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What's Hip (in Antitrust) Today Should Stay Passé

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What's Hip (in Antitrust) Today Should Stay Passé

Henry G. Manne and Geoffrey A. Manne [1]

You done went and found you a guru,
In your effort to find you a new you,
And maybe even managed
To raise your conscious level.
While you're striving to find the right road,
There's one thing you should know:
What's hip today
Might become passé.

– Tower of Power, *What Is Hip?*[2]

[1] Henry G. Manne, who passed away in 2015, was Dean Emeritus of the George Mason University School of Law. In 1991, at the inaugural meeting of the American Law & Economics Association (ALEA), Manne was named a Life Member of ALEA and, along with Nobel Laureate Ronald Coase, and federal appeals court judges Richard Posner and Guido Calabresi, one of the four Founders of Law and Economics. Geoffrey A. Manne is founder and Executive Director of the International Center for Law & Economics, which is dedicated to the memory of Henry G. Manne and UCLA economist, Armen A. Alchian. *About Us*, INTERNATIONAL CENTER FOR LAW & ECONOMICS, https://laweconcenter.org/about (last visited Apr. 30, 2018). He is also Henry Manne's son. The bulk of this paper is a reprint of Henry Manne's testimony on the Industrial Reorganization Act before the Senate Judiciary Committee, Subcommittee on Antitrust and Monopoly, on April 9, 1974. The introductory material was drafted by Geoffrey Manne.

[2] EMILIO CASTILLO, JOHN DAVID GARIBALDI & STEPHEN M. KUPKA, WHAT IS HIP? (Bob-A-Lew Songs 1973), performed by Tower of Power on TOWER OF POWER (Warner Bros. 1973).

Introduction: The (Unfortunate) Relevance of Henry Manne's Testimony Today

In 1973, Michigan Senator Philip A. Hart introduced Senate Bill 1167, the Industrial Reorganization Act,[3] in order to address perceived problems arising from industrial concentration. The bill was rooted in the belief that industry concentration led inexorably to monopoly power; that monopoly power, however obtained, posed an inexorable threat to freedom and prosperity; and that the antitrust laws (*i.e.*, the Sherman and Clayton Acts) were insufficient to address the purported problems.

That sentiment — rooted in the reflexive application of the (largely-discredited[4]) structure-conduct-performance (SCP) paradigm[5] — had become largely passé, but has resurfaced today as the asserted justification for similar (although less onerous) antitrust reform legislation[6] and the general approach to antitrust analysis commonly known as "hipster antitrust."[7]

The critiques leveled against the asserted economic underpinnings of efforts like the Industrial Reorganization Act are as relevant today as they were then:

> Industries have become concentrated where that was the road to lower costs. It is these lower costs that have created temporary, above-average profitability in concentrated industries when it has occurred. Where concentration was not the road to lower costs, industries have remained unconcentrated. The market has worked surprisingly well, where it has

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[3] Industrial Reorganization Act, S. 1167, 93rd Cong., 1st Sess. (1973) (Sen. Hart also previously introduced the bill under the same name in 1972 as S. 3832, 92nd Cong., 2nd Sess. (1972). Apparently he also introduced the bill in 1974 and 1975. *See* Harry First, *Woodstock Antitrust*, CPI ANTITRUST CHRONICLE (Aril 2018) at 1, *available at* https://www.competitionpolicyinternational.com/wp-content/uploads/2018/04/CPI-First.pdf.).

[4] *See* INDUSTRIAL CONCENTRATION: THE NEW LEARNING (Harvey J. Goldschmid, H. Michael Mann, and J. Fred Weston, eds., 1974), and *see especially* Harold Demsetz, *Two Systems of Belief About Monopoly*, in *id.* at 164-184. *See also* Sam Peltzman, *The Gains and Losses from Industrial Concentration,* 20 J. L. & ECON. 229 (1977); Yale Brozen, *The Concentration-Collusion Doctrine,* 46 ANTITRUST L. J. 826 (1978).

[5] *See* JOE BAIN, INDUSTRIAL ORGANIZATION 372-468 (1968).

