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## POSSIBLE LEVELS OF CENTRAL PLANNING

The aim of the paper is to discuss some limitations of planning in the area of economic activity. To achieve the goal we analyze the notion of planning and some of arguments for and against central planning. Most of the ideas of the paper are inspired by the essay of G. Warren Nutter – “Central Economic Planning: the Visible Hand”<sup>1</sup>.

### Free market *versus* central planning

Free market economy is commonly seen as the system of spontaneous order in which autonomous selfish actions of individuals constitute a socially accepted result. As Adam Smith wrote in his “The Wealth of Nations”

By pursuing his own interest [an individual] frequently promotes that of the society more effectually than when he really intends to promote it<sup>2</sup>.

On the other hand, at least from the beginning of the 20th century the idea of rational improving of this spontaneous order has been a permanent feature of our social thinking. As G. Warren Nutter recites:

And so planning has been advocated to increase economic efficiency, reduce unemployment, control inflation, moderate the business cycle, distribute income more justly, make the economy grow faster, make it grow slower, prevent discrimination, eliminate pollution, improve the quality of life, and so on. In other words, planning is frequently hailed as a cure for whatever seems to be the economic ailment of the moment<sup>3</sup>.

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<sup>1</sup> G. Warren Nutter, “Central Economic Planning: the Visible Hand” in: G. Warren Nutter, “Political Economy and Freedom. A Collection of Essays”, Liberty Press, Indianapolis 1983, pp. 107-129.

<sup>2</sup> G. Warren Nutter, op. cit., p. 113.

<sup>3</sup> G. Warren Nutter, op. cit., p. 113.

In the following two paragraphs we examine whether the above opposition – free market versus central planning – is entirely correct.

### Planning – a reconstruction of the notion

In our discussion we assume that the notion of planning involves four elements – a starting point, a final point, a set of rules of transformation, a time of transformation. Having this assumption, we define a plan as the idea of **how to achieve a goal** (which is a **future situation**), from a **present situation** in a **given time** using only **rules** from a **given set** of possible (or accepted) rules of transformation.

We can symbolize the above in the following way:

$$S_m = F_m(S_n, R_1, R_2, \dots, R_k, T_w),$$

where

$S_m, S_n$  are respectively a final point and a starting point ( $S_m, S_n$  belong to a given set of possible situations),

$R_1, R_2, \dots, R_k$  are rules of transformation ( $R_1, R_2, \dots, R_k$  belong to a given set of accepted rules of transformation),

$T_w$  is a time given for the transformation ( $T_w$  belongs to the set of time periods)

and

$F_m$  is a plan of transforming  $S_n$  into  $S_m$  in a time  $T_w$  by the proper use of the rules  $R_1, R_2, \dots, R_k$  ( $F_m$  belongs to the set  $\mathbf{F}$  of all possible arrangements of given rules of transformation).

The set of all possible situations achievable from a given starting point in a given time by the use of the rules of a given set of rules of transformation is **the range of possible planning** connected with given starting circumstances. In symbols:

$$RPP(S_n, R_1, R_2, \dots, R_k, T_w) = \{S_x : S_x = F_x(S_n, R_1, R_2, \dots, R_k, T_w)\},$$

where  $x$  is a variable.

It is obvious that it is not possible to achieve any final point we like having defined a starting point, a set of rules of transformation and a time for transformation (if the “power” of rules is limited and the given time is limited). However, it may be questioned whether every two sets of rules of transformation determine different sets of final points having defined a starting point and a time for transformation. In symbols:

$$\{R_1, R_2, \dots, R_k\} \neq \{P_1, P_2, \dots, P_k\} \rightarrow \\ \rightarrow RPP(S_n, R_1, R_2, \dots, R_k, T_w) \neq RPP(S_n, P_1, P_2, \dots, P_k, T_w).$$

In terms of our discussion it is the problem whether free market rules and central planning rules can lead us to the same results in the same time from the same starting point.

## **Levels of central planning**

Having the above definition of planning and assuming that central planning is the planning performed by the government, we see that the opposition free market *versus* central planning is not entirely correct. Every government plans at least at the areas of tax policy, monetary policy and government expenses policy (i.e. expenses connected with financing the army, the police, the government itself etc.). In fact, we haven't got just two opposite models: free market or central planning. It is better to talk about a spectrum of levels of central planning – with the minimal central planning on the one side of the spectrum (centrally planned: tax policy, monetary policy, expenses on the army and the police), through various kinds of soft central planning (centrally planned: as above plus expenses on social policy) and various kinds of medium central planning (centrally planned: as above plus a system of governmental indirect impact on economic decision of individuals; such system is a system of certain legal regulations: progressive taxation, tax reductions, licensing regulations for certain economic activities) and with several systems of strong central planning on the opposite side of the spectrum. The systems of strong central planning are based on the principle of direct governmental impact on every particular activity. One of these (strong) levels is exemplified by the system of central planning commonly imputed to the command economy of the Soviet Union:

For example, one commonly held view portrays Soviet economic programs as a set of boxes within boxes. According to this view, the first box to be built is the one corresponding to the five-year plan, and even this one is said to have its general contours determined by a long-range plan, covering fifteen to twenty years. Once the five-year box is constructed, the next step is to fit successively smaller boxes inside it, each applying to a successively smaller time period. Thus, the schedules of day-to-day activity contained in quarterly and monthly plans are visualized as mere miniatures of the grandest scheme of all<sup>4</sup>.

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<sup>4</sup> G. Warren Nutter, op. cit., p. 111.

