

BOOK REVIEW: NIKOLA NJEGOVAN (2022) FRIEDMAN'S CHALLENGE

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ABSTRACT

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I

The initiators of the “marginalist revolution”, Jevons, Menger and Walras, had no idea how much intellectual energy their ideas would trigger in the decades and centuries to come and what implications they would leave for the development of economic theory and methodology. From their time, it was unforeseeable that the “golden age of economic theory” of the 40s and 50s of the twentieth century would follow, as evidenced by the “marginalist controversy” and [Friedman's \(1953\)](#) “*The methodology of positive economics*”. The “golden age of economic theory” enabled the emergence of Samuelson's “neoclassical synthesis” and the constitution of modern microeconomic theory. It was even less predictable that the history, methodological controversies, and literature related to the “marginalist revolution”, “marginalist controversy”, “Methodology of positive economics”, and “neoclassical synthesis” would arouse so much interest at the Faculty of Economics in Belgrade. It is worth reminding that the professors at this Faculty have written significant works dedicated to topics whose comprehensiveness, method of analysis and attitudes do not lag behind the level of similar papers at other universities in the world. These papers undoubtedly include “Contemporary bourgeois theories of value and prices” by [Zoran Pjanić \(1965\)](#), “Austrian theory of capital” by [Milić Milovanović \(1986\)](#), “Fundamentals of Austrian theory” by [Božo Stojanović \(2008, 2021\)](#), and we hope that the list will soon include “Friedman's Challenge” by Nikola Njegovan, which was recently published by the Publishing Centre of the Faculty of Economics, Belgrade.

Dr Nikola Njegovan's book is evaluated by the public at a time when economic science, as well as economics as a whole, is in a long-term serious crisis. Empiricism and normativism, supported by the rapid growth of corporate profits in the conditions of accelerated globalization, relegated methodological research of economic theories to the background, often reducing economic science to the mere verification of the properties of a certain phenomenon by applying a suitable mathematical model. Empiricism has gone to such proportions that today, even in academic circles, we talk about the "visual economy", "digital economy", "green economy", etc. In modern times the voice of marketing agencies and the sector of large companies are heard more than the voice of economic science. Fortunately, in the time of the "marginalist revolution" and "marginalist controversy", there was no such approach in economic science. Otherwise, we would have had "steam economy", "diesel economy", "electric economy", etc. Normativism has reduced the objective importance of economic science around the world, and often, through various international agreements and directives, it has imposed itself as a set of desirable features of the economy, so that, in such a system, economic science aims to prove that these features are actually realized. Bearing in mind such tendencies and not forgetting [Hammond's remark \(1992\)](#) that economic theory and methodology live separate lives, the idea of Nikola Njegovan to seriously engage in the analysis of one of the most significant works in the field of positive economics methodology seems quite logical. He thereby calls for strengthening the objective side of economic science and the need to determine its relationship to empiricism and normative economics.

II

Although aware of the fact that the choice of the book's title, "Friedman's Challenge," may cause associations among some readers that it deals with monetary problems or issues of the price system weakness at the time of the Great Depression, the author consciously opted for it precisely because the subject of analysis in this book "represents a challenge to arguments about the necessity of building theories on realistic assumptions" (p. xii). In Friedman's works, one can find several places that represent a real challenge to everything that has been said about the given topic in economic science, so the author's decision to give the book a chosen title is quite justified because Friedman's "*Methodology of positive economics*" in the real sense, is a challenge to the "marginalist controversy" and the theory of monopolistic competition. At first glance, the book has an unusual content, as its first part is a translation (a good translation!) of the original version of Friedman's work into Serbian, followed by three more parts containing

an overview of different interpretations of Friedman's views, the historical context from the aspect of the marginalist controversy and Chamberlin's theory of monopolistic competition, and a summary of his own views and findings of the analysis. However, when one approaches a more detailed reading, one comes to the conclusion that the author organized the structure of the book very functionally, enabling the reader to follow the views of different authors and schools of thought regarding the topics that Friedman offers as a challenge in the methodology of economic science. The author believes "that the translation of Friedman's text at the beginning of the book, as well as the discussions that follow, will be useful to students and economists who want to delve deeper into this topic, but also to those who just want to gain an insight into the work that should be an essential reading for anyone interested in not only economics but science in general" (p. xiii).