[6] *See, e.g.*, Consolidation Prevention and Competition Promotion Act, S. 1812, 115th Cong., 1st Sess. (2017).

[7] See, for example, the essays collected in the April 2018 volume of the CPI ANTITRUST CHRONICLE, "Hipster Antitrust" (Konstantin Medvedovsky, ed.), *available at* https://www.competitionpolicyinternational.com/wp-content/uploads/2018/04/AC_APRIL.pdf.

> been permitted, to conserve our resources and maximize our output. The antitrust agencies concentration on concentration in recent years is misdirected and should cease. If we need villains, regulatory agencies are a more appropriate prospect.[8]

The proposed bill itself was the subject of a series of hearings in both the Senate and the House, including one on April 9, 1974, at which Henry G. Manne (then professor of law and political science at the University of Rochester) testified (along with UCLA economist,[9] Harold Demsetz) in opposition to the bill. His trenchant testimony, reprinted in full in Section 2, below,[10] should be required reading for advocates of a return to antitrust law and policy rooted in the SCP paradigm.

The basics of the Industrial Reorganization Act

The Industrial Reorganization Act would have made it unlawful "for any corporation… to possess monopoly power."[11] Monopoly power would be established under the bill based on a rebuttable presumption established by evidence that 1) a corporation earned an average, after-tax rate of return in excess of 15 percent; 2) "there has been no substantial price competition among two or more corporations;" or 3) any four or fewer corporations account for 50 percent of sales in a line of commerce.[12]

The Act specified two affirmative defenses to the presumption: 1) that monopoly power was due solely to the ownership and lawful use of valid patents; or 2) that monopoly power was essential to the realization of "substantial economies."[13] It's unclear whether these were meant as the only evidence that could rebut the presumption of monopoly power.

The proposed statute was to be administered by a newly created, one-man commission (plus staff), the Industrial Reorganization Commission (to be succeeded after 15 years by the Federal Trade Commission).[14] The Commission would

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[8] Brozen, *The Concentration-Collusion Doctrine, supra* note 1 at 856.

[9] And International Center for Law & Economics Academic Advisory Board member.

[10] *Infra* pages 13-30.

[11] Industrial Reorganization Act, *supra* note 3 at Title I, § 101(a).

[12] *Id.* at Title I, § 101(b).

[13] *Id.* at Title I, § 101(c).

[14] *Id.* at Title II, § 202(b) & (h).

determine which corporations had violated the statute's prohibition against the possession of monopoly power and bring suit before a newly created, 15-member Article III court, the Industrial Reorganization Court.[15]

Perhaps most remarkably, the bill would also have required the Industrial Reorganization Commission to "study the structure, performance, and control" of seven "priority" industries[16] and, for each, to

> develop a plan of reorganization… whether or not any corporation [was determined to possess monopoly power]. In developing a plan of reorganization for any industry, the Commission shall determine for each; such industry—
>
> (A) The maximum feasible number of competitors at every level without the loss of substantial economies;
> (B) The minimum feasible degree of vertical integration without the loss of substantial economies; and
> (C) The maximum feasible degree of ease of entry at every level.[17]

The impetus behind the Act and its relevance to today's "hipster antitrust" movement

The bill was, obviously, never enacted into law. But the conversation around the proposal is instructive, as efforts to invigorate antitrust enforcement today have adopted many of the same underpinnings as those of the Industrial Reorganization Act.

Of course, the sort of thinking that gave rise to the Industrial Reorganization Act was nothing new, even then — and nor were its defects. As the late, great business historian Thomas McCraw writes of Louis Brandeis' efforts to combat "the curse of bigness" early in the 20th century:

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[15] *Id.* at Title III, § 301.

[16] *Id.* at Title I, § 203(a)(1). The identified industries were 1) chemicals and drugs; 2) electronic computing and communication equipment; 3) electrical machinery and equipment; 4) energy; 5) iron and steel; 6) motor vehicles; and 7) nonferrous metals. According to Sen. Hart, these industries "account for, in the aggregate, nearly 40% of the total value created in U. S. manufacturing. One hundred and forty of the country's top 200 corporations participate in them." Philip A. Hart, *Restructuring the Oligopoly Sector: The Case for a New 'Industrial Reorganization Act'*, 5 ANTITRUST L. & ECON. REV. 35, 40 (1972).

