Dobb-Lerner Controversy on a Socialist Economy

Sun Whan Rhee*

< Contents >

1. Introduction

Dobb-Lerner controversy seems to have the background that Marx made few remarks about the operational mechanism which his scientific socialism should work on, while he devoted all of his efforts to the criticism of capitalism. As Lerner puts it, economic discussions of socialist problems fit well into the dialectical system of theses, antitheses and synthesis. Since after Marxian socialism appeared, there emerged as antitheses Weber-Hayek-Mises who vehemently stood against the former showing the impossibility of establishing a proper economic calculus under socialism. Naturally, strong repercussions to this view were coming from cadres who had been actually engaged in building a Marxian society.

Between these two extreme theses and antitheses, there appeared such attempts which had been made to bring about a synthesis, as proposed by H.D. Dickinson from capitalist camp. A similar synthesis also appeared from some of Marxian economists, who had held a view that no economic laws operate in a sociaist society and that political economy loses its role as a science with the end of capitalism, and that political economy is a science of capitalism and ends when the capitalist system ends[6]. As

* Professor of Economics, Department of Economics, Hanyang University

the view clearly contradicts the Marxian orthodoxy, O. Lange refutes it. He argues that the basis of the scientific treatment of the political economy of socialism is the assumption that there exist in a socialist society the objective economic laws—different of that of capitalism, and that socialist society is subject, firstly, to the general laws of socialist development which are formulated in the theory of historical materialism, and, secondly, to certain special economic laws. Lange asserts that the experience of existing socialist economies has shown that economic laws do operate within them—e.g., on Lange-Lerner rule.

Socialists, for the first moment, may be interested in such new-found allies like Dickinson coming from the ideological center of the enemy's camp in view that his article devotes to refute Weber-Hayek-Mises, but for the next moment, they may be suspicious and disgusted of him to find that his real theme is to construct a new model of socialism on a competitive price mechanism, seemingly borrowed from capitalist's. To socialists, any attemt to base the socialist economy on a rationally worked-out system of prices and markets may be a subtle scheme of sabotage for building the socialist society on 'rotten' foundations. Meanwhile, they would find a big friend in M. Dobb who ranks with O. Lange in the argument that socialism essentially has its own laws.

This paper is to review the controversy and to put some questions and comments on Dickinson's construction, Dobb's charge on it and on Lerner's view in support of Dickinson against Dobb.

2. Dickinson's Construction of Socialist Economy

First of all, let me introduce a brief summary of Dickinson's model of socialist economy [2].

(1) **Postulates:** It divides the economy into the sector of individualized consumption and the sector of socialized consumption. The model considers only price formation and cost determination in the sector of individualized consumption. For this purpose money is in use. Consumption goods are

sold freely at a price to consumers, and demand of labor input is determined as similarly in capitalistic mechanism, and the organization of production in this sector is in the hands of a hierarchy of autonomous corporations, similar to limited liability companies in a capitalist community. Then, the problem is how, under these conditions, prices would be determined for consumption goods and for production goods.

(2) Pricing of Consumption Goods and of Production Goods: The selling agencies make the construction of price-demand schedules for both of consumption and production goods on the basis of stocks increase and decrease. The managers attempt to keep them at a level that just suffices for current needs; as stocks are exhausted, the managers replenish them by orders sent back to the productive organs of society.

On the basis of the orders sent back by selling agencies the manufacturing organizations draw up demand schedules for their products. And each productive organization can offer a price for the goods that it uses in the process of manufacture. The quantities of factors of production are assumed to be known. Then for each factor the Supreme Economic Council fixes a price which, according to the demand schedule, just ensures its full employment. Now, the costs of production will be calculated on the basis of these figures. For the supply schedule of factors of production, the supply of natural resources is assumed to be fixed, and for labor a wage operation similar to that of capitalistic system is employed. Now, with price-demand function for each consumption good; with technical production function connecting consumption goods with factors of production, either in terms of unit quantity and of price; and with price-supply function for each factor of production, the model could determine unique quantities and prices of a given number of finished goods and of the factors of production that go in use to make them. The system is to be completed by being so modified to include interest and risk allowance for costing similarly as in a capitalist mechanism.