With a rich selection of literature (161 references), which includes almost all important works of a significant epoch in the development of economic science, the author tried to build his own view on the subject of analysis but also to show the circumstances and the way the modern microeconomic theory is constituted. Using a variation of Emmett's "historical reconstruction" principle, the author performs a reconstruction of Friedman's work, but also that of other authors who participated in the great debates of the time – the marginalist controversy and the theory of monopolistic competition. The author starts from Friedman's position that the validity of economic theory should not be judged solely on its tautological completeness, which is not unimportant, but rests primarily on the possibility and simplicity of prediction, at least as much as the alternative theory but with less information, and based on efficiency, comprehensiveness and accuracy of forecasting and encouraging new research. Thus, in a methodological sense, the author engages in the analysis of extensive literature and different attitudes that are inspired either by the acceptance or rejection of Friedman's opinion about the impossibility of testing a theory by the realism of its assumptions (p. 31. and 36.). Friedman himself defined the methodological framework in which the entire analysis takes place, with the opinion that the realism of the underlying assumptions is not important for the evaluation of the theory but the quality of its predictions. A hypothesis is only an instrument of prediction, and as such, it can never be proven. Numerous comparisons of the predictions that follow from the hypothesis with experience provide the basis for accepting or rejecting the hypothesis (p. 85). Predictions based on a hypothesis that are not disconfirmed by experience give the possibility of tentatively accepting the hypothesis. In general, the author accepts the point of view that economic theories should be accepted if they result in good predictions (Caldwell, 1980,

1992), not based on the belief that they are correct, and that they should be rejected if they give bad predictions, not if we believe they are incorrect (p. 94). A number of economists reproached Friedman for including falsehoods in his theory because he advocates explaining only phenomena of special interest for forecasting. Samuelson called this the F-Twist, a warning that such an approach could lead to an unscientific selection of results (Samuelson, 1963, "Problems of Methodology: Discussion"). By losing the ability to predict, the theory's validity decreases, so the Friedman's conclusion that "every theory is of a temporary character" (p. 53-54) becomes a logical outcome of the author's chosen methodological approach to analysis. Accordingly, the author's dealing with the "*Methodology of positive economics*" is not only a review of the great debates about the fundamental problems of microeconomics or a presentation of the historical emergence of modern microeconomics, but at the same time, it is a way of building one's own methodological approach to the analysis of economic phenomena. Building one's own methodological approach on the literature of the "golden age of economic science" represents a difficult but dignified path of development of a serious researcher.

III

The marginalist controversy from the 40s of the last century occupied a special place in the analysis conducted by the author in the book "Friedman's Challenge". Although in the Chicago school, there are differences in the assessment of Friedman's work, starting from his acceptance as a manifesto of the Chicago school, supported by the majority of followers of this school, to individual opinions (Ronald Coase and James M. Buchanan) that the validity of economic theory lies in its intuitive appeal, and not in the alignment of its predictions and empirical features, as stated by Melvin Reder (1987), most economists accept that Friedman's work played a crucial role in resolving the marginalist controversy and strongly encouraged the development of modern microeconomic theory. The author of "Friedman's challenge" tries to bring to the public, the methodological side of solving controversial situations in one of the crucial periods of the development of economic thought, from today's time when a lot of literature on Friedman's methodological challenge has been accumulated. Perhaps this is a hint that the development of contemporary economic thought, when empiricism and normativism reach global proportions, needs a new methodological challenge such as Friedman gave in his time!?

The author sees Friedman as a marginalist who defends Marshall's approach and who is aware that it would be "extremely desirable to have a more general

theory than Marshall's" (p. 50). Thus, Friedman wants a more general theory but is firm in the opinion that the marginalist controversy and the theory of monopolistic competition do not offer such a theory. The enthusiasm with which the author of "Friedman's Challenge" performs the analysis of literature and positions, starting from Lester to Samuelson, shows that he is driven by the desire to enter into the smallest details of the arguments "for" and "against" in the discussions regarding the marginalist controversy. Such an approach shows that he tries to master the essence of Friedman's views, but it is, at the same time, the best way to master the essence of economic theory, which the author proved through the interpretation of the implications of the marginalist controversy. He observes that the marginalist controversy has a much broader context in terms of a more consistent constitution of the theory of prices and the theory of the firm and concludes that it came as a kind of attack on marginalism and ended up strengthening it and that Friedman's *Positive Economics* is a strong response to the tendency to replace the theory with history (p. 135). Therein lies the full justification of "Friedman's challenge" because the author's reconstruction of the methods of defence of orthodox economic thought showed that this process contributed to its development.