[17] *Id.* at Title I, § 203(a)(2).

> Brandeis' fixation on bigness as the essence of the problem doomed to superficiality both his diagnosis and his prescription.... It meant that he must argue against vertical integration and other innovations that enhanced productive efficiency and consumer welfare. It meant conversely that he must favor cartels and other loose horizontal combinations that protected individual businessmen against absorption into tight mergers but that also raised prices and lowered output. It meant that he must promote retail price fixing as a means of protecting individual wholesalers and retailers, even though consumers again suffered. It meant, finally, that he must become in significant measure not the "people's lawyer" but the spokesman of retail druggists, small shoe manufacturers, and other members of the petite bourgeoisie. These groups, like so many others throughout American history, sought to use the power of government to reverse economic forces that were threatening to render them obsolete. In Brandeis they found a talented champion.[18]

Today's "hipster antitrust" movement evinces many of the same failings, as well.

As Henry Manne notes in his testimony below:

> To be successful in this stated aim ["getting the government out of the market"] the following dreams would have to come true: The members of both the special commission and the court established by the bill would have to be satisfied merely to complete their assigned task and then abdicate their tremendous power and authority; they would have to know how to satisfactorily define and identify the limits of the industries to be restructured; the Government's regulation would not sacrifice significant efficiencies or economies of scale; and the incentive for new firms to enter an industry would not be diminished by the threat of a punitive response to success.
>
> **The lessons of history, economic theory, and practical politics argue overwhelmingly against every one of these assumptions**.[19]

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[18] THOMAS K. MCGRAW, PROPHETS OF REGULATION: CHARLES FRANCIS ADAMS, LOUIS D. BRANDEIS, JAMES M. LANDIS, ALFRED E. KAHN 141 (Harvard University Press, 1984).

[19] *Infra* page 21 (emphasis added).

Both the subject matter of and impetus for the proposed bill (as well as Manne's testimony explaining its economic and political failings) are eerily familiar. The preamble to the Industrial Reorganization Act asserts that

> competition… preserves a democratic society, and provides an opportunity for a more equitable distribution of wealth while avoiding the undue concentration of economic, social, and political power; [and] the decline of competition in industries with oligopoly or monopoly power has contributed to unemployment, inflation, inefficiency, an underutilization of economic capacity, and the decline of exports….[20]

The echoes in today's efforts to rein in corporate power by adopting structural presumptions are unmistakable. Compare, for example, this language from Sen. Klobuchar's Consolidation Prevention and Competition Promotion Act of 2017:

> [C]oncentration that leads to market power and anticompetitive conduct makes it more difficult for people in the United States to start their own businesses, depresses wages, and increases economic inequality;
>
> undue market concentration also contributes to the consolidation of political power, undermining the health of democracy in the United States; [and]
>
> the anticompetitive effects of market power created by concentration include higher prices, lower quality, significantly less choice, reduced innovation, foreclosure of competitors, increased entry barriers, and monopsony power.[21]

In a 1972 statement in support of his first effort to introduce the Act, Sen. Hart defended the legislation:

> It could also be, if it lives up to my expectations, a giant step toward eliminating some of the current feeling that opportunities no longer exist for the individual and that the economic life of the nation will always be dominated by a few. We all recognize, for example, that too much power in too few hands is bad for social and political as well as for economic reasons.[22]

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[20] Industrial Reorganization Act, *supra* note 3, at preamble.

[21] Consolidation Prevention and Competition Promotion Act, *supra* note 6, at § 2(a)(4) - (6).

[22] Hart, *Restructuring the Oligopoly Sector*, *supra* note 16 at 37 (which reprints Sen. Hart's statement, along with the text of the bill and an analysis of the bill prepared by the Senate Antitrust and Monopoly Subcommittee staff).

