

Socialism and the Market: Methodological Lessons from the Economic Calculation Debate

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I. INTRODUCTION

1. There is a renewed interest in ideas that are broadly known as market socialism.
2. The relation between socialism and the market has been an issue of contention among socialists since Marx’s own time. For instance, Marx, criticized Pierre Joseph Proudhon as “the paradigmatic theorist of petty bourgeois socialism” who “sought to improve society not by abolishing commodity production but, rather, by purifying commodity exchange.” (McNally 1993:139) Proudhon offered a vision of a socially regulated network of private small-holdings through the administration of mutual aid including such means as interest free credit.
3. The first great debate on the relationship between socialism and the market was initiated by Ludwig von Mises (1920) who claimed that without private property market exchanges could not take place and without them rational valuation would cease resulting in economic chaos. The historical background to this debate was the establishment of the Soviet power in Russia in 1917 and the subsequent degeneration of the Soviet state and the Communist party after Lenin’s death in 1924. The second wave of debates took place in the 1960s when market socialist ideas gained significant support in Eastern Europe and Soviet Union, and were implemented in a number of countries most notably in Yugoslavia. At the same time the leadership of the Cuban revolution engaged in a public international debate regarding the relationship between socialism and the market.
4. The historical conjuncture for this new interest in market socialism is remarkably different: it is characterized by long-cycle of economic stagnation in industrial capitalist countries, failure of Keynesian policies and nationalist projects of import-substitution industrialization in latecomers, and demise of bureaucratic central planning in the Soviet Union and Eastern Europe during the 1970s and 1980s (Nayeri 1998). These developments aided the ideological campaign to advance neo-liberalism that aims to solve the capitalist crisis upon the back of the working people. Thus W. Scott Arnold writes:
5. Sometimes in the middle-to-late 1980s, something approaching a limited consensus began to emerge among the intelligentsia in the West. This consensus holds that the inefficiencies endemic to any centrally planned economy are serious to the point of being

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catastrophic and that the only reforms that have any chance of success are those which are part of a process of fundamental change that replaces central planning with the market. The view that central planning must be *replaced* by some form of market economy and not just augmented by the market in some way or other seems to be the distinctive feature of the new consensus (Arnold 1994:35).

6. This essay examines the underlying methodological issues in the “economic calculation debate” of the 1920s and 1930s from the perspective of the Marxian theory in order to shed some light on the current debate on market socialism and to inform socialist planning research and working class policy. I will show that the participants in the 1920s and 1930s debate used methodologies that are alien to the Marxian theory of socialism and I maintain (but do not attempt to show here²) that much of the debate since then suffers from the same fundamental methodological issues.

7. The economic calculation debate shifted the attention of many socialists from the political-ethical terrain to the field of economics. The primary issue in the debate was the feasibility and desirability of replacing the market mechanism with central planning as the principal mode of economic organization of the socialist society. While the participants in the debate focused on economic advantages or disadvantages of the use of central planning instead of markets, they paid very little attention to the character and goals of the emerging socialist society, or if they did, these differed sharply from Marx’s theory. The Marxian theory is singularly concerned with the process of socialist transformation of the capitalist society through replacing market-based or otherwise alienated and exploitive human relations with those consciously formed on the basis of human needs and solidarity. The key here is the revolutionary potential of the working people to transform capitalist reality and in the process transform themselves. Thus, a methodological schism between means and ends has characterized the economic calculation debate and subsequent debate on the relationship of socialism and the market.

8. Section 2 briefly reviews the contending claims in the economic calculation debate focusing on their methodological underpinnings. The essential conclusion here is that market socialist ascendancy in the economic calculation debate resulted from its ability and willingness to use the neoclassical theory and methodology to argue for socialistic values. As such the modern market socialist claim that markets are consistent with and indeed necessary for socialism is based on methodologies alien to the Marxian theory. Section 3 outlines the essential methodological underpinning of the neoclassical and Austrian critiques of central planning. It is argued that these theories are not methodologically robust and their critiques of central planning are based on assumptions that *a priori* preclude socialist transformation of the capitalist societies. The argument that Marxian socialist theory is methodologically different from these and all other pro-market theories, including market socialist theories, is outlined in Sections 4 and 5. Section 6 offers some concluding remarks and directions for future research.

