

# Why didn't Keynes participate at the socialist economic calculation debate?

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## Abstract

The socialist economic calculation debate is an important one for everyone concerned with the transition from the capitalist to the socialist economic accounting. It represents the struggle of socialist economists against Mises's claim that socialism is theoretically impossible and Hayek's adjustment that it is practically unfeasible. Although being a very clear polarized clash, Keynes was antagonistic to both sides of that debate and did not take part explicitly in the controversy. Why? The paper answers this question by arguing that this would have forced him to broadly reveal his political position as the most powerful defender of capitalism through his proposals of *capitalist* economic planning.

**Key-words:** socialist economic calculation, Keynes, Hayek, Lange

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## 1 Introduction

The socialist calculation debate is a topic that, while creating radically contrary positions, has serious difficulties in creating roots in the permanent memory of the economist. In spite of being a highly abstract discussion that attracts authors linked to the Austrian and the market socialist perspectives, it has concrete connections to the political debates from the end of classical liberalism.

One of the greatest transformations in the beginning of the 20<sup>th</sup> century was the Russian Revolution, which created a debate on the economic feasibility of a socialist economy. Ludwig von Mises, in the article *Economic Calculation in the Socialist Commonwealth* (1920) argued that a socialist economy, with administered prices, was impossible. According to him, since private property would not exist in the socialist economy, the system of the exchanges would not exist either. In other words, the price system would not work simply because trade presupposes private property. How is it possible to make evaluations and calculations in these conditions?

Instead of ignoring him, socialist economists accepted his challenge. They could not afford to ignore him because Mises correctly pointed to an important practical

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problem.<sup>3</sup> The reconstruction of the debate is not only an exercise of history of economic thought or pure economic theory. Its concrete applications show that a more adequate understanding of this point will be fundamental to the construction of a conscious society that utilizes thoughtfully the natural resources and that projects a specific social livelihood wished by its population.

The logic of the capitalist system after 1918 and, chiefly, after 1929 was one in which the unbounded price mechanism, as idealized by the liberals, did not exist. Whether by the war effort through State intervention, whether for the mechanism of sectorial protection by the developmentalist State, the allocation of resources was not free during a good part of the 20<sup>th</sup> century. And, after the Second World War, the Keynesian system of intervention prevailed in the national economies.

However, after the 1970s and, with greater intensity, after the fall of the Berlin Wall and the end of the Soviet economy in 1989, the capitalist economies advanced in the direction of diminishing the political structure that operated on the price system. Would Hayek's ideas be returning with all its power and substituting Keynes's ideas, which reigned absolute in the Golden Age of capitalism? Or the late 2000s crisis assured, in Skidelsky (2009) terms, the return of the Master?

This takes us to Keynes. The exact description of his economic and political thought is a harsh task. Many commentators sought to synthesize the Keynesian doctrine, but this process turns into the vulgarization of ideas inside Keynesianism. Keynes believed that the pure liberalism was an unreasonable utopia, since such a system never existed in reality, even during the gold standard age under the leadership of London. For this, the solution would have to be a specific capitalism, where the dynamics of individual decision over the utilization of money would fit in an environment ordered by the government so that rational investments occur in a continuous and crescent rate.

The political and economic dispute between Keynes and Hayek is called by Wapshott (2011) as "the clash that defined modern economics." It concentrates on the direct opposition between State intervention (or State control over investments, adequate policies for the effectuation of the demand, *et cetera*) and liberalization. However, the spreading of their ideas distorted their original thought, further increasing the distance between them.

So Keynes struggles against two opposite sides: *laissez-faire* liberalism and socialism. To unveil this point and go beyond the political and ideological battles, we consider to be necessary to understand how Keynes refuted, in the theoretical plan, both the proposals of Austrian and socialist economists. In other words, we cannot only show, as Plumptre (1947) did, that one of the most important lessons taken from Keynes was that "the end of liberalism was not necessarily the beginning of the communism" or even

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<sup>3</sup> Lange (1962) shows how different econometric models were used in both socialist and capitalist systems. Those planning techniques helped to construct the modern economic orthodoxy (cf. Bockman, 2011).

the beginning of the authoritarian economics of fascism and Nazism. It is also necessary to expose the fundamentals of the theoretical basis of this political position. Our argument is that this can only be done if Keynes's position in the socialist economic calculation debate is brought to investigation.

Unfortunately Keynes did not participate at this debate. Why?

## **2. The debate on the socialist economic calculation**

From the general history of economic thought, it is possible to say that the debate is older than it is generally thought to be. Plato, in his utopia, believed that all economic and non-economic activity should be strictly regulated, and that probably implied in administered prices by a central authority, in a society that many commentators would identify as 'communist'. Aristotle, in his criticism to Plato, was one of the first to establish a relation between value and price and that the existence of a 'non-communist' society required the existence of exchange. Here, the bargain would be the method to realize them and, eventually, money as a means of exchange and measurement of value would emerge as almost spontaneously, as any Monetary Economics textbook would explain (cf. Schumpeter, 1954, p. 53-66).

In theoretical terms, the debate was important to both Austrians and socialists. How can a debate be so important to such distinguished philosophical positions?