More specifically, Sen. Hart asserted that concentrated industry — not monetary policy, of course — was the source of the day's most pervasive economic problems (inflation and unemployment):

> Concentrated industries not only display little price competition but tend to maintain or increase prices as demand falls in order to prevent the erosion of their profits. Government efforts to halt inflation by cutting demand thus tend to backfire in these industries, producing still higher prices — and more layoffs — as the companies involved seek to maintain their targeted profits, a situation that has been all too familiar to us over the past 4 years. Government has used all the traditional tools in its arsenal to fight our recent inflation but both it and high unemployment have continued to flourish. The reason, I suggest, is that we have been applying a medication designed for a competitive enterprise system when concentrated industries have in fact already wiped out much of the competition.[23]

Faced with the threat of "pervasive regulation of wages, prices, and profits" to combat these and other ills, Sen. Hart introduced his bill as "an alternative to government regulation and control."[24] Sen. Hart saw the need for a bill that:

> involves changing the life styles of many of our largest corporations, even to the point of restructuring whole industries. It involves positive government action, not to control industry but to restore competition and freedom of enterprise in the economy.[25]

Like many defenders of today's antitrust populism, Sen. Hart saw his bill and the invigoration of structural antitrust it entailed as a *restrained*, necessary aspect of a free, inclusive economy:

> Government regulation is not the way for a democracy. The tradeoff — less power in the hands of a few citizens for more power in the hands of government — is, to me, a bad bargain. It would be immeasurably better, in my view, if we could have an economy where the marketplace is the regulator, the rules are fair to all, and the more efficient and more

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[23] *Id.* at 40.

[24] *Id.* at 37.

[25] *Id.* at 37-38.

> diligent to do the rest. Freedom prevails under such a system, freedom for companies to succeed and fail — freedom for new companies to be born — freedom of government from the will of superpowerful corporations — freedom for consumers to make companies respond to their desires.[26]

Viewing enforcement metrics as an indication of the merits of an antitrust regime, and looking solely at structure as an indication of a problem, Sen. Hart claimed that

> [u]nfortunately, however, this thrice-stated philosophy of Congress [to "wipe out the power over men's lives — as well as the power over the economy" exercised by large corporations[27]] has been generally ignored in the enforcement of our antitrust laws. In most cases the Government has sought chiefly to prove that the power in question had been or could be used to harm competition and seldom to wipe out monopoly or oligopoly power just because it was there. Indeed, these laws have not even been used vigorously to prevent the development of new monopoly power.[28]

And, like today's advocates of increased government intervention to design the structure of the economy, Sen. Hart sought — without a trace of irony — to "cure" the problem of politicized, ineffective enforcement by doubling down on the power of the enforcers:

> While I still believe that the existing antitrust laws could go a long way toward eliminating much of the concentrated economic power we are concerned about, I have given up hope that — absent a new congressional mandate — any attorney general will in fact bring the necessary cases to undo the concentration which has already taken place. We are seemingly caught in a web of our own weaving: popular reasoning is that, while dismantling some of these corporations is theoretically in the public interest, the effect of that dismantling would nonetheless be, in some unspecified way, disastrous. To accept that conclusion, however, is to accept the notion that we must allow the government to increasingly become the handmaiden of the

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[26] *Id.* at 38.

[27] *Id.*

[28] *Id.* at 38-39.

> corporations, that we must sit back and watch public government being replaced by private control.[29]

As Henry Manne pointedly notes in response to concerns such as these, the worst problems of monopoly power are of the government's own making. The real threat to democracy, freedom, and prosperity is the political power amassed in the bureaucratic apparatus that frequently *confers* monopoly, at least as much as the monopoly power it spawns:

> [I]t takes two to make that bargain [political protection and subsidies in exchange for lobbying]. And as we look around at various industries we are constrained to ask who has not done this. And more to the point, who has not succeeded?
>
> It is unhappily almost impossible to name a significant industry in the United States that has not gained some degree of protection from the rigors of competition from Federal, State or local governments.
>
> * * *
>
> But the solution to inefficiencies created by Government controls cannot lie in still more controls. The politically responsible task ahead for Congress is to dismantle our existing regulatory monster before it strangles us.
>
> We have spawned a gigantic bureaucracy whose own political power threatens the democratic legitimacy of government.
>
> We are rapidly moving toward the worst features of a centrally planned economy with none of the redeeming political, economic, or ethical features usually claimed for such systems.[30]

Or, as Phillip Areeda aptly noted: "Indeed, the fabric of restraint woven by government is so extensive that private restraints may seem trivial in comparison."[31] And as I have noted elsewhere, constraining firm size in an effort to promote consumer political and economic power may actually have the *opposite* effect:

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[29] *Id.* at 39.

