Vienna and Chicago: Friends or Foes? A Tale of Two Schools of Free Market Economics. By Mark Skousen. Washington, D.C.: Capital Press, 2005.

Mark Skousen has written a book that is designed to entertain as well as to inform. Though he succeeds partially in both of these two goals he is more successful in the first. The book is not deeply informative, it does not break any new conceptual ground or provide the reader with a thorough and reliable understanding of the relationship between these two schools of thought. Yet it is somewhat entertaining and contains some interesting ways of looking at things. The book also benefits from Skousen's energy as an interviewer of "big names" including Milton Friedman and Friederich Hayek from whom he is able to quote relying on personal communication. But it is not a book to which one can go to find a credible and insightful understanding of the issues involved in this episode in the history of economic thought. Skousen shortchanges both schools. His fails to convey the very real diversity within both the Chicago and the Austrian Schools, and what it is that really separates the schools in spite of their inner diversity—that is, how the differences between the schools dwarf the differences within them. This failure is mainly due to his misunderstanding of, and hence mischaracterization of, the methodological differences between the two schools of thought (chap. 4).

After a short introductory chapter presenting the commonalities and the issues involved, Skousen presents the essential features of the Austrian and Chicago schools of thought (chaps. 2 and 3) and then grades these two market-oriented schools on their treatments of four key issues (chap.s 4 through 7). He concludes each of the key-issue chapters with a summary scoring in the form of "Advantage: Vienna" or "Advantage: Chicago." He ends up with a 2-2 tie. Vienna scores higher on macroeconomics and monopoly theory; Chicago scores higher on methodology and money. As I will argue below, to award Chicago the advantage on methodology reveals a real problem in his understanding and hence assessment of the issues involved. The final quarter of the book deals with the two schools' alternative assessments of the Great Economists (chap. 8), arrays these two schools and two others (the Marxists and the Keynesians) along a spectrum ranging from "no faith" to "complete faith" in the market system (chap. 9), and discusses the future of free-market economics (chap. 10).

Before turning to the methodological question, some comments about the intended audience and the style of the book are in order. It is not clear for whom this book is written. For those who already know something, or a lot, about the subject, the book may be entertaining but also somewhat disconcerting. Skousen's style is breezy and colloquial, aiming often to be humorous, sometimes succeeding. But the level of scholarship is very spotty. Sometimes the treatment is very superficial, sometimes it is inaccurate ("Menger stressed the utility or *maximum benefit enjoyed by each individual* according to the value and utility of goods and services produced and consumed" p. 26; italics added); and sometimes it is wrong (for example in failing to distinguish between value and price—or marginal valuation, "[Menger] showed that the *value* of goods is determined by their *marginal* utility rather than by their *total* utility" (p. 28; italics added)—one knows what he means, but such an important point ought to be written clearly.

For those who know little or nothing about the subject the book is likely to be informative but also to be a source of misinformation, particularly for those who know something about one school and are seeking enlightenment on the other. So Chicagoans seeking knowledge about the Austrians will get a lot of useful information about the history of the Austrian School and its development, but nothing about the subtleties of its investigative method or misgivings toward the mainstream way of doing things. In particular the Chicagoan is likely to come away from the book having his prejudices about the Austrian School as being "scientifically soft" reinforced. On the other hand, the Austrian seeking guidance into the Chicago School is also likely to get a lot of useful historical information, but to have his prejudice of the Chicago School as a bunch of naïve, technically proficient, philistines reinforced. Neither view is, of course, the truth. Given that few Chicago-types, or any "mainstream"-types are likely to read this book, I imagine that it will be mostly Austrians (and other heterodox-types) who will read it, and they are unlikely to really learn much about the subtleties of the Chicago-method from it.

According to Skousen, the Austrians are guilty of ignoring empirical evidence (which he equates with history), doing very little if any empirical studies, and focusing exclusively on theoretical and exegetical exercises. On the other hand, the Chicagoans have a healthy scientific respect for "the facts" and have produced multiple studies that pay rigorous attention to them—most notably in the field of monetary policy (the age of the Monetarists).

There is perhaps an element of truth in this. Up until recently the "modern" Austrian School did very little by way of "empirical" work and spent most of its time attacking non-Austrians for what they did. This is not a strategy designed to win friends and influence people.[1] But the explanation for this lack, it seems, lies in the time it has taken to develop a new generation or two of young scholars ready to move beyond the reassertion of resuscitated Austrian ideas and methods to the performance of a slew of new studies hot off the press. These new studies apply Austrian methods to current and historical situations.[2] Very little of this work is mentioned by Skousen.