Roberts (1971), starting from the notion of 'alienation' in Marx, explained that the estrangement of the direct producer in relation to the product is a necessary reality that derives from a developed market economy. The production process of consumption goods has a consequence in which the worker distances himself from the result of his work, turning the mercantile society act into an unconscious way to satisfy their necessities. From this perspective, the socialist society requires an organization form distinguished from the market, where the economy is subordinated to established rules that indicate the direction of the use values along the process of material reproduction of the community. In this sense, Marx's socialist economy is necessarily a planned economy, not spontaneous or decentralized market economy. Thus the adoption of system of economic planning would be the best alternative to eliminate the basic problem of the mercantile society.

The decentralized system of exchanges would be replaced by a society that would behave like a great factory. At the same time, other problems would be solved, like the controls of the means of production. But, before reaching this stage, the economic organization would take advantage of the virtues of the market recognized by the socialists, like, for example, the capacity to expand the production and to create a high material wealth and thus individual welfare. As consequence of this progress, the socialist distributive concept of 'to everyone according to his necessity' would become reality, initially with the State proving each individual, each factory, etc. the exact quantity of products and raw materials needed. The problem of alienation and exploitation of labor

would be eliminated, culminating in the end of the proletarian State itself. In the end, the communist objective of a society without classes would be accomplished.

The debate on the socialist economic calculation is especially important to the supporters of socialism in general because it reveals a real economic problem in the construction process of the said objective. Oskar Lange (1936), both seriously and ironically, understood the degree of relevance to Mises's challenge to the point of suggesting the construction of a statue to honor the Austrian in front of an eventual socialist central planning department. The practical problems of planning in the USSR were studied with the theoretical basis of the problem of economic calculation, though the details of this process may be distant to the theoretical occidental economist who is not aware of the debate. Barbieri (2004) reminds correctly that the Soviet attempt to create an economy without prices immediately after the Revolution of 1917 failed. There was a need to 'regress' (from a socialist point of view) to a market economy, with the New Economic Policy in 1921.

The socialist economists, to whom Mises (1920) directed his work, believed that they could establish the ideal of a planned economy. Mises argued that the socialists, in their willingness to achieve this non-market economy, ignored practical problems. The presence of prices, he emphasized, gives the capacity to calculate the viability of projects by the comparison of costs and returns. In his view, the market makes possible that the productive process of finding the solution on how to use resources to achieve the demanded production by the most efficient way. Everyone works with market prices and with the weighing of costs and benefits, including the consumers. According to the Austrian theory, there is no way to have an efficient economy that could bring welfare to people without the market<sup>5</sup>. It should be noted that Mises's main argument is also an ideological defense of liberalism<sup>6</sup>, but his emphasis is technical. In fact, the liberal political philosophy related to the Austrian school does not immediately interfere in the challenge to the socialists, because, even with the antagonistic position to them, it is a concrete problem of the economic order.

Barbieri (2004) shows that the debate allowed the Austrian school to become a distinct school from the neoclassical one: this allowed the Austrian School to distance itself from general equilibrium models, denying the centrality the neoclassical economics attribute to them, and forced them to dedicate its attention to the real problems of information, knowledge and adaptability. The equilibrium to the Austrians is never a firm criterion of the market, because this would give a static character to the exchange process, which is necessarily a process of unending adjustments and individual learning

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<sup>5</sup> Mises had in mind one of the propositions by Otto Neurath, who advanced that the economic planning of the wartimes could be applied in peace times through a 'national accounts system' (no relation with the modern term) that could objectively attend the necessities of each person; in such a situation, money would be dispensable, creating a moneyless economy. See Caldwell (1997).

<sup>6</sup> Mises believed that "the economic science (and least in [his] hands) taught that the unhampered market economy within a system of private property accomplished [the economic welfare] goal more effectively than alternative systems." (Boettke, 1995).

and, thus, out of equilibrium. The change of priorities allowed them to popularize the perception of the market as a discovery process, where the agents interact using their information in a scarcity context. Additionally, the ideas on the function of prices, welfare and methodology were equally consolidated by the Austrian effort in the debate (Kirzner, 1988; Boettke, Coyne & Leeson, 2005).

After Mises launched his argument, many authors tried to answer him. Barbieri (2004, p. 82) identifies two sets of replies: first, in the 1920s in German, and, afterwards, in the 1930s in the English speaking world. The English debate had greater resonance between the economists, because the socialist authors incorporated the Walrasian neoclassical model in their arguments. Since there is no practical difference between the capitalist economy and the socialist economy in the general equilibrium model, as Barone already showed twelve years before Mises's article (Barone, 1908), the socialist State would have the same role of the producer-consumer agent in the general equilibrium model and would become the 'benevolent dictator' or the 'Walrasian salesman'. The socialist authors tried to show that with the help of the Walrasian model it could be possible to calculate optimal quantities and prices in any economy, either socialist or capitalist. Thus, the problem of the central planner would be simply "to build the model" (Caldwell, 1997). There would be an analytical equivalence between the Walrasian model both to a planned economy and to a free-market economy. Lange (1936) proposed the definitive socialist answer to Mises's challenge. In his two-part article, *On the economic theory of socialism*, he argued that if we understand prices as opportunity costs, fixing prices would not be a peculiarity of the socialist system. With the knowledge of the historical prices series of the pre-socialist system and using them as a benchmark to the central planning (under the oversight of a central planning board), and the knowledge of the costs of capital and labor, the central planning board would instruct the managers of the factories to find an optimal combination of inputs.