[30] *Infra* pages 22-23.

[31] PHILLIP AREEDA, ANTITRUST ANALYSIS: PROBLEMS, TEXT, CASES 29 (3rd ed. 1981).

> To begin, at the margin, if you limit firm growth as a means of competing with rivals, you make correspondingly more important competition through political influence. Erecting barriers to entry and raising rivals' costs through regulation are time-honored American political traditions,[[32]] and rent-seeking by smaller firms could both be more prevalent, and, paradoxically, ultimately lead to *increased* concentration.
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> Next, by imbuing antitrust with an ill-defined set of vague political objectives, you also make antitrust into a sort of "meta-legislation."[[33]] As a result, the return on influencing a handful of government appointments with authority over antitrust becomes huge — increasing the ability and the incentive to do so.
>
> And finally, if the underlying basis for antitrust enforcement is extended beyond economic welfare effects, how long can we expect to resist calls to *restrain* enforcement precisely to further those goals? All of a sudden the effort and ability to get exemptions will be massively increased as the persuasiveness of the claimed justifications for those exemptions, which already encompass non-economic goals,[[34]] will be greatly enhanced. We might even find, again, that we end up with even *more* concentration because the exceptions could subsume the rules.
>
> All of which of course highlights the fundamental, underlying problem: If you make antitrust more *political*, you'll get less democratic, more politically determined, results — precisely the opposite of what proponents claim to want.[35]

But these concerns only touch on the comprehensive critique leveled by Henry Manne in his 1974 testimony on the Industrial Reorganization Act. The following is

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[32] *See*, *e.g.*, James Bessen, *Lobbyists Are Behind the Rise in Corporate Profits*, HARVARD BUSINESS REVIEW (May 26, 2016), https://hbr.org/2016/05/lobbyists-are-behind-the-rise-in-corporate-profits.

[33] Geoffrey Manne, *The Antitrust Laws Are Not Some Meta-Legislation Authorizing Whatever Regulation Activists Want: Labor Market Edition*, TRUTH ON THE MARKET (Sep. 22, 2017), https://truthonthemarket.com/2017/09/22/the-antitrust-laws-are-not-some-meta-legislation-authorizing-whatever-regulation-activists-want-labor-market-edition/.

[34] See generally ANTITRUST MODERNIZATION COMM'N REPORT AND RECOMMENDATIONS, Chap. IV.B 333-342 (2007), *available at* http://govinfo.library.unt.edu/amc/report_recommendation/amc_final_report.pdf.

[35] Geoffrey Manne, *The Illiberal Vision of Neo-Brandesian Antitrust*, TRUTH ON THE MARKET (Apr. 16, 2018), https://truthonthemarket.com/2018/04/16/the-illiberal-vision-of-neo-brandeisian-antitrust/.

his testimony in full, including his exchange with Sen. Hart and committee staffers following his prepared remarks. It is, sadly, nearly as germane today as it was then.

Henry Manne's Testimony on the Proposed Industrial Reorganization Act of 1973

STATEMENT OF HENRY G. MANNE, PROFESSOR OF LAW AND POLITICAL SCIENCE, UNIVERSITY OF ROCHESTER, ROCHESTER, N.Y.[36]

Dr. MANNE. Thank you.

The political and intellectual debate about the cause and effects of corporate size and industrial concentration has continued without resolution for nearly a century now.

Apparently, we are no closer to agreement today that we were during the murky and confusing debates on the Sherman Act over 85 years ago.

The subject still affords a happy hunting ground for anyone seeking simplistic and often sensational solutions to questions of vast complexity.