(3) Interest: For the calculus of interest rate two procedures are proposed; In the first case the Supreme Economic Council fixes a certain rate of interest for the specific year and earmarks the corresponding quantity of capital accumulation out of the total social income-the rate of interest to be determined exogenously. In the second case the Council fixes the amount of capital that is to be raised, and then the ruling rate of interest for the current accounting period will be determined-the amount of capital to be saved to become exogenous. In either case the rate of interest, however arrived at, will be used for all accounting purposes like in depreciation and insurance, etc., and the capital will be supplied to undertakings in accordance with their original demand schedules.

(4) **Costing:** Since we have all knowledges which are necessary for cost accounting such as prices of factors of production and a rate of interest (including risk surcharges), a costing system could be set more efficiently in a socialist construction. It could eliminate or reduce the divergence in net marginal products between social and individual. The use of marginal cost is proposed as the pricing criterion. To the sum of costs, as determined in the ordinary way, additions would be made in the case of goods produced under conditions of increasing costs (in the form of a uniform unit tax); from the sum of costs deductions would be made in the case under decreasing costs (in the form of subsidy). The amount collected from the tax on increasing cost industries would go into a Marginal Cost Equalization Fund, and from this fund subsidies would be paid to the decreasing cost industries.[1] The balance of this fund would be added to (or come out of, in case of net deficit) the general income of the community.

Then, he concludes; Thus there is, in theory, no ground for the assertion that a socialist community, lacking a free market, would be unable to regulate production in accordance with the principles of scarcity

---

1) N. Ruggles comments on this point in her article [11] that Dickinson failed to recognize that increasing cost industries would in their own self-interest produce at the proper point. It seems that under the circumstance in which all industries are put under the control of the Supreme Economic Council which can regulate demand of final goods, pricing of factors of production and the rate of interest, etc., such idea of Marginal Cost Equalization Fund may be possible merely for accounting purposes, at least in his construction.

and utility.

(5) **Distribution:** He puts: "It is clear that in a socialist society the return to natural resources, interest on capital and surcharges on risk are mere accounting terms. They would be calculated as described above, but instead of inuring directly to individuals as personal income, they would be paid into a general fund that would be at the disposal of the community as a whole. This fund might be called the Social Fund. (Into it would also go the balance, if any, of the Marginal Cost Equalisation Fund and all surplus of selling price over cost, not otherwise allocated.)"[2)]

For the share of labor, in a socialist system there is no essential connection between the valuation of labor and its wage rate except for accounting purposes. But in the model, for simplicity's sake, Dickinson proposes a similar marginal product valuation principle. Then after two prior charges on the social dividend, i.e., capital accumulation and the cost of socialized consumption (e.g., social services), the whole product of industry could be divided in personal income.

3. Contentions between M. Dobb and A.P. Lerner on Dickinson's Model

Dickinson's article elicits contentions between Maurice Dobb and Aba P. Lerner. Here, I introduce some of major points of the controversy.

(1) Dobb, putting preliminary to the main argument, launches an attack

2) J.W. Conard [1] argues "...I believe this analysis (Schumpeter's) is seriously wrong...unlike Schumpeter, I should argue that the *category* of interest as an accounting item is essential in the plans of a socialist economy...The difference between us arises because of Schumpeter's almost total neglect of time preference in his analysis..." Throughout the last decades of actual experiences of the socialist world, they had neither denied the reasoning of time preference in theory nor neglected in the reality, in fact observed it in costing upon the investment criteria. In connection with Mr. Connard's assertion of "Schumpeter's *almost total* neglect of time preference", It is important to see the point that the reasoning of *explicit* account of interest in costing should not necessarily be led to *explicit* inuring to, say, individuals. As in Dickinson, we see that explicit account of interest could yield an implicit fruit to the society as a whole—in contrast to explicit fruit (interest payment) to individuals. This alone may not give a sufficient answer to the question of "whether the fruit be inured to individuals or to the community as a whole" simply with the reasoning of the existence of time preference.

upon the "alleged" neutrality of economic science. Quoting Robbins; "Economics, as a theory of equilibrium, he points out, is unconcerned with norms and ends; it is concerned solely with constructing patterns for the appropriate adaptation of scarce means to given purposes. The corollaries of economic theory do not depend upon facts of experience or of history, but are implicit in our definition of the subject matter of Economic Science as a whole." Dobb quietly leads to one of his main themes "a maximum of the kind which the 'equilibrium' economist talks." His points are found well in; "...The theory of value, conceived simply as a theory of equilibrium, can postulate that, in a given set of circumstances, prices will conform to a certain pattern; in a different set of circumstances to a different pattern. It can say this, and it can say no more. It may *define* a "maximum" as consisting in one particular "pattern"; but the definition will be entirely arbitrary...i.e., the dilemma of any pure equilibrium theory; it can give no means at all for prefering the "unique" equilibrium of an individualist economy to any of the *n* possible alternative equilibria that a planned economy might choose. Economic theory reduced to these dimensions provides absolutely no criterion of judgement at all [3]." To the Dobb's argument,[3] Lerner's contention would be that unless an economic system achieves (or approach) a max-

3) N. Ruggles [11] notes; "...But his (Dobb's) treatment makes it somewhat difficult to discover exactly what he meant by this statement..." However, I think it will become clear from Dobb's passages [4] : ...But when one speaks of a maximum in economics, the maximum must necessarily be expressed as a quantum of *values*; and economic value is not a simple objective quantity like energy or weight or height or any of the things with which the technician deals. (Under *laissez-faire* conditions, of course, it played the role of such an objective quantity, but it ceases to do so in the degree that these conditions recede.) Mr. Lerner's engineering analogy is beside the point. In economics there will be *n* possible maxima according to the *n* possible price-structures which may prevail. Hence, to discuss the relative appropriateness of alternative price-structures is inevitably implied in any discussion such as that which Messrs. Dickinson and Lerner have raised. It is rather as though in connection with researches into the upper atmosphere Mr. Lerner were to assert the fundamental importance of arriving at a definition of "the top of a mountain" (in terms, for instance, of the slope of the mountain sides); and I were to retort that this was of little use until first one had determined which were the tallest mountains. Mr. Lerner would then presumably charge me with introducing the irrelevant concept of "height".

imum, it will be inefficient; to achieve a maximum, the concept of marginal productivity as a part of definition of a maximum must be employed.

(2) The second point, which I believe to be central shadowing behind Dickinson's construction, originates from Dobb's skepticism upon that, in searching for "maxima", the virtue of "economic democracy" which is conferred on a competitive market rests on the economist's assumption of the 'sacredness' of consumers' preferences. On this point, Lerner's argument would be summarized as; granting that we should discredit the word 'sacredness' by some revealed results of malfunctioning of a free pricing system, but still it is better means 'to give people what they want' than any other authoritarian devices. If we go along Lerner's, Dickinson's construction may have some validity for a socialist economy being ruled by a competitive pricing in searching for "maxima", i.e., a perfect maximum would be achieved by the 'better' ruling scale of priorities, which is set by the automatic determinations of a market. To this, Dobb's retort is somewhat persuasively laborious and vehement; Dobb argues that Lerner's view of the situation is too complex in a sense that he overestimates the complexity of satisfactorily arriving at what people need—implying a possibility of computational capability—and too simple in a sense that he (Lerner) seems to think in terms of simple antithesis between authoritarian and democratic determination, identifing naively the latter with the market system. Dobb says that actually there is a large number of intermediate position between the two extremes. And he gives a very persuasive analogy, "When...doctor prescribes a diet for a patient, is it arbitrary authoritarianism or is it democratic determination of 'what he wants'...?" Dobb adds in saying "Mr. Lerner would agree with me, I think, in saying that under capitalism it is the reverse of democratic and is in a high degree authoritarian. The masses have dangled before their eyes the illusion of free choice—freedom to have what they want *if* they had the money—and are then handed over to the rack devised for them by the advertising agent, the commercial

salesman, and the social conventions of a ruling class. Is not Mr. Lerner rather like one who, engender? In the question of *new* wants, the major part of the initiative, even (probably more) under a market system, must necessarily come from the side of producers, since consumers cannot express a market demand for new commodities until these are made and supplied."[4)]

(3) For the valuation of intermediate products and of factors of production, Dobb's argument is quite sensible when he says that he sees no sufficient necessity for a competitive pricinng system, because precisely consumers are also producers, both "cost" and "needs" are precluded from receiving simultaneous expression in the same system of market valuations, and in the case of this factor of production there should be no competitive market and hence no "automatic" pricing index, and instead its distribution should be determined in terms of a purely accounting valuation. This involves a problem of equal income distribution and of "plural voting" as a consumer.