In this sense, firms would not exist to maximize profits, but to provide goods to society in order to achieve the criteria "each one according to its necessity". The mechanism of entering and exiting of firms would be emulated by expansion and contraction of activity. In the end, central planning would be better than the market economy, because there was no theoretical difference between them. Burczak (2006, p. 32) reminds us that Lange believed the neoclassical model was a precise representation of the real economy and that it could be used to analyze the observed price system. In this way, the dynamics between the price and the value system could be assimilated and put up with the general problem of economic planning or programming.

However, Hayek rebuked his model. He showed the difficulty to obtain the necessary information for such an endeavor, pointed the difficulties on how to formulate the equations, and showed the system was incapable of adapting to uncertain changes. In his interpretation, it would be a pointless effort to attempt to build a complete Walrasian model of the economy to artificially create a socialist system of prices to attain the

socialist principles. In two articles, *Economics and Knowledge* (1937) and *The Use of Knowledge in Society* (1945), he argued that no central planner has enough information to decide what is better to society, because the “concept of [general] equilibrium is of no significance” (Hayek, 1937, p. 36) and its relevance lies only at individual level.

The problem arises with the expression “given data”, which is a relevant concept for theoretical models, but it does not apply to reality. Hayek starts to direct his attention to the “problem of knowledge” (Barbieri, 2012), which is different from the problem of asymmetrical information: knowledge is not only information, but it encompasses all that has been socially constructed through a process of cultural evolution. In this sense, the market would be more efficient in taking advantage of the limited, disperse and tacit knowledge in order to mobilize resources and to create institutions that can take advantage of it, in a way that is more efficient than any central planner. Thus, the apparent “chaos” of the decentralized process of production would not be a defect, but rather a creative feature of the capitalist economy.

The aftermath of the debate was that, lending the military jargon, the socialists obtained a tactical victory, because they managed to show that there is no difference between a centrally administered economy and a pure free-market economy. Thus, they were seen as the winner of the debate for a long time, which meant a defeat for Mises in the theoretical field. The problem was just the practicality of such a mode of production, organization and distribution: how can one implement this in practice? This open question was already touched upon by socialists and becomes extremely relevant at that point. It would be reckless to announce the Austrian defeat, because they had obtained a strategic victory with the collapse of the Soviet Union, which supposedly closed the debate.

In terms of progression of scientific programs, the debate on the socialist economic calculation can be seen as the precursor of many paradigms that did not exist before the end of the Classical Political Economy. For example: (i) the research program of econometrics, in which Oskar Lange became one of the precursors in combining quantitative methods developed in the West with planning strategies from the East, and the linear programming theory applied to the economy; (ii) the development of the objective value theory in a modern incarnation, with Sraffa (1960); (iii) the definition of complexity in the economy, with the adoption of dynamic models with spontaneous order and out-of-equilibrium economics; and (iv) the agent-principal problems, especially shown with the practicality question of economic planning. Due to the fact that various theoretical aspects of economics in the 20<sup>th</sup> century have (directly or indirectly) their origins in Mises’s challenge, it would not be wrong to consider the question of how the calculation realized in capitalism turns into the calculation in the socialist economy as the most abstract theoretical problem of the frontier of economic science.

But the main feature of the socialist economic calculation debate was to have drawn a clear line between two groups that stand for the real economic transformations

that developed after the British hegemony and the barbarity of the First World War. Here, the high level of abstraction allowed the use of neoclassical models by the socialists that, analytically, the planned and market economies would be identical. Barbieri (2004) emphasizes that the three schools of thought (Marxist, Austrian and Neoclassical) found points of contact and dialogue because they had a definitive objective in common, but the dividing line was always markets versus planning, mirroring the contradiction that was capitalism versus socialism, in the Cold War.

In this quarrel between groups of much defined opinions, where would Keynes be? Would he be at the Austrian side, which endeavored to showed that the construction of a centrally planned economy was a wrong and impossible task, or at the socialists side, who fought to assimilate the analytical methods as a tool that helped turning the national economic planning a reality?

### **3. Keynes, his political thought and relation with Austrians and socialists**

Keynes was a natural polemicist and had strong political opinions and they are spread through all his works. The Keynes family had a tradition of erudition and he was conscious of his privileged situation: “The *class* war will find me on the side of the educated *bourgeoisie*.” (Keynes, 1932a, p. 297, emphasis in the original). He entered into politics and he became a lifelong member of the Liberal Party. The Downing Street frequently called him to list his ideas. When the Conservative Party won the elections in 1932, his suggestions of heterodox policies made the government stop consulting him. He guided his political philosophy under these aspects:

“The political problem of mankind is to combine three things: economic efficiency, social justice, and individual liberty. The first needs criticism, precaution, and technical knowledge; the second, an unselfish and enthusiastic spirit, which loves the ordinary man; the third, tolerance, breadth, appreciation of the excellencies of variety and independence, which prefers, above everything, to give unhindered opportunity to the exceptional and to the aspiring.” (Keynes, 1932a, p. 311).

It should be noted that, while he was a liberal, he was against the consensus that favored *laissez-faire* policies. As Dillard points, in one of the earliest of his many biographies, “[He] was predisposed to be critical of orthodox economic policy and theory from the beginning of his career.” (Dillard, 1948, p. 317). Merquior places Keynes as a “left liberal”, part of the social liberalism that rejected the *laissez-faire* and social darwinist doctrines, while respecting the individual liberties in the process (Merquior, 2014).

The British economic orthodoxy favored free-market policies and Keynes criticized them. In “The End of Laissez-Faire” (in Keynes, 1932a), he wrote “The world is *not* so governed from above that private and social interest always coincide.” (p. 287), thus rejecting the premise that self-interest is enlightened, that the ‘invisible hand’ automatically moves society in the best possible path and that it should not suffer

interference from the government. *Laissez-faire* seemed more “natural” because it established a narrative in which the unbounded market creates wealth, and this narrative is much stronger than its opponents, viz. protectionism and Marxism. However, his historic summary in the beginning of the cited article serves to show that *laissez-faire* is not *that* natural.

He criticized not only the theoretical foundation of the *laissez-faire* but also the attitude of its supporters: “devotees of Capitalism are often unduly conservative, and reject reforms in its technique, which might really strengthen and preserve it, for fear that they may prove to be first steps away from Capitalism itself.” (p. 294)

While Keynes was aware of the flaws of capitalism, he did not believe that revolution would solve its problems. Rather, he adopted an approach similar to the Fabian Society, i.e., a gradual increase of wealth enough to provide acceptable individual wealth for each person. In “Economic possibilities for our grandchildren” (in Keynes, 1932a), written in the early stages of the Great Depression, he was undoubtedly optimistic concerning the future of mankind: “The prevailing world depression, the enormous anomaly of unemployment in a world full of wants, the disastrous mistakes we have made, blind us to what is going on under the surface to the true interpretation of the trend of things.” (p. 322) The Great Depression would pass because it was part of the growing pains of a new age that concentrated the greatest share of mankind’s economic development. “All this means in the long run *that mankind is solving its economic problem.*” (p. 325, emphasis in the original). His optimism also remained in the conclusion to his last article: “We shall run more risk of jeopardising the future if we are influenced by indefinite fears based on trying to look ahead further than anyone can see.” (Keynes, 1946, p. 187).

Thus, having established a draft of Keynes’s political thoughts, we move to consider Keynes’s position concerning the Austrian school and the socialism. Keynes did not have a direct opinion on the Austrian school itself<sup>7</sup> but he surely rejected *laissez-faire*. However, he did review Mises’s book on monetary theory<sup>8</sup>, and his relation with Friedrich Hayek is one the most discussed personal relations in economics. Christiansen (1993) remarked that the reconstruction of the original debate is very truncated, as seen that they were positioned indirectly in relation to each other. Scheall (2015) argues that the differences makes the debate pointless whether it is possible to say if one is ‘right’ and the other is ‘wrong’. Anyway, it is not impossible to give a general presentation of main differences between the two thinkers, given extant researches.

In his analysis of the relationship between the two intellectuals, Wapshott relates that they first met in 1928 (Wapshott, 2011, p. 47). They discussed from their first meeting on the role of the interest rate in the economy and they were mutually interested

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<sup>7</sup> Given how we explained that the school was in formation during the 1930s, it would be unlikely that Keynes, or any other economist, could have an opinion on the Austrian school as we know today, unlike socialism.

<sup>8</sup> Keynes described Mises’s book as “enlightened”, but at the same time comments that it offers no alternative in its criticism of monetary theories. (Keynes, 1914).

in their ideas. They formed a friendship without problems, despite the difference in their approaches. In Hayek's own words, "we remained thereafter friends who had many interests in common, although we rarely agree on economics" (Hayek, 1966, p. 240). Afterwards, Lionel Robbins invited Hayek to the London School of Economics with the intention of making a counterpoint to Keynes in Cambridge, whose ideas started to take a different form from the liberal orthodoxy. The invitation resulted in a lecture series and the eventual admission of Hayek in the faculty in 1931.

The controversy on Hayek's review of *A Treatise on Money* was the most known academic episode involving the two. We will not enter in details because this controversy is beyond the scope of the article and there is enough literature on it<sup>9</sup>. However, the aftermath is of interest: this debate showed how far Keynes had departed from the *laissez-faire* liberalism. Hayek used a microeconomic framework, in which the focus was the individual influencing the economy. Keynes, on the other hand, analyzed the economy from an upside-down point of view, where the analysis consists of seeing supply and demand as aggregates of all unities. And it is from this point that the detachment of macro from microeconomics starts, completed with the Keynesian revolution<sup>10</sup>.

In the aftermath of the debate, Keynes wrote a letter to Hayek, dated 03/29/1932, saying: "I am trying to reshape and improve my central position, and that is probably a better way to spend one's time than in controversy." (Keynes, 1932d, p. 173). And the central position would become *The General Theory of the Employment, Interest and Money* (GT) (Keynes, [1936] 1992). Hayek's reply, awaited for the entire British community, never came, and to speculate why his answer never came is a debate for its own<sup>11</sup>.

They remained in contact during the following years until Keynes's death. He got a copy of *the Road to Serfdom* (Hayek, [1944] 1990) and the book was well-known for being a warning against the increasing size of the State in the economy, that in the end freedom would be seized and thus signaling the end of the civilization. Although it is clear that Keynes advocated planning, he wrote that "morally and philosophical I find myself in agreement with virtually the whole of it; and not only in agreement with it but in a deeply moved agreement." (Keynes, 1944, p. 385). The reason why he agreed, again, was the fact that they both grew in the same tradition: liberalism. However, Keynes did not hesitate in criticize some points of his book, to which we will address later.

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<sup>9</sup> Caldwell (1995) compiled Hayek, Keynes and Sraffa's exchanges.

<sup>10</sup> We avail that the separation between macro and microeconomics made the return to the Classical Political Economy a difficult movement. The separation between macro and micro is also solved by the Austrians, according to Garrison (2005).

<sup>11</sup> See Caldwell (1998) and Howson (2001). Hayek himself reminisced, "I have to the present day not quite got over a feeling that I had then shirked what should have been a plain duty." (Hayek, 1963, p. 60). Sanz Bas (2011) reconstructs Hayek thought and analyzes how an indirect reply to the GT is present spread through his post-GT works.

Now concerning Keynes's opinion on socialism, there is a great number of reports on his opinions. He had a low opinion on Marx and Marxism: "How a doctrine so illogical and so dull can have exercised so powerful and enduring an influence over the minds of men and, through them, the events of history." (Keynes, 1932a, p. 285). He also blamed the ineptness of Marxism one of the factors why *laissez-faire* succeeded.

In his report about his visit to the Soviet Union, Keynes (in Keynes, 1932a) criticized the communist rule and the intolerance of the Communist Party in accepting dissenting views. "Lenin [was] a Mahomet, not a Bismarck" (p. 257) and that communism could succeed only as a religion<sup>12</sup>. Keynes, echoing Mises, also criticized communism because of its lack of practical solutions to economic problems:

"On the economic side I cannot perceive that Russian Communism has made any contribution to our economic problems of intellectual interest or scientific value. I do not think that it contains, or is likely to contain, any piece of useful economic technique which we could not apply, if we chose, with equal or greater success in a society which retained all the marks, I will not say of nineteenth-century individualistic capitalism, but of British bourgeois ideals." (p. 267).

Thus, it was clear that Keynes saw Soviet Communism a threat to the civilization as great as German Nazism<sup>13</sup>. However, concerning British socialism, Keynes had a more moderate view, but still critical. He had contact with the Fabian socialists, especially in his younger years<sup>14</sup>. One of his most important protégés was Maurice Dobb, who participated of the socialist calculation debate<sup>15</sup>. In fact, British socialist intellectuals were an important minority. In an earlier draft of the GT, Keynes intended the last chapter of the book to be about socialism. It was from 1932 and it seemed to be discarded. (Keynes, 1932e, p. 50). In a speech for the Society for Socialist Inquiry, he said the following:

"Besides two arms and two legs for oratory, gesticulation and movement, Socialism has two heads and two hearts which are always at war with one another. The one is ardent to do things because they are economically sound. The other is no less ardent to do things which are admitted to be economically unsound. I mean by economically sound, improvements in organisation and so forth which are desired because they will increase the

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<sup>12</sup> Comparing Sidney and Beatrice Webb's report on the Soviet Union, written over ten years after Keynes's, and in a more positive (some would say sycophantic) note, one is ought to find amusing the contrast: "The administrators in the Moscow Kremlin genuinely believe in their professed faith. And their professed faith is in science. No vested interests hinder them from basing their decisions and their policy upon the best science they can obtain." (Webb & Webb, 1936, p. 18).

<sup>13</sup> Concerning Soviet views on Keynes, Letiche (1971) wrote that the GT had a censored translation in Russian and the Soviet *intelligentsia* heavily criticized him for his bourgeois positions. Lenin, though, held him in high regard due to his opposition to the Treaty of Versailles (p. 442).

<sup>14</sup> In 1914, J. N. Keynes called out him for being "a Socialist and is in favour of confiscation of wealth" (Moggridge, 1992, p. 190).

<sup>15</sup> See Dobb (1933). Although Dobb had a critical view of the quick acceptance of neoclassical views by socialists, because they made little effort to conciliate with Marx's value theory of labor (sometimes even rejecting it).

production of wealth; and by economically unsound things which will, or may, have the opposite effect.” (Keynes, 1932b, p. 155).

Here, Keynes admits that the socialist economists want to pursue “economically sound” objectives mainly because the majority of the socialist economists Keynes was addressing were not the Marxian pro-Soviet economists, but rather the Labour Party. “[The Labour Party] have not fundamentally disagreed with the other parties as to what is economically sound or unsound.” (p. 157). In his opinion, the problems with socialism was that they wanted to pursue ideal, “higher goods” such as justice and equality (which are honorable objectives in themselves) in exchange for wealth – Keynes asks if the sacrifice is worthy, because for Keynes increasing wealth was necessary to attain the “higher goods”; and, of course, the political problem, “the stir of humors”, the revolutionary way had problems. The main problem was that it might presuppose that socialism would need to “ruin” the system in order to build a new one – which is quite similar to Mises’s argument in 1920, that socialists ignored practical problems.