² For some recent examples see Nayeri 2003.

II. THE EMERGENCE OF NEOCLASSICAL SOCIALISM

9. There are conflicting histories of the economic calculation debate. Early surveys by eminent economists such as Joseph Schumpeter (1954), Abram Bergson (1948) and Paul Samuelson (1948) took the position that in large measure the proponents of market socialism—Oscar Lange, H.D. Dickinson, Fred Taylor, Abba P. Lerner, and E.F.M. Durbin—offered the winning arguments against the Austrians, Ludwig von Mises, Friedrich A. Hayek, and Lionel Robbins.

10. Since the early 1980s, this view has been effectively challenged (Ramsey Steele 1981, Morel 1983, Lavoie 1985, Timken 1989). The most extensive of these re-interpretations is Lavoie's restatement and defense of the Austrian position. Lavoie's major criticism is that the early interpretations were influenced by the neoclassical readings of the Austrian arguments. Thus he is able to recast the debate in terms that state and leave unanswered certain well-known claims of the modern Austrian theory centered on the virtues of private property and the market process.

11. The critiques of central planning employed marginalist methodology from the onset (Howard and King 1992, 1994). In the 1880s, Friedrich von Wieser (1956) and Eugene von Böhm-Bawerk (1959) claimed that categories of the marginalist theory were universally applicable to all socioeconomic formations. Therefore, they saw these as essential to any economic system concerned with efficiency. Enrico Barone (1908) argued from a Walrasian perspective that the conditions necessary for an efficient allocation of resources (Pareto Optimality) were the same for any economy. However, it was also believed that accomplishing the requirements of the competitive general equilibrium was formidable in an actual planned economy. Ludwig von Mises (1920) argued a stronger case against socialism. He claimed that without private property market exchanges could not take place and without them rational valuation would cease resulting in economic chaos. It is generally agreed that Mises' argument was very poorly stated and most also agree that his original attack on central planning was not sufficiently differentiated from the neoclassical critique. However, it is also true that Mises gradually developed distinctively Austrian arguments against socialism (Chaloupek 1990).

12. Oskar Lange (1938) refuted the marginalist critique while providing a neoclassical case for realization of values of equality, rationality, planning and elimination of waste. Lange's model even provided room for workers' participation or self-management. As such it has served as the prototype for subsequent models of market socialism. Lange's essential insight was that neoclassical theory ignored capital-labor relations such that it makes no analytical difference whether capitalists hire workers or workers hire the management. Thus it was possible, Lange argued, to use the price mechanism to plan the economy in the context of public ownership of the social means of production.

13. Lange and the market socialists adapted to marginalist methodologies. Lange adopted the curious position that neoclassical theory was of far greater relevance to socialism than Marx's theory; his dictum was that Marx's theory was as essential for understanding capitalism as neoclassical theory was for socialism. In essence, Lange argued that markets are compatible with and necessary to socialism. This has become the central thesis of market socialists of every type.

III. METHODOLOGIES OF NEOCLASSICAL AND AUSTRIAN CRITIQUES

14. It is now necessary to examine the methodological underpinnings of the Marginalist critiques of central planning. Marginalist critiques are essentially arguments for the virtues of private property and the market that socialist planning will undermine. Noted Austrian economists Buchanan and Vanberg (1991) propose three types of virtues for private property and the market.

15. The neoclassical theory emphasizes the *efficient allocation* of market processes (Arrow and Hahn 1971). In this view, distorted incentive structures in a planned economy results in alternative choices that do not correspond to an individual's own preferences. Similarly, resources do not flow to their most highly valued uses because individual decision makers do not find it in their own interest to shift allocation in ways that meet this conceptually definable, and desirable, result.

16. This critique of central planning is centered on the notion of competitive general equilibrium. However, the very notion of general equilibrium involves a host of presuppositions, including perfect competition and perfect rationality of economic agents. Practically all these essential assumptions are objectionable. Rationality is only perfect when relevant information is perfect, and that includes knowledge of the consequences of actions. However, the consequence of actions not yet taken does not exist at the moment of choice. Thus, direct knowledge of objective and publicly assembled consequences of still available options for action is logically impossible. Perfect rationality belongs only to the timeless equilibrium in which all actions conform to a general simultaneous solution of the pooled statements of the preferences and resources of all participants. "When economic theory elects to bring in imperfect competition and to recognize uncertainty, there is an end of the meaning of general equilibrium (Shackle 1967: 295)." This criticism is valid even for the less presumptive neoclassical views such as rational expectations or Bayesian adaptive rationality (Buchanan and Vanberg 1991:318).

17. Thus modern Austrian theorists recognize the fatal flaw of the neoclassical critique of central planning and put forward their own arguments. Israel Kizner (1985) argues for the virtue of the market as a *discovery* process. In this view, only a decentralized market structure can capture and fully utilize the knowledge of localized circumstances required for a definition of the ultimate valuation that is placed on resource use. Only the market can allow individuals effective liberty to discover the particularities of local needs that form their preferences. However, Kizner's notion of the market as a discovery process "fails to escape the subliminal teleology of the equilibrium framework" as does his notion of entrepreneurial "discovery of opportunities or error" when the analysis moves from a cross-sectional to an inter-temporal framework (Buchanan and Vanberg 1991:320-321).

18. Therefore, basing themselves on the methodology of *radical subjectivism* associated with Shackle (1979), Buchanan and Vanberg propose the notion of market as a *creative* process. The basic insight of this new paradigm is that nature and society are creative, and novelty and genuinely unpredictable outcomes are generated as the evolutionary process unfolds over time. A characteristic of such a system is that small changes can have large effects. Thus, Shackle (1983:28) holds that every person's choice among alternative courses of action can be seen as "making history, on however small scale, in some sense other than mere passive obedience to the play of all-pervasive causes." Wiseman

(1989:230) concludes: “The essence of the radical subjectivist position is that the future is not simply ‘unknown,’ but is ‘nonexistent’ or ‘indeterminate’ at the point of decision.” To radical subjectivist Austrians, private property and the market process represent the institutional settings most compatible with the flourishing of the creative potentials of human beings. Thus, even though “indeterminate” change in the individual’s behavioral over time is admitted in principle, any social change in an anti-capitalist and pro-socialist direction is precluded by definition. As such, the radical subjectivist position is evolutionary only within the bounds of the capitalist system, which is claimed to provide the ultimate form of social organization for humanity. This implicit teleological and normative position undermines their claim to a non-teleological and purely scientific methodology and theory. Thus, the radical subjectivist case for the virtue of the market process and against central planning and socialism is also based on questionable methodological grounds.

19. Therefore, all three marginalist theoretical claims for the virtues of private property and the market seem to suffer from internal contradictions and their objections to central planning and socialism based more on normative judgment than scientific or logical merit. In fact, since marginalist theories are organized on grounds of methodological individualism, that is, they exclude the desirability and feasibility of socialism by definition. Jevons, Menger, and Walras represented the continuation of the individualistic, utilitarian premises of Say, Senior, and Bastiat. For them economics is defined as “the science which studies human behaviour as a relationship between ends and scarce means which have alternative uses (Robbins 1994:85).” It is on this basis that marginalist categories are developed and held to be universally valid. Thus all marginalist theories, including the radical subjectivist variety, tends to be too restricted to allow for any serious study of transition from one mode of production to another, and they are useless by design for study of transition for transition from capitalism to Marxian socialism. They are rather designed for analysis of what they hold to be common to all modes of production. In contrast, central planning in the Marxian theory is an essential means to inform and affect the process of socialist transition based on self-activity and self-organization of workers who gradually shed all forms of exploitation, oppression and alienation to bring about the society of Associated Producers.

IV. ESSENTIAL AND TECHNICAL ISSUES IN SOCIALIST PLANNING

20. The overall case against central planning is that non-market mechanisms of economic organization lack, impede or distort information, incentives and entrepreneurial activities necessary for efficiency and growth. However, the marginalist critiques of socialist planning are based on questionable methodological and theoretical grounds. The market socialist defense of central planning based on marginalist methodologies is also suspect. Still, issues raised by the economic calculation debate merit careful attention and the non-market socialist literature provide a host of responses to each of them. The more recent English language contributions include full-scale models for socialist planning (such as Devine 1988; Albert and Hahnel 1991; Cockshott and Cottrell 1993A) and responses to specific marginalist objections (such as Cottrell and Cockshott 1993B; 1989; Adaman and Devine 1996). This essay does not discuss any of the specific economic issues raised by the

calculation debate nor does it suggest that they are satisfactorily solved either in theory or in practice. Rather, it aims to expose the methodological divide between the Marxian theory of socialism and the pro-market critiques of socialist planning. These important methodological issues are not usually dealt with in the literature on non-market socialism.

21. From a methodological perspective the issues raised by the economic calculation debate can be divided into essential and technical ones. The essential issues deal with the nature of human activity such as the essence and structure of motivations and incentives. The technical issues involve limits imposed on human activities by the existing level of knowledge and the given set of technologies. The two sets of arguments can be invoked independently. However, it is important to note their interdependence. The level of knowledge and technical possibilities depends on the dynamics of society's social relations, and in turn, conditions them. The essential characteristics are primary but they can also be shaped by society's level of knowledge and technological matrix.

22. To bring the Marxian methodology into focus, it is useful to indicate how radically it differs from marginalist economic theories. The underlying premise of all pro-market theories is the liberal notion of human nature and society that developed between the sixteen to eighteenth centuries as a market economy took hold with the emerging capitalist mode of production in Western Europe.³ A central characteristic of this new mode of thinking was bourgeois individualism that attributed naturalized (eternalized) qualities to social, hence economic relations (Marx 1857-58:17-26). Thus Adam Smith imagined a calculating savage, with his inborn or acquired "propensity to truck, barter, and exchange one thing for another." Bentham's *homo economicus* and the philosophy of utilitarianism followed. Liberal theory holds that the bourgeois notion of human nature and society emerged only because inborn human "propensities" at last found their suitable outlet in a market economy. All pro-market theories, including those that purport to be socialist, share this methodological foundation centered on *homo economicus*.

23. Thus, these theories rely on a fundamentally different foundation than the Marxian theory. Furthermore, despite the marginalist claim to positive science, we know of no proof for the existence of the ahistorical *homo economicus*. In fact, recent research has found large and consistent deviation from textbook representation of *homo economicus*. Roth and his co-authors (1991), Fehr and Cächter (2000), and Camerer (2001) have found that in addition to their own material payoffs, many of their experimental subjects seemed to care about fairness and reciprocity, and willing to change the distribution of material outcomes at personal cost. The subjects seemed willing to reward those who act in a cooperative manner while punishing those who do not, even when these actions are costly to them. Using game theory in combination with anthropological and ethnographic research methods in 15 small-scale societies, Henrich and his coauthors (2001) found that universal patterns of behavior deviated strongly from the *homo economicus* model. Further, they found that a combination of economic *and* social factors appeared to condition economic behavior in these societies.

24. Thus, recent research tends to support the historical materialist conclusion that

³ The term liberal and liberalism take on different meaning in different countries and across time (see, Cranston 1967). I am particularly interested in their most general shared characteristics, especially as they relate to economic theory and policy.

25. Bentham's *homo economicus* was shaped in tandem with bourgeois transformation of traditional ways of life and consistent with the requirement of the new capitalist mode of production. Further, it lends support to the hypothesis that "human nature" itself can be shaped by human action to transform their environment, including a given social mode of production.

26. The Marxian theory of socialism recognizes the historical fact that capitalist societies function on the basis of ethical values and material incentives first generalized through what economic historians call the "commercial revolution" and has since been become institutionalized and constantly reinforced and deepened among individuals. The capitalist order requires sustained insecurity not only through the threat of unemployment and destitution, but also through fetishism of commodity and in the constant struggle "not to fall behind" or the hope of "getting ahead." These permeate bourgeois consciousness, not only among capitalists and managers, but in the very pores of the working people themselves. Greed, self-interest and competition, not solidarity and social harmony, lie at the base of the capitalist society. However, these very same capitalist social relations that form the bedrock of a historically unprecedented epoch of economic growth lie at the root of mounting social and environmental crises that threatens the very foundation of life on this planet. These crises and the ongoing class contradictions of the capitalist order generate social protests that can gradually take a class form with the potential to transcend the bounds of capitalist mode of existence. The theoretical and practical challenge is to begin from these actual, ongoing struggles, to generalize them, and to build independent mass organizations of workers and their allies to take power and chart a course to a society built on socialist values.