In fact, the problem is much deeper. Skousen is correct to think that historical studies are empirical. But he is naïve in thinking that what Chicago is doing with its "empirical studies" is history. He has it exactly the wrong way round. It is Chicago that is ignoring history and the Austrians who emphasize the perils of doing so. The

[1]This is of course notably not true of the elder statesmen like Mises and Rothbard whose work contained a lot of history.

[2]For example, see works by Baulier, Boettke 2001, Chamlee-Wright, Coyne, Leeson, Powell, Stringham, Whitman, and many others—see the references for some links to their recent publications.

Chicago approach is, in a word, "scientistic." It is an attempt to be like the hard-sciences by mimicking their methods. This involves reducing history to numbers, and only numbers, and then massaging those numbers in ever more complex, clever statistical models. The debate between these schools is *not* about the importance of using evidence—it is about what *constitutes* evidence and what constitutes a "test." Chicago emphasizes "thin" stories which summarize the complexity of historical situations into quantitative representations that can be manipulated. The worse the data the more complex the statistical methods and the less believable its results. For example, many of the magnitudes manipulated refer to unobservable entities, like expectations or other attitudes. These are understood as latent-variables and are measured "indirectly" using structural-equations models with proxies or "instruments" standing-in for the unobservables. It is true that the econometrics that Friedman and Schwartz did in investigating monetary history was much more straightforward than this, but this is not the whole story of Chicago, particularly of the microeconomic empirics.

The Austrians for their part have never ignored history when doing positive, as opposed to critical analysis. Even Mises's *a-priori* approach, simplified distortions to the contrary notwithstanding, should never be understood as downgrading historical analysis. He is clear that history needs interpretation for which *a-priori* economic laws must be used. In contrast to Chicago, Austrian accounts are "thick" stories, that do not eschew the use of numbers where considered helpful, but that, most importantly, attempt to capture as much of the complexity of the historical (or current) situation as possible by including an account of social institutions and their roles. Skousen shows little appreciation of the Austrian understanding of the role of institutions in the work of Hayek, Mises, and others. He totally ignores the seminal contributions of Ludwig Lachmann (whom he dismisses in one page) and of Don Lavoie (who is not mentioned). The judgment "Advantage Chicago" is at the very least highly premature, and a good argument can be made that it is quite mistaken.

According to this latter way of thinking it is not the sophistication of its empirical methodology that is responsible for the richness of the Chicago School's contribution to economics. Rather it is the school's penchant for imaginative theoretical insights, using the equilibrium-method, that is responsible for this.[3] The equilibrium-method consists in understanding equilibrium to mean individual constrained-maximization, which really means purposeful action. The economic models take basic economic situations and manipulate logical (mathematical) symbols, representing aspects of those situations, like attitudes, costs, benefits, etc., to wring-out hard-to-come-by, but important, economic intuitions that often explain observed phenomena in new and insightful ways. That is the genius of this productive period in the history of the Chicago School. One has to look past the method, which is both a way of thinking and a way of gaining "scientific" respectability, to see the richness of the insights. This richness is a result of the "Chicago-method"[4] of applying basic Marshallian price

[3]For example, the economics of the family, the economics of crime and punishment, human capital, discrimination, religion—I am thinking in particular of the pioneering work of Gary Becker and his collaborators; see Skousen's book pages 87–89, and the references he cites, for a brief survey of "Gary Becker and Socio- Economics."

[4]Shared at the time by UCLA, Rochester, and other "Chicago-farms."

theory in a flexible and imaginative way. It is perhaps this which many of the Austrian-inclined fail to see. So Skousen gets it wrong on both sides of the fence.

Finally, it should be noted that this is now an old fight. In an important sense neither school is still with us. The Austrians are still here, in small numbers, and have developed a new and productive research program—largely ignored by Skousen. They no longer spend much time fighting this kind of battle. They are trying to get on with the job of doing the research. The Chicago school that Skousen describes is even more illusive. It is a fairly accurate representation of an episode in Chicago history—the age of Monetarism and of "Chicago Imperialism" in price theory. But those days are long gone. In many ways, unfortunately for both schools, Chicago seems to have lost the battle to MIT and Harvard and their focus on mathematical virtuosity in a general-equilibrium setting. The so-called adherence to empirical standards is often honored in the breech and is considered *passé*. Many of the Chicago-Austrian ideas have passed instead into other fields like that of business-strategy and management.

In the final analysis, *Vienna and Chicago* is a mildly entertaining, but superficial and sometimes inaccurate, account of an historical episode, one that was never really important to anyone but the Austrians and one in which interest is rapidly fading.

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