So, in order to find “economically sound” solutions, we must find ways to increase individual wealth, “Our prime task, therefore, is to discover, and then to do, what is economically sound. This temporary concentration on the practical is the best contribution which we of today can make towards the attainment of the ideal.” (p. 161)

Thus, Keynes definitely was no socialist. However, there were many authors that did try to combine Keynesian ideas with socialism. One of them was Hayek’s main interlocutor in the debate, Oskar Lange. Lange never met Keynes personally. However, they exchanged letters, in which the author of the GT “had a moderately good opinion” of the Polish, according to Louçã (1999). Adept of the historical materialism, Lange had been involved in interpreting Keynes. He came to elaborate a Walrasian-Keynesian economic model, one year after Hicks had drawn the IS-LM model<sup>16</sup>.

Lange also contributed with notable interpretations of Keynes’s work, affirming that the concept of liquidity preference had been present in Walras. Even though his model and observation were published after the IS-LM, his view of Keynesian economics could be considered closer to the neoclassical synthesis. Because of this, ‘Lange’s Keynes’ was divulgated “without a full understanding of Keynes’s breakaway from mainstream orthodoxy” (Olesen, 2008). Lange, it seems, was more interested in making Keynes’s views fitting into his own writings<sup>17</sup>.

And thus, this brings us to one of the most important things debated in the socialist calculation debate: the role of the State in the economy, whether planning or

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<sup>16</sup> See Lange (1938). However, the 1938’s article did not focus only on Keynes, but also further issues along with Kaldor and Kalecki, see Assous & Lampa (2014).

<sup>17</sup> For more details, see Olesen (2008) and Toporowski (2012). Joan Robinson, commenting on Lange’s article, wrote that “Lange’s article tho’ silly is formally quite correct” (Robinson, 1938, p. 169). Schumpeter, on the other hand, would agree with Lange, “the Keynesian analysis of the *General Theory* (not of the *Treatise* of 1930) is but a special case of the genuinely general theory of Walras.” (Schumpeter, 1954, p. 1047). Also, according to Letiche (1971), Lange also believed that the Keynesian theory of unemployment could explain the Neo-Marxist theories of underdevelopment.

free-market, the State needs a role. Again, Austrians thought the role to be minimal, while the socialists supposed that the State was essential for the progress of the communist objective.

Throughout Keynes's *oeuvre* there are innumerable thoughts on the role of State. For the article, we will try to narrow our approach to the thoughts on planning. In "Can Lloyd George do it?" (in Keynes, 1932a), he openly advises active governmental intervention in order to ease the consequences of the slump and depression: "A very large part of those economic enterprises which absorb substantial amount of capital have fallen under the influence or the control of government departments... Thus it is not a question of choosing between private and public enterprise. *The choice has been already made.*" (p. 113, emphasis added).

The denoted phrase reveals that, for Keynes, there was no point in discussing whether there will be planning or not, because it *already* exists. In spite of the danger of crowding-out, it was the duty of the State to step up when market coordination failed and to cultivate a good environment for the entrepreneurs to create new technologies, because they were expressions of individual liberty as well – and this is something he criticized in the socialism, "because it takes away from man's natural liberty to make a million, or because it has courage for bold experiments" (Keynes, 1932a, p. 290). Bold experiments and state regulation were necessary to create a liberal order. In a radio broadcast, he said:

"I have said that it is of the essence of state planning to do those things which in the nature of the case lie outside the scope of the individual. It differs from Socialism and from Communism in that it does not seek to aggrandise the province of the state for its own sake. It does not aim at superseding the individual within the field of operations appropriate to the individual or transforming the wage system or of abolishing the profit motive. Its objective is to take hold of the central controls and to govern them with deliberate foresight and thus modify and condition the environment within which the individual freely operates with and against other individuals." (Keynes, 1932c, p. 88)<sup>18</sup>.

His views on the role of the State are prevalent in the GT. In few words, it is possible to affirm that the General Theory presents the problem in its own terms: how does one change the negative results for the public that stems from the plain comparison between the marginal efficiency of capital and the interest rate as the criterion for making investment? Keynes's system answers this by indicating that the State influences the interest rate so that the private decisions of use of resources go in the projected direction. It is a mediated kind of planning: the State controls the economy only indirectly by changing the taxes of return connected to the issue of State money. Here we see what kind of planning is in Keynes's mind: it does not change the fundamental stone of capitalist logic, since the animal spirits of investors are merely "guided" by the State towards some chosen destiny. It is not a centralized method of coordination. Private owners of capital are free to use their property as they wish. But the market

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<sup>18</sup> His argument can be considered as a precursor to the concept of "entrepreneurial state", as advanced by Mazzucato (2013).

circumstances are such that their decisions are forced to attend public interests, besides fulfilling their aim of achieving profits (see Almeida F<sup>o</sup> & Lopes, 2011).

And this brings us back to Keynes's letter to Hayek. Sheamur claims that "Keynes' criticism misses the mark, and rather badly" (Sheamur, 1997, p. 70) because he failed to understand that Hayek was not a *laissez-faire* economist. However, we argue that his reply to Hayek is consistent with what he believed on planning, especially the fact that the tendency of economies to adopt some sort of planning already.

He echoes Lange's argument when he wrote that "from the purely economic point of view [planning] is efficient" (Keynes, 1944, p. 386) and that planning technologies were improving, to the point of not requiring the "superfluous sacrifice of liberties" that Hayek was concerned about in his book.

For him, Hayek's ideal society needed planning and it had a moral component: "planning should take place in a community in which as many people as possible, both leaders and followers, wholly share your own moral position." (p. 387). As long as planners are aware of the precepts to build a good society, the world envisioned in "Economic possibilities of our grandchildren" would be possible.

However, Keynes's position on planning and the role of State would not stay unchallenged. Hayek himself in his "Nobel" lecture blamed planners for committing the "pretense of knowledge" (Hayek, 1974). They did not understand that economic variables cannot be freely manipulated without consequences, and thus they plunged the world in a crisis of stagflation<sup>19</sup>. And, of course, modern Austrian school thinkers are generally critics of Keynesianism (e.g. Steele, 2001; Sanz Bas, 2011). Socialists, on the other hand, have criticisms of their own. Paul Sweezy criticized Keynes for "treating the state as a *deus ex machina* to be invoked whenever his human actors, behaving according to the rules of the capitalist game, at themselves into a dilemma from which there is apparently no escape" (Sweezy, 1946, p. 303).

The issue will be expanded in the next section, that will explain how Keynes solves beforehand the economic calculation problem.

#### **4. The elimination of calculation in Keynes and the 'information problem'**

Keynes had a solid statistical formation and wrote on theoretical probability (Keynes, 1921). For him, it was clear how much uncertainty could influence the economy and that long run expectations could not be always correct. In his own words, "we have, as a rule,

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<sup>19</sup> However, Hayek spared Keynes of *some* of the blame: "And I have little doubt that we owe much of the post-war inflation the great influence of such over-simplified Keynesianism. Not that Keynes himself would have approved of this. Indeed, I am fairly certain that if he had lived he would in that period have been one of the most determined fighters against inflation. About the last time I saw him, a few weeks before his death, he more or less plainly told me so. As his remark on that occasion in illuminating in other respects, it is worth repeating. I had asked him whether he was not getting alarmed by the use to which some of his disciplines were putting his theories. His reply was that these theories had been greatly needed in the 1930s; but if these theories should ever become harmful, I could be assured that he would quickly bring about a change in public opinion." (Hayek, 1966, p. 243).

only the vaguest idea of any but the most direct consequences of our acts” (Keynes, 1937) and the more distant the horizon of action, the more uncertain will be the results<sup>20</sup>. In other words, they are subject to uncertainty: there is no scientific base on how to calculate events like “the price of copper and the rate of interest twenty years hence, or the obsolescence of a new invention, or the position of private wealth owners in the social system in 1970.” As Butos and Koppl (1997) put, Keynes “did not believe that entrepreneurs could simply make a list containing every possible future outcome, assign a probability to each item on the list, and then calculate an expected value.”

The animal spirits, genuine expressions of the ultimate wishes of the profit-seeking investors, are present in the structures of a monetary economy and turn the market inherently unstable. This view of the agent that makes the investment decision removes completely the base of calculation or the study of the objective condition of demand: for Keynes, the money-possessing consumer is not concerned in knowing the conditions of market. The owner of abstract wealth, money, absolute liquidity, the social power of conversion of value does not seek to know which level of effective demand will be effectuated. This would be an issue for the State. In this sense, we can notice that the calculation problem in Keynes does not belong to the individual, but to the instance responsible to keep the demand level.

To Keynes, the interest rate derives from the positive spirit of the investor, and it seems that there are no objective conditions to calculate the individual adjustment to social demands. In the usual non-keynesian perspective, the investor is taken as a punctual analyst who collects information on the market he wants to act, makes calculations, projections, based on economic conjecture analysis and from this point he makes an investment decision.

The contrary applies to Keynes’s view: there is no reason to collect information, the first step is the realization of the investment as pure and simple leap from liquidity to a less liquid position, whose counterpart would a return greater than the interest rate concerning the sold liquid asset (Carvalho, 1992; Ferrari, 1991). The only task would be the comparison between the interest rate and the current marginal efficiency of the capital. The effects on the investment in his concrete determination, in other words, in his expansive and resultant production in a specific supply structure, is not a role of the investor, but of the State. And it is from this point that one can build a conception of socialization of investments in Keynes: a coordinated capitalism, in which the calculation problem would necessarily disappear for the individual producer.

In this direction, the concept of Keynesian uncertainty seems to approach Hayek’s original thesis of unfeasibility of calculation, which does not only attend the logic of valorization of value. Rather, the very concept of uncertainty seems to create a potential

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<sup>20</sup> It might be argued that was the reason why Keynes considered Marxism to be unfit: the communist society was a bold prediction in the context of uncertainty.

common basis between Keynes and Hayek, although the precision of the term can create discrepancies between them, as Angeli (2007) shows, on Hayekian uncertainty.