Analysing the extensive literature created on the occasion of the debate on the validity of Chamberlin's theory of monopolistic competition, the author tries to provide answers to two questions: 1. Why does Friedman talk about the unrealism of the theory of monopolistic competition if it is unimportant? 2. Does he defend the Marshallian theory or attack monopolistic competition in this way? (p. 176). Asking such questions makes sense, especially because the author places Friedman's work in a broader context of the development of economic thought and its methodology. Relying on the views expressed in the debate by Archibald, Friedman and Stigler, he observes that *The Methodology of Positive Economics* gives two possible interpretations of the unrealistic assumptions: (1) irrelevance and (2) unreality as a virtue, with the first interpretation referring to the marginalist controversy, and the second to the critique of monopolistic competition (p. 177-178). The author observes that Friedman does not favour predictions based on the theory of perfect competition, nor does he criticize the assumptions of the theory of monopolistic competition, but starts from the assumption that monopolistic competition, as an alternative theory, is based on the idea of using realistic assumptions, in which he sees the virtue of unreality of assumptions (p. 178). Such an approach is an authentic example of the application of Friedman's methodological views on the constitution of a consistent theory. After presenting Friedman's debate with Archibald (1961, 1963) and Mäki (2009), the author concludes that we are not interested in how

business people actually behave and what the real elasticity of the demand curve that the company is facing is (p. 179). The principle of “as if” maximization in the behaviour of business people and the justification of using a horizontal demand curve, i.e. the principle of “as if” perfect competition, will be supported by predictions (p. 179). The use of a horizontal or downward-sloping demand curve is not a matter of choice because the number of substitutes determines the elasticity of the demand curve (Kaldor, 1938). The author, looking at all the pros and cons of Chamberlin’s theory, concludes in line with Mises (1998) that what Chamberlin (1933, 1966) talks about “just describes the competitive process so that monopolistic competition represents a mythology” (p. 171). The author does not want to place himself in the position of an arbiter between opposing views, and it could be concluded that he is close to Williamson’s opinion “that restoring confidence in the validity of neoclassical theory was high among Friedman’s goals” (p. 182). Through “Friedman’s challenge”, he tries to single out and analytically present the important positions that contributed to the constitution of the modern microeconomic theory. This is to be expected from the author who, almost at the beginning of his career, tries to draw attention to the key principle in science, according to which there are no good results without good methodology. The author clearly observes that Friedman’s views should be interpreted in the light of his answers to the prevailing questions of the time when the basis for *The Methodology of Positive Economics* was created. At the same time, the author bears in mind Emmet’s reminder of the possibility of a subjective measure of scientific value, that is subjectively assigning importance to a text and avoiding exclusivity in the analysis and assessment of opposing views. He does not enter polemics with opposing views of the authors he cites and mainly observes them in the relationship which the authors have set and thus reconstructs the debate.

IV

The book by Nikola Njegovan, PhD, entitled “Friedman’s Challenge” brings a complex view of the general methodology of positive economics, the marginalist controversy and the theory of monopolistic competition, synthesizing different views on the debates that marked the development of economic thought during the “golden age of economic science”. At the time when the author decided to write this book, all the positions it talks about were already known in the literature. However, this did not sway the author to engage in the analysis of details and comparison of views, creating a new perspective, brighter and more extensive, on the most significant period in the development of microeconomic theory. The great value of this book is that it shows that economic theories with no

methodological foundation are unsustainable. The author showed that Friedman interprets the theory's validity through the ability to predict. However, in the end, referring to Sen, Last, Quirk (1986) and Gonzalez, he concludes that it would be a big “mistake to think that only predictions can represent the central issue of economic science”, as well as that “science cannot be based exclusively on prediction and that the enterprise of searching for truth should not be abandoned” (pp. 188-9). Furthermore, the author did not miss the views of Mäki (2009), Hirsch and De Marchio (1984, 1990), according to which we cannot claim “that Friedman in his dealings with economics was consistent with the views expressed in the Methodology of Positive Economics” (p. 187). Although the book was created as a kind of “return to the past”, i.e. by refreshing and reconstructing ideas, it represents an extensively documented study on the methodology of positive economics and its application in defence of the positions of orthodox economic science. In the true sense, it represents a scientific monograph that our scientific public needs, especially in the conditions of the invasion of empiricism and normativism. The book will be useful to doctoral students in economics, postgraduate students, methodologists and scientific workers in the field of economics. It is written in a simple and comprehensible style, so it is also acceptable for those who do not have a high degree in economics.

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**ПРИКАЗ КЊИГЕ: НИКОЛА ЊЕГОВАН (2022)
ФРИДМАНОВ ИЗАЗОВ**

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САЖЕТАК

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