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Controversy: Are Antitrust Laws Immoral? A Response to Kenneth G. Elzinga

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Professor Elzinga argues for the moral and practical advantages of government intervention in free enterprise—in the form of trust-busting and antimonopoly regulations—but, in doing so, stays in the realm of the thought experiment and pure theory. Thus he dismisses my examples of *Toys 'R' Us* and *Microsoft*, two of the most important antitrust trust enforcement cases of our time, as "statistical outliers."

But he need not have analyzed my examples of ill-conceived interventions. For there is a century of case history on antitrust enforcement, but Elzinga chooses to ignore it. He does not relate a single real-world example that would cause a reader to say: "Now, that is an example of an economically beneficial and morally sound intervention. We need more of that!" Nowhere does he cite a case in which antitrust enforcers, presently or historically, were clearly working on the side of the angels.

This is disappointing. It robs the reader of the chance to pick apart the details, just as so many economists have done for all the ill-conceived interventions of the past. It turns out that, in case after case, dating back to the passage of the Sherman Antitrust Act, we see four primary features of antitrust action in the real world: 1) suits are brought or encouraged by disgruntled competitors, 2) the targeted firm had economically rational reasons to be engaged in supposedly objectionable pricing and merger practices, 3) consumers were benefitting from supposed monopoly practices, usually by enjoying falling prices and increasing quality, and 4) the antitrust intervention forced new inefficiencies, squelched innovation, and made property rights less secure.

Is avoiding real-world examples a wise tactic? Probably. Economists who push violent intervention in market exchange, in the name of busting supposed trusts and monopolies, make their strongest case in the realm of pure theory. On the blackboard, static curves can be manipulated to show firms as exploitative, consumers as passive price takers, and profits as resulting from every manner of conspiracy; government meanwhile has no interest but the public good and the preservation of an orderly market.

But actual world experience teaches us that the conventional neoclassical model just does not comport with reality.[1] Firms cannot dictate prices, not even those suspected of being monopolists (I am old enough to remember IBM being hounded as a monopolist). Predatory pricing does not work in the long term because companies cannot suffer losses forever, and profits attract new entries. Attempts to create ironclad cartels fail due to strong incentives for defection. So long as markets are free, consumers are not exploited by companies, even those deemed monopolistic. This is the conclusion of the empirical literature, and readers are invited to examine it to see how erroneous Progressive Era theories of monopoly truly were, even when these theories were at their height.[2]

In the real world, versus the undisturbed Eden of equilibrium models, antitrust enforcement is a dirty business. It consists of entrenched bureaucrats using the legal arm of the state to placate the demands that rent-seeking corporate lobbyists have against their more successful competitors. It is because of policies like antitrust that Jennifer Roback Morse describes government policy as “an occasion of sin.” Its very existence tempts businessmen to resort to violence instead of persuasion and innovation to better their competitors.

But Elzinga is unconvinced. And, in his response to me, he has demonstrated that it is not necessary to draw graphs in order to perpetuate flawed and static assumptions about market failures; this can be done in prose as well. So, in his thought experiments, we are invited to toss out everything we know about the way real markets work. He conjures up an image of firms that “tire of competing against each other” and decide to divide up the market geographically. He introduces us to sellers who, “unhappy with prevailing prices,” just “agree” to set a floor. It is just that easy. We meet bid poolers who successfully conspire to divide up the profits. The wise guys at Goldman Sachs, if they so desired, could orchestrate “the merger of every paper manufacturer in the United States” and then make out like bandits.

His examples show that Elzinga has more than a mere quibble with one aspect of the way markets work. If he really believes business has this kind of power, he should also have profound doubts about the merits of capitalism itself, despite his claim that he would merely like to save the system from itself (that is also what the New Dealers said).

Businessmen can indeed be greedy. They may indeed attempt to act in the way Elzinga suggests they do. So let us take for granted that all businessmen "tire of competing," that all producers would like to sell their wares at a higher price (just as consumers would like everything at zero price), and that all bidders would love to be part of a bid-pooling conspiracy. Finally, let us assume that every investment banking firm would love to possess and hold onto a global resource monopoly.[3]

What prevents monopolies from prevailing in a market setting? Why, if pricing conspiracies are so easy to achieve and industrial concentration always consistent with profitability, is not the whole economy one big cartel or huge firm? How can we account for the fact that some firms are big, and some small, yet in a market no single firm can gain sufficient power to set its own prices, make huge profits, and hold the consuming public hostage?[4] The answer lies in the dynamics of market competition. Competition requires that firms win and keep the affections of consumers in order to generate profits in the short and long term. Those who attempt to raise their prices above the market rate, or merge in order to control a greater market share, or divide geographically to carve up consumers, confront the reality that a) they cannot control the buying decisions of consumers, and b) there are always others out there who respond to perceived market inefficiencies by entering the market to serve the consumer when others are not doing so. In the market economy, competitive forces are built into the very structure of the profit and loss system. They do not need strengthening by government regulators, the most notorious cartel creators the world has ever known.

In trying to isolate the oversight that has led Elzinga to attribute superhuman powers to mere makers and sellers of products, I can only come up with this: he has not seriously considered that the free market itself imposes limits on the size of firms. Without going further into the theory of the firm, let me simply recommend three articles that help clarify the issue: "Economic Calculation and the Limits of Organization" by Peter G. Klein; "Cartels as Efficient Productive Structures" by Pascal Salin; and "The Myth of Natural Monopoly" by Thomas DiLorezno. All three appear in *The Review of Austrian Economics,* vol. 9, no. 2.

The economic costs imposed by antitrust laws are vast. They consist not only of the expenses involved in defending one's companies against antitrust suits; we must also consider the mergers that are blocked, the innovations not pursued, and the competitive strategies not undertaken because of the legal uncertainty stirred up by antitrust overseers. We are witnessing a practical illustration of this less visible problem in the attempt by the Justice Department to manage the pace of product improvement in the software industry.

Now to morality. "Antitrust laws which deter cartels are deterring the bearing of false witness," Elzinga writes.[5] An intriguing argument, but one that does not stand scrutiny. It assumes that somehow there is an unambiguous distinction between the "true" or the "right" price, known only to regulators and economists, and the price being offered on the free market. No such distinction exists (again, outside rarified neoclassical pricing models, in which prices can appear to be rigged simply by changing the slope of a curve). If prices are generated by markets, consumers are justified in thinking of them as true; they can buy or abstain from buying based on their own needs and resources. There is no standard outside of real market experience to say otherwise.

What is the right price of Mr. Potato Head? Of oil? Of luxury cars? Of paper towels? Of professors? Only the interaction of supply and demand, worked out by real people buying, selling, and producing with real property, can tell us for sure. There is no independent crystal ball that reveals true prices. No one has access to the vast array of information that would be required to announce, apart from the market's own verdict, "this is the true price and the market is lying."[6]

Elzinga's critique of "output restriction" illustrates the point nicely. (This practice occurs when firms withhold products from the market in order to drive up the price and earn higher profits). But output restriction cannot be inherently immoral unless there is some moral rule with which I am unfamiliar that requires owners of property to disgorge themselves of their holdings at any price so long as consumers demand it of them. Economic morality, in fact, suggests the opposite: owners of property have the right to allocate resources in the most efficient (i.e., profitable) way over time consistent with existing market scarcities.

As regards the bearing of false witness, how pleasant it would be to see government held to account for its litany of violations of this commandment.[7] Commandments even more relevant to this debate would be the seventh and tenth: "Thou shalt not steal" and "thou shalt not covet your neighbor's house." The seventh is an outright condemnation of theft, which the antitrust department of the Justice Department and the Federal Trade Commission engage in each time they prevent the owners of property from organizing their business affairs in the most efficient manner possible (as judged by the owners of property themselves). The tenth commandment is a condemnation of envy, the sin of which businessmen who ask the government to hobble their competitors are profoundly guilty. The long history of antitrust policy is a prime example of institutionalized envy and theft. It is not necessary to adopt a purist libertarian attitude towards politics to say this is wrong; it only requires that we understand the difference between mine and thine.

Finally, Elzinga is right that patents are monopolistic. They are granted by the government.

Notes

[1] An essential overview is provided by Michael E. DeBow, "Markets, Government Intervention, and the Role of Information: An 'Austrian School' Perspective, With an Application to Merger Regulation," *George Mason University Law Review* 14, no. 1 (Fall 1991): 1-98.

[2] Three good places to start: *Antitrust and Monopoly: Anatomy of a Policy Failure* by Dominick Armentano (New York: John Wiley & Sons, 1982); Murray N. Rothbard, *Man, Economy, and State* (Auburn, AL: The Mises Institute, 1993); *The Antitrust Reader*, compiled by Clyde Wayne Crews, Jr. (Washington, DC: Competitive Enterprise Institute, 1997). Elzinga has a contribution to this last volume in which he assures us, in contrast to the public-choice model of government, that better regulators will make better policy. We need only trust their judgment.

[3] I am assuming that by warning about the prospect of a single paper monopolist, Elzinga meant to raise fears of a "resource monopoly," the strongest trump card of the antitrust advocate; but, of course, a full resource monopoly in paper would require owning all the world's trees as well.

[4] Elzinga says monopolies may work themselves out in the long run, but short run intervention can be effective in protecting consumers. Given the slow pace of antitrust litigation, however, the long run often arrives before the legal process is complete. In the high tech world, where antitrust intervention is very conspicuous, the short run is extremely short indeed, and intervention has done nothing but slow the pace of innovation.

[5] I was at first startled by Elzinga's claim that antitrust police are necessary to keep businessmen from breaking the ninth commandment which, in my Catholic Catechism, is "Thou shalt not covet thy neighbor's wife." A good rule, to be sure, but seemingly more related to sexual harassment law than antitrust. After the Reformation, it turns out, Protestants renumbered the commandments to split the first commandment into two parts, so that the rule against graven images would appear as a separate commandment. This then would seem to provide a moral justification for iconoclasm, a particularly gruesome form of property-rights invasion. That, in turn, required the reformers to combine the last two commandments into one, so that the ninth commandment does indeed end up being: "Thou shalt not bear false witness."

[6] For a moral argument that the market price is the just price, and that the only monopolies which are morally objectionable are those created by the state, see Alejandro Chafuen, *Christians for Freedom* (San Francisco: Ignatius Press, 1986), 93-119, and particularly 116-119.

[7] James T. Bennett and Thomas J. DiLorenzo, *Official Lies: How Washington Misleads Us* (Alexandria, VA: Groom Books, 1992).