(4) An important point is raised by Dobb: Another reason that Dickinson's model of a competitive pricing should not be relevant to the socialist economy, in his contention, is that it has a serious limit which affects one fundamental economic relation, i.e., what is the criterion on which capital and labor costing should be based between the production of immediate consumption goods and of capital goods. How cost is determined between the hire of a lathe and of a man's labor?[5)] "...But the question receives no answer from any spontaneous verdict of a free market...

4) This fashion of argument is reinforced by Mrs. J. Robinson [10]. She puts; "... The true moral to be drawn from capitalist experience is that production will never be responsive to consumers' needs as long as the initiatives lie with the producers...No one who has lived in the capitalist world is deceived by the pretence that the market system ensures consumer's sovereignity. It is up to the socialist economies to find some way of giving it reality."

5) Marginal productivity valuation may give a good criterion to weight between lathe's and horse's labor or between Mr. John's and Smith's. In this sense, we may praise it "Good Economics". But economics has clearly gone far beyond its "transcendental" *ethical* proposition of individualist society, i.e., the human dignity, by weighting horse's and man's labor on the same scale of the so-called marginal

Neither is it answered in a capitalist economy. In a capitalist society the two classes of productive agencies are supplied by two distinct social classes; and the pricing property depends upon the level of wages (i.e., the supply-price of labor) relative to productivity, modified by the rate of saving. In a socialist society property will be in the hands of the State, and this fundamental cost-relation will, of necessity, be determined a priori by the decisions of the State as to the proportion of resources to be devoted to the production of consumable goods and of capital goods." And he argues that a free market can and must provide the criterion as to what this relation should be is an illusion, i.e., the illusion that money rate of interest correctly reflects real marginal productivity of capital and that real rate of interest would accompany some optimal rate of saving, and the illusion of "...particularly of the 'necessity' of being ruled by this 'natural' rate in a socialist community." And he claims that in a socialist society there is no excuse for the illusion.

On this point, Lerner acknowledges it, putting that since in any society the rate of interest must reflect the marginal productivity of waiting, but what that will be depends upon the amount of saving and investment, and that Dobb at most could question the optimum-rate-of-saving element, but still the consideration of the actual productivity of waiting is fundamental.

(5) Let me write first a textual definition: For efficient allocation of inputs among various uses, the marginal rate of technical transformation of inputs must be equal among uses at a least cost combination of inputs, which is obtained when the ratio of marginal product (the marginal rate of technical substitution) is equal to input—price ratio. And this is relevant to equilibuium at "maximum." Now, let's consider a different situation. Suppose there were no pricing mechanism, then the principle of least

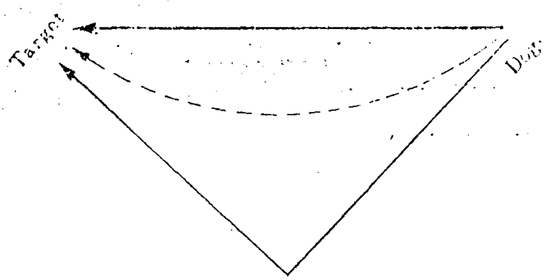
productivity valuation. In this sense, we may term it "Bad Economics". The scale must be different. M. Friedman [5] is comprehensively cautious in saying, "...the marginal productivity analysis of the determination of rates of return to resources does not have any unique ethical implications. Acceptance of this analysis in no way commits one to acceptance of the existing distribution of income as the right or the appropriate distribution—or, for that matter, to its rejection."

cost becomes an engineering matter which is given in terms of input ratio to be equal to the ratio of marginal physical product. If the ratio of marginal physical product of inputs would not be equal among various-uses, we might say it inefficient allocation of inputs or "loss" should occur. This is clearly referring to disequilibrium "not at maximum." Disequilibria are always possible, if time response of factors is not continuously momentary; rather, equilibrium is simply a concept in statics, in dynamics, i.e., in the reality, the relevant situations are always at disequilibria.