From another point of view, Barbieri (2012) accents that the recent debate on the socialist economic calculation, retaken by modern adepts of the market socialism, return to the same problem identified by Hayek: the knowledge problem. The models that try to emulate the decentralized spontaneous discovery processes do not consider the nature of calculation errors in an adequate way. So, to what extent does this knowledge affect the agent in the market, and would they be closer to the position of Keynes and Hayek? This would be a parallel question that, even if it clarifies similar methodological backgrounds among the two authors, it does not resolve our question, as Keynes would stay without a definite position.

Thus, recognizing that uncertainty is inevitable, Keynes did not enter in the calculation debate because his theory seems to veneer a State responsible to avoid the frustration of the individual investments, or better, to oblige the investors to handle the wrong investment choices. With this, it seems that there exists, beyond the two political motivations suggested in the introduction, a third point, coming from the theoretical basis of his economic thought. This third point needs to be studied with greater care, since it is developed from a post-keynesian point of view, which, according to our interpretation, is faithful to Keynes's original general intent of elaborating a new view on the economics.

In fact, Carvalho (2008) already had touched on the topic of positioning Keynes in the debate, but his immediate answer did not touch the fundamental theme. He argues that the problem for Keynes was completely different from the debate in which Mises, Hayek and Lange got involved, which enforces the idea that the main motivation for not participating in the debate would be his theoretical vision. Certainly, "the problem in capitalism, according to Keynes, is not the allocation, but the mobilization of resources" (Carvalho, 2008, our translation), because what matters is the employment of all production factors, regardless of the concrete characteristics of the use values realized in the markets.

It happens that the socialist economic calculation debate problem does not limit itself to the problems of capitalism. *It is a problem of normative politics, limited to the general economic laws.* Among those who intend to construct a system beyond capitalism, the debate serves to identify problems and solutions to a different, non-capitalist order, in which the use values follow the will of the working population and not of the capitalist producers. For those who keep the economic organization around private property, the debate is useful to demonstrate the difficulties of this transition and to illustrate their claim that a system of collective property is doomed to failure. Thus, the debate treats the general economic problem, the production and distribution of useful goods to society. In this sense, the analyst, the economic advisor and the policymaker in capitalism will deal with the question as long it is a practical political problem that touches in the current social relations. But the question in itself cannot be bypassed by the

economic scientist, because it is a *general* problem of the economy, and not only of capitalism.

In this sense, even if Keynes had avoided entering in the discussion, the historic conditions that indicate that the transition to socialism is an empiric fact will, sooner or later, oblige the identification of his theoretical positioning in the debate. Keynes's supremacy over Hayek and Lange is secured only while the third way continues being the solution of the contradiction between planning and market.

## **5. A three-fold answer**

Finally, why didn't Keynes participate at the socialist economic calculation debate? The solution found in this article seems to furnish a secure basis for the search of greater details on the notion of economic planning in Keynes. The research started here points to an answer composed of three elements, two of political and one of technical nature.

In first place, the debate occurred among traditions which doctrines Keynes did not show interest. In order to participate of the debate, he would need to choose a specific framework, Neoclassical, Austrian or Marxist. Besides, the abstraction level turns the debate into something distant from the relevant policies of the moment. In the 1920s, Keynes prepared his theory without concerning itself with technical questions: he just wanted to give support to the new State at the end of classical liberalism and the problem of the socialist economic calculation would have no practical influence on the points he judged to be important. His intuition and political wisdom were correct and his domain in the economic teaching was assured.

Second, the participation in the debate required that all participants had a clear position concerning the planned socialist economy: in spite of the debate being technical, the politics clouded the technicalities, and the debaters had to take a position. Keynes tried to avoid both extremes (the pure liberal economics and the complete centralized planning), creating a balance between market and control without a rigorous theoretical ballast. Politically, it was relevant to establish the idea of a conciliatory political economy that combined both liberal market elements, as well as the national coordination. In addition, the social democracy already dawned as the most appealing system in the West and the reformist path opened the possibility of the modification of capitalism without its overcoming.

Third, the concept of uncertainty emphasized by the Post-Keynesians seems to explain why Keynes solved the individual calculation problem beforehand: the question of being guided by market data to make correct decisions is not part of the Keynesian perspective of investment. Here, the investor has the single task of placing his private resources at the disposal of the society, which will be publicly used by an agent that knows how to operate productive investments that will guarantee the pecuniary return to the individual owner. In this sense, the problem is already solved with Keynes's

description of socialization of investments, something that is an open question inside the theory of one of the most influential economists of the 20<sup>th</sup> century.

This indication stays, as such, as an invitation to the contemporary Keynesians to the debate on how an economy that surpasses the individual decision on the utilization of the resources of society must be organized. The effort to approach the terms of discussion between different schools of economic thought is of great importance to give unity and amplitude to this debate. For this reason, it must be part of the main tasks of economic scientists of the present, as well as of those who have the political objectives of advancing the change towards socialism and of those who wish to avoid it.

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