footnote to the passage in *Man, Economy, and State* (1970, pp. 549–50) in which he, elaborating on the argument presented in Mises’s 1920 article, disproves the assertions of the mathematical general equilibrium socialists, states: “Far from being refuted, Mises had already disposed of this argument [that of the mathematical general equilibrium socialists] in his original article (Mises 1990, pp. 25–26). Further, Barone’s article was written in 1908, 12 years before Mises’s. A careful perusal of Mises’s original article, in fact, reveals that he there disposed of almost all the alleged ‘solutions’ which decades later were brought forth as ‘new’ attempts to refute his argument” (Rothbard 1970, p. 901).

The standard interpretation of the socialist calculation debate is that certain economists had shown that the socialist planner could utilize the equations of general equilibrium analysis to calculate. Thus, Mises’s thesis that economic calculation is impossible under socialism had been proven, at least in theory, incorrect. However, in his 1920 article, Mises anticipated and refuted the assertion that the central planner could utilize the equations of general equilibrium analysis to solve the socialist calculation problem. In this article (as well as in his later writings on the subject), Mises noted that the static state of general equilibrium does not and cannot exist in the real world as the economic data are continually changing. General equilibrium is only a hypothetical mental construct of economists. Mises further noted that because of the static nature of general equilibrium, economic calculation is not required; in effect, the need for economic calculation has been assumed out of existence.<sup>4</sup>

Mises also noted in his 1920 article that the establishment of a socialist state would, by definition, require the reallocation of the ownership of the factors of production from the previous private owners to the state. This reallocation would undoubtedly significantly alter the economic data, including incomes and preferences, so that any reference by the planner of the newly established socialist state to the economic data that existed in the final state of the previous market economy would be worthless. This aspect of Mises’s argument is particularly relevant to the claim that proximal equilibrium theory provides a basis that could enable the socialist planner to calculate. According to this variant of equilibrium analysis, the economy, while not in general equilibrium, is virtually always close enough to general equilibrium so that the prices of the immediate past reflect all the information needed for

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<sup>3</sup>Mises’s thesis demonstrating the impossibility of economic calculation and, hence, rational resource allocation in a socialist economy can be found in Mises (1990, pp. 1–50; and 1966, pp. 695–715).

<sup>4</sup>Assuming the calculation problem out of existence in a theoretical construct, does not, however, relieve the socialist planner of having to address and solve the problem in the real world. The socialist planner must still calculate if he is to achieve any rationality in the allocation of the factors of production. As Boettke and Coyne state, solving the problem by assumption “in fact is no solution at all” (2004, pp. 76–77).

future-oriented decisions. But as Mises's analysis demonstrates, the significant change in the economic data that necessarily must occur when the market economy moves from its final state to socialism, renders useless any attempt by the socialist planner to calculate through the application of proximal equilibrium theory. Mises presented these arguments in his 1920 article.

The static state can dispense with economic calculation. For here the same events in economic life are ever recurring; and if we assume that the first disposition of the static socialist economy follows on the basis of the final state of the competitive economy, we might at all events conceive of a socialist production system which is rationally controlled from an economic point of view. But this is only conceptually possible. For the moment, we leave aside the fact that a static state is impossible in real life, as our economic data are forever changing, so that the static nature of economic activity is only a theoretical assumption corresponding to no real state of affairs, however necessary it may be for our thinking and for the perfection of our knowledge of economics. Even so we must assume that the transition to socialism must, as a consequence of the levelling out of the differences in income and the resultant readjustments in consumption, and therefore production, change all economic data in such a way that a connecting link with the final state of affairs in the previously existing competitive economy becomes impossible. But then we have the spectacle of a socialist economic order floundering in the ocean of possible and conceivable economic combinations without the compass of economic calculation. (Mises 1990, pp. 25-26)<sup>5</sup>

Subsequently, in his 1938 article and in *Human Action* in 1949, Mises again responded to and refuted the mathematical general equilibrium socialists. Mises noted that in order to utilize the equations of general equilibrium analysis to calculate, the socialist planner would need to know these equations' required preference scales as they would exist under general equilibrium. But since general equilibrium is a hypothetical state only, that does not and cannot exist in reality, these preference scales cannot be ascertained by the socialist planner. Mises stated in his 1938 article:

The socialist director-general, however, needs, if he is to solve the equations, the knowledge of a hypothetical situation which is different from the reality with which he is acquainted and is a construction of our thinking which we know, without any doubt, will never become reality. It is no help to him in setting up his equations to know the conditions that are given today and the opinions that prevail today about the shape of things in the future. He would need to know how things would look if a hypothetical state were reached in which all data had become rigid, and no further change would be set in motion, because no change could afford any further increase in welfare. (Mises 2000, pp. 31-32)

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<sup>5</sup>In order to present Mises's analysis as accurately as possible, this paper incorporates extensive quotations from his writings.

Those who think that it would be possible to apply the equations of mathematical economics for making the calculations fail to see that included among the items of which these equations are composed are unknown preference scales belonging to a situation which is unreal and can never be realized in practice. The circumstance that they are unknown frustrates all attempts to use the equations for purposes of economic calculation. (Mises 2000, p. 32)

Mises also presented this argument in *Human Action*:

But for a utilization of the equations describing the state of equilibrium, a knowledge of the gradation of the values of consumers' goods in this state of equilibrium is required. This gradation is one of the elements of these equations assumed as known. Yet the director knows only his present valuations, not also his valuations under the hypothetical state of equilibrium. He believes that, with regard to his present valuations, the allocation of the factors of production is unsatisfactory and wants to change it. But he knows nothing about how he himself will value on the day the equilibrium will be reached. These valuations will reflect the conditions resulting from the successive changes in production he himself inaugurates. (Mises 1966, p. 711)

In addition, in order to utilize the equations of general equilibrium analysis to calculate, Mises noted that the socialist planner first would need to move the economy from its existing nonequilibrium state to the state of general equilibrium, but this would be impossible because the socialist planner lacks any means of economic calculation to rationally guide his actions. The equations of static equilibrium analysis, since they only describe the final equilibrium position, can provide no guidance to the socialist planner regarding the path the economy must follow in order to reach the final stage of equilibrium. As Mises stated in his 1938 article:

It is necessary to find out which of all the conceivable changes can, in the given conditions, secure the fullest satisfaction of wants from the standpoint of the preferences of the consumers or of the dictator. For this purpose the equations which describe the final equilibrium position are quite inappropriate. They say absolutely nothing about the path which the economic system has to follow in order finally to reach the equilibrium. (Mises 2000, p. 30)

Mises also addressed this issue in *Human Action*:

This hypothetical future state of equilibrium will appear when all methods of production have been adjusted to the valuations of the actors and to the state of technological knowledge. Then one will work in the most appropriate locations with the most adequate technological methods. Today's economy is different. It operates with other means which do not correspond to the equilibrium state and cannot be taken into account in a system of equations describing this state in mathematical symbols. The knowledge of conditions which will prevail under equilibrium is useless for the director whose task it is to act today under present conditions.

What he must learn is how to proceed in the most economical way with the means available today which are the inheritance of an age with different valuations, a different technological knowledge, and different information about problems of location. He must know which step is the next he must make. In this dilemma the equations provide no help. (Mises 1966, p. 713)

Mises concluded his discussion in *Human Action* regarding the assertion that the socialist planner could utilize the equations of general equilibrium analysis to calculate with the following:

It was a serious mistake to believe that the state of equilibrium could be computed, by means of mathematical operations, on the basis of the knowledge of conditions in a nonequilibrium state. It was no less erroneous to believe that such a knowledge of the conditions under a hypothetical state of equilibrium could be of any use for acting man in his search for the best possible solution of the problems with which he is faced in his daily choices and activities. (Mises 1966, pp. 714-15)

I hope the above discussion has helped to clarify a crucial and apparently largely neglected aspect of the socialist calculation debate and its reinterpretation.

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