So, free market economy is also a subject of central planning. However, the central planning of free market economy is never based on methods of direct governmental impact on every particular activity<sup>5</sup>.

That is why we tell that the opposition free market *versus* central planning is not entirely correct. The correct question is as follows: which level of central planning is the best from the point of view of economic progress? And in particular: can any system of strong central planning be more effective than free market economy?

### **Some arguments for the idea of strong central planning**

The issue of the optimal scope of central planning has been discussed for centuries and some of the most important arguments for and against the idea of strong central planning were put forward more than two hundred years ago within the discussion on the mercantile system then dominating Europe:

Mercantilism was, of course, nothing more than the economic side of the authoritarian state. It was common for government to regulate all kinds of economic activity: to fix prices, wages, and interest rates; to prohibit speculative trading; to specify the quality of goods; to license labor; to prescribe what people should and could consume; to create monopoly rights for favored proprietors; to control chartering of corporations; to foster state enterprises; to control foreign trade; and so on. The American colonies revolted against this excessive governmental meddling in economic life as much as anything else<sup>6</sup>.

Nevertheless the issue was not solved at that time and several economic systems with at least elements of strong central planning have been carried into effect since then. Among countries which have had the experiences of this kind we can recite not only the Soviet Union and countries of the so-called former “Soviet camp” but also such countries as France, Norway, the Netherlands, Sweden, Japan, the United Kingdom, Korea, Taiwan and India<sup>7</sup>. Also in the United States the issue of instituting central economic planning was discussed in 1970s<sup>8</sup>.

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<sup>5</sup> Free market system can be well defined as the system of economy based on two principles: the principle of private property and the principle of liberty of economic activity.

<sup>6</sup> G. Warren Nutter, “Strangulation by Regulation” in: G. Warren Nutter, “Political Economy and Freedom. A Collection of Essays”, Liberty Press, Indianapolis 1983, p. 87.

<sup>7</sup> G. Warren Nutter, *op. cit.*, p. 114.

<sup>8</sup> G. Warren Nutter, *op. cit.*, p. 107.

In my opinion, among all arguments for the strong central planning there are two which are the most important.

The first argument is that the interest of no individual is the same that the interest of the society as a whole. So, the society needs to regulate all kinds of economic activity to secure the interest of the society as a whole and to prevent the society from being hurt by selfish actions of individuals.

The second argument is that no individual has the full knowledge about the economic environment. In particular, no individual has the full knowledge about the economic plans of the others. That is why no individual can prepare a completely rational plan for her economic actions. So, the government should help individuals in their economic activity by establishing central plans of economic actions. As Vera Lutz wrote in her “Central Planning”:

Collective forecasting (...) is supposed to make a twofold contribution to the solution of this problem. The first is that of rendering the economy “transparent”, by gathering together and making generally available the knowledge, beliefs and intentions (often referred to for short as “information”) of the individual economic agents regarding future developments in their respective sectors. The second is that of making economic activity “coherent”, by welding the individual forecasts and plans into a consistent whole, corresponding to a “common view of future economic development”<sup>9</sup>.

### **Some arguments against the idea of strong central planning**

Among the arguments against strong central planning which were raised upon last two centuries the following arguments are, in my opinion, the most important.

The first: it is not only a peculiarity of individuals to make errors in plans of economic actions, the governmental central plan also can be wrong and the consequences of such situation are rather unpleasant:

That is, the likely mistake inherent in a centralized forecast will have a more harmful impact on the economy than the variety of mistakes distributed among individual forecasts, since the very spread in the latter, involving overlapping margins of error, generates differential market adjustments that diminish average forecasting error over time<sup>10</sup>.

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<sup>9</sup> G. Warren Nutter, *op. cit.*, p. 117.

<sup>10</sup> G. Warren Nutter, *op. cit.*, p. 119.

The second: since the interest of no individual is the same as the interest of the society as a whole, any central plan is merely a resultant of interests of various individuals and groups involved in preparation of the plan.

The third: the plan itself may carry into effect the unwelcome situations it predicts. So, to avoid such unwelcome situations the responsible government should probably – if necessary – forge the plan. It was the case of the Fourth Plan in France:

(...) the Fourth Plan took no account of repatriation from Algeria because, as the commissioner of planning explained, “it was impossible to build a Plan on such a disagreeable eventuality. The government might have been reproached for having precipitated the event by announcing it”<sup>11</sup>.

The fourth: the process of preparation and monitoring of any central plan costs a lot. So, if superiority of strong central planning over softer forms of central planning is not proved, it is not reasonable to spend money on strong central planning. In other words, softer forms of central planning are much cheaper.

### **Inventiveness – the strongest argument against the idea of strong central planning**

Recently one more argument against the idea of strong central planning is raised and, in my opinion, it is the strongest argument: the idea of strong central planning cannot be reconciled with the idea of inventiveness. Any invention is always a product of creative thinking and so it is always unforeseeable. If our social activity cannot be foreseen it cannot be also the subject of effective strong central planning.

In the terms introduced above, we say that – thanks to the inventiveness of the mankind – the set of possible (acceptable) rules of transformation continuously grows larger. So, even if the starting point of a plan could be described as precisely as we want, it is not possible to make an effective plan since the set of rules of transformation is not constant. Every new invented rule changes **the range of possible planning** connected with given starting circumstances.

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<sup>11</sup> G. Warren Nutter, op. cit., p. 120-121.

*Possible levels of central planning*

Moreover, the greater invention is made, the more important changes in the range of possible planning it involves.

However, it is obvious that central planning of a certain – lower than strong central planning – level is inevitable in the economic activity of the mankind.