V. THE TRANSITION PERIOD

27. As we have seen, the goals and methods of the Marxian theory differ fundamentally from the marginalist theories. While Marxian theory has contributed significantly to the development of a number of fields of human interest, it is first and foremost a theory of socialism. Marx's critical study of the capitalist mode of production and the classical political economy was to lay the theoretical foundation for the working class movement to enable it to establish a workers' government and begin the process of socialist transition. Moreover, Marx's critique of the political economy is methodologically similar to his critique of Hegel who placed logic before experience and philosophers of the Enlightenment who treated abstractions as actualities. Marx showed how under the capitalist system animated abstraction of capital, including powers attributed to the market by pro-market theorists, assumed priority over nature and humanity. Thus he related Hegel's philosophy and political economic theories to the deep structures of the rising capitalist order. From these analyses, Marx arrives at his vision of socialist transformation of the capitalist mode of production centered on withering away of value as a social reality and for a new attitude towards nature and work embodied in a new form of production. To Marx, socialist planning was one powerful policy mechanism to affect this transition.

28. The efficacy of socialist planning is a function of the degree of organization and consciousness of the direct producers, the level of culture and technology already attained, and the balance of class forces internationally. A central task of socialist planning is to

replace bourgeois structure of incentives with socialist norms and motivations, which involve replacing accidental value driven market exchanges based on private gain with planned interchanges of use values based on human needs and solidarity. While the goal and the general direction of this movement are known, its precise course will depend on many factors. It is a historical process that depends on the self-activity, self-organization, and creativity of the direct producers themselves who emerge from the womb of the old society and carry with them limitations imposed by the bourgeois culture. In a world dominated by capital, it also depends on the extension of workers power internationally, especially to the capitalist centers. While much of the human character is shaped by circumstances of our existence, human beings have the creative capacity to remake the world in their own image. Therein lays the socialist aspiration.

29. While economic concerns, especially development of forces of production, are important to the Marxian concept of socialism, the central challenge in the transition period is a fundamental change in social relations predicated on the development of what Che Guevara called new women and men. Thus, economics of the transition period is always framed by socialist political and ethical goals. In fact, a central goal of the transition period is the withering away of the law of value, and with it, the withering away of economics as the science of how a market economy functions as the emerging new society will increasingly rely on conscious planning by the working people themselves through their organizations.

VI. SUMMARY CONCLUSION

30. This brief survey of the economic calculation debate set aside important topical issues and instead focused attention on the broader theoretical and methodological context. Neoclassical and Austrian arguments for the virtues of private property and the market process are not convincing on their own grounds and their critiques of socialist planning are framed on the basis of methodologies presumptions that are questionable. In particular, these theories and their methodologies are not suitable for a socialist examination of the problems of transition from the capitalist mode of production to socialism. Lange and the market socialist response attempted to refute marginalist criticisms on their own grounds. The result was a neoclassical defense of economic planning that breaks fundamentally with the Marxian theory. This type of methodological eclecticism is widespread but usually not acknowledged in the literature on socialism and the market, and socialist planning. Thus, both the standard account of the economic calculation and the recent Austrian reinterpretation mistakenly claim that the Marxian view was presented alongside the neoclassical and Austrian theories. This is far from the truth. In fact, the rise of the modern market socialist theory registers a new strand of reformist literature characterized by substantial theoretical and methodological concessions to marginalist economic theories in particular and bourgeois values and aspirations in general.

31. The historically informed Marxian theory of socialism requires a theory of transition that is distinguished by policies that gradually replace capitalist and pre-capitalist modes of social existence, including monetary and market relations, with self-activity and self-organization of the direct producers. While this essay has outlined the methodological contours of Marxian theory to show how radically it differs from the marginalist and other

pro-market theories, it is important to stress that it has not offered any validation of this theory. Clearly, the critically important theory of the transition period can benefit from considered response to all criticisms and careful assessment of the historical experiences of all post-capitalist societies based on Marx's own methodology. In particular, it is essential to base any such theory on the practical movement of the working people themselves as it is their liberation that the theory purports to facilitate. The final liberation of the working people is task of the working class itself. Still, this review of the economic calculation debate uncovered no theoretical or methodological reason to abandon the Marxian theory that is developed to inform and advance the cause of workers' and socialist movements in their effort to eradicate the exploitive, reified, and alienated human relations based on private property and the market society.

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