But in order to judge ultimately what is efficient still we need to define "maximum." As Dobb mentioned earlier, economic scale which is needed for defing "maximum" should by no means be absolute one, like meter or gram, instead be always relative, and at most, we could say "relative maximum". Making the thing further difficult and complicated is the involvement of time rate—the rate of interest. However, up to this point, one could say that violating the earlier mentioned textual definition might not necessarily be led to be labeled as "inefficient." Dobb's rather seems to imply an emphasis on dynamics.

(6) Dobb safeguards why a socialist State should observe, not one equality of net marginal yield, but an alternative rule as the principle of capital investment. He points that this is mainly related with the fact of obsolescence and of uncertainties arising from technical innovation. And he gives some fanciful illustrations of which I introduce one as "dog's pursuit curve" graphically. Dog runs always toward its master, with the result that his path in pursuit of his master is a curve. A planned economy should,he puts, take a similar straight line toward a technical level of the future.

(7) Dobb concludes that planned economy will have its economic laws, as has laissez-faire economy; it will have its economic accounting and its calculus.



4. A Concluding Remark

Throughout the whole series of the controversy between Dobb and Lerner, my general impression is that Dobb's neat and vehement arguments which seem to be met by somewhat weakly directed Lerner's contention might lead to the implication of the superiority of socialist price mechanism. In the experience of last decades in theory and in actual practice, there is some variety of technical economic principles both economists—capitalist and socialist—face commonly, apart from his own ethical and ideological propositions. The focus point is whether or not the principle of a competitive pricing could be conceived as the technical matter. So hot the contention, since it is thought so critical even to affect his own paramount ethical and ideological propositions.

There are a few points I would like to consider: (i) Firstly, if the system for a shadow price as a socialist calculus has, mathematically, the "unique" optimal solution, this is clearly contrasting to its counterpart—a competitive market price. The point is that, in dynamics, i.e., in the reality, it has no unique solution, which implies the indeterminacy of the solution of the general equilibrium price. "Indeterminacy" in mathematics may be interpreted in the real world as relevant to "relative situation." (ii) Secondly, presumably more important, *under some conditions,* a competitive market price could give a "better" approximation to the probable dynamic trial-and-error solution of the equilibrium price. (iii) Thirdly, to put aside the proof of whether or not a competitive pricing is more efficient for 'giving the people what they want' than any other authoritarian devices; suppose it is so, there should not any ideological difficulty be involved in hiring it except for a psychological hostility, e.g., 'rotten capitalist device.'

《References》

(1) J.W. Conard: *Introducion to the Theory of Interest*, Berkeley 1959, pp. 106~7.

(2) H.D. Dickinson: "Price Formation in a Socialist Community," *Economic Journal*, Vol. XLIII (1933), pp. 237~50.

(3) M. Dobb: "The Problem of a Socialist Economy," *Economic Journal*, Vol. XLIII (1933), pp. 588~98.

(4) ________ "Economic Theory and Socialist Economy: A Reply," *Review of Economic Studies*, Vol. Ⅱ (1934—35), pp. 144~51.

(5) M. Friedman: *Price Theory*, Chicago 1967, pp. 196~98.

(6) O. Lange: "Problems of Political Economy of Socialism," People's Publishing House 1962, pp. 1~15.

(7) A.P. Lerner; "Economic Theory and Socialist Economy," *Review of Economic Studies*, Vol. Ⅱ (1934—35), pp. 51~61.

(8) ________ "A Reply to Mr. Dobb," *Review of Economic Studies*, Vol. Ⅱ (1934—35), pp. 152~54.

(9) Sun Whan Rhee: "Dobb-Lerner Controversy on a Socialist Economy," Mimeographed Paper, Department of Economics, Duke University, January 1968.

(10) J. Robinson: "Consumer's Sovereignty in a Planned Economy," *On Political Economy and Econometrics Essays in honour of Oscar Lange*, Perggamon Press 1965, pp. 513~21.

(11) N. Ruggles: "The Welfare Basis of the Marginal Cost Pricing Principle," *Review of Economic Studies*, 1949—50, pp. 29~46.