I should like, therefore, to isolate the few aspects of the industrial organization field on which there may be general professional agreement and address myself primarily to the question of how best to secure greater benefits of industrial competition in relation to what we know and what we do not know.

We may start any logical analysis of this subject by pointing out that a high concentration ratio could signify either that relatively large size firms are efficient or that they have engaged in monopolization or collusion of some sort.

It should be noted, however, that the efficiency argument does not in any sense mean that only one size of firm is optimal or will survive in a given industry.

A competitive industry may well generate firms in a variety of efficient sizes. Further, various combinations of numbers of large and small firms may occur in a competitive industry with all of them operating at high levels of technological efficiency.

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[36] This hearing transcript is reprinted from the original transcript produced by the GPO, captioned: THE INDUSTRIAL REORGANIZATION ACT, Hearings Before the Subcommittee on Antitrust and Monopoly of the Committee on the Judiciary, United States Senate, Ninety-Third Congress, Second Session, on S. 1167, Part 4: Ground Transportation Industries. April 4, 9, 10, and 11, 1974. Printed for the use of the Committee on the Judiciary (Pursuant to S. Res. 255, Sec. 4). The material reprinted here begins on p. 2291.

But it is essential to understand at the outset a point many economists seem to ignore. There are economies of scale other than the purely technological ones relating to the size of a factory or the output of a given plant.

Competitive marketing strategies, management, labor laws, tax rules, safety regulations, communications, and a host of other issues may all lend themselves to economies of scale in firm size, as well as account for varying optimal sizes for firms within an industry.

Probably the single most significant nontechnological basis for large size relates to economies in complying with the myriad regulations affecting market contractual arrangements.

That is, we have by various market regulations often made it cheaper to handle production through intrafirm arrangements, thus swelling size, than through contracting in the open market.

An honest study of these costs, and the resultant effects, seems more overdue than another public debate over size and concentration.

It may not be remiss at this point to compare what we know about political parties to the issues in industry addressed by S. 1167. In the completely free political structures allowed by the U.S. Constitution we have developed only two significant political parties.

And one of these, measured by party registration, is significantly larger than the other. Generally in the last 45 years it has achieved an overwhelming superiority of all votes cast.

It would seem, by all of the criteria used by proponents of the instant bill to judge the General Motors Corp. or IBM, that the Democratic Party should forthwith be reorganized into nine, or some other arbitrary number, of smaller, safer, more competitive, more innovative, and less politically powerful organizations.

Senator HART. I am tempted to say that you must not be a Democrat because we are organized into at least 90.

Mr. MANNE. That just proves how endemic competition really is.

How else, after all, can we expect our system of democracy to survive, competing interests to be recognized, and freedom to prevail.

I am, of course, merely paraphrasing some of the rhetoric used by economists who have previously testified before this committee.

But the analogy is in no sense far-fetched, and indeed the spectre of only two competing political parties in a nation whose central government has become as powerful as ours is more frightening to any thoughtful citizen than the vision of 200 large domestic corporations each competing in many ways for the consumers' dollars.

Yet no one with enough influence to be taken seriously has suggested that our political system is evil or that it exhibits monopolistic characteristics that could only be corrected by altering the structure of the parties.

Still it is a sobering thought. However, to return to industrial organization, the economic effects of monopoly power are twofold, and indeed the entire logical argument against monopoly, as opposed to large size per se, rests on these arguments.

One is that these firms are in a position to realize unwarranted high profits, and the second is that monopoly power causes an allocation of resources to their less efficient uses.

Unfortunately, the latter point, while it may express the more significant informed concern about monopoly, is not subject to any direct tests of which I am aware, since we do not have any non-market standards for determining allocational efficiency.

We are forced, therefore, by the nature of the data and techniques available, to limit ourselves to making comparative studies of returns in different industries and firms.

And even this must be done with a clear understanding that our statistical and accounting techniques for assembling this data and interpreting it are not terribly reliable.

Nonetheless the studies done to date strongly indicate that there is little or no significant correlation between industrial concentration and corporate profits.

To be sure, if one selects a particular year with peculiar characteristics, the figures can be made to appear otherwise, but in general, over a significant period of time, this lack of correlation seems well substantiated.

This is not to say, however, that no firm in a concentrated industry may not be realizing monopoly profits. The studies referred to only indicate that there is no causal relationship between concentration on the one hand and monopoly profit on the other.

We are, it appears, as apt to find companies earning a higher than market rate of return in nonconcentrated industries as in concentrated ones.

Indeed, one thing on which there is unequivocal agreement among economists — a rare circumstance indeed — is that monopoly rates of return are realized regularly in some of the least-concentrated industries imaginable: those for personal services.

Members of the medical profession, many other licensed professionals, and members of strong craft unions in particular all appear to display this characteristic.

Again, as with political parties, it is rare to hear of remedial legislation being offered to remedy this clear monopoly problem.

In the industrial sector on the other hand, where remedies for unproved problems abound, monopoly rates of return, when they do occur, seem unlikely to persist for a significant period of time.

The reasons for believing this have little to do with the complex econometric industry models and concentration ratios so popular in this computer era.

To begin, unless entry into an industry is actually prevented by law or private coercion it is highly unlikely that new firms will not enter any industry in which some firms are presently and persistently realizing monopoly profits.

The information cannot be hidden for long. In this fashion, as the new firms increase total industry production, they compete down the monopoly profits previously being realized and will frequently be more efficient than the older firms.

This process of competitive entry is so powerful, and so irresistible without Government protection, that we need only consider one possible limitation to it as a complete solution to any monopoly problem, real or imagined.

There may be substantial nonproduction costs for entering an industry. These would mainly be entry costs associated with Government regulations, since any other costs should be considered merely capitalized costs of production applicable to any firm in the industry. To the extent that these artificial entry costs exceed the present discounted value of anticipated net revenues from production and sales, monopoly profits can persist.

In its most extreme form, when entry into an industry is made illegal — as when a certificate of public convenience and necessity cannot be acquired — entry costs become infinite.

Then any monopoly returns being realized by firms presently in the industry can be anticipated to continue indefinitely.

But it should be emphasized that merely because the most efficient size for a new firm is large does in no sense imply that artificially high returns to existing firms can persist.

Start-up costs are simply costs of production and the fact that they are high because the most efficient size plant is relatively large certainly does not imply any monopoly power in the existing firms.

There is no difference from an economic point of view in a large capital outlay for plant financed through periodic payments on bonds and equivalent periodic payments made for raw materials in another industry with low start-up costs.

Each should be viewed as production costs. Yet some economists erroneously persist in referring to one of these as a "barrier to entry" and the other as a competitive cost.

The next reason for suggesting that S. 1167 addresses itself to a largely imaginary issue is the growing body of evidence that private firms are incapable of perpetuating a monopoly or cartel by private means— though the same evidence also shows that they have frequently made the attempt.

Recent historical works have made clear what economic theory had long implied about the perpetuation of monopolies: that it is prohibitively expensive to maintain a monopoly through purely private means.

Especially to be recommended to the members of the committee is the important work of Prof. Ellis Hawley entitled, "The New Deal and the Problem of Monopoly," Princeton, 1966.

About the only clear case one can imagine of long-term private exaction of monopoly rents are those in which racketeers use physical coercion to restrict competition and prevent entry.

Naturally we have no evidence about rates of return in such industries, but since such behavior is clearly illegal, its persistence would reflect largely a failure of law enforcement by governmental authorities rather than any evidence that private monopolization is normally persistent. In any event this type of behavior has not, at least in recent history, characterized any known efforts of large scale private industry in America.

Conventional business firms have much more frequently turned to the State or Federal Government for assistance when their private efforts to monopolize have failed.

Competition is after all the most dreaded and threatening process any business firm can confront. Before its power the mighty cringe and giants beg for surcease.

And when either the many or an influential few have "demonstrated a need for help," as the cliché has it, our Government has long shown its helpful readiness to respond.

In fact, in this function of protecting competitive firms from the harsh rigors of competition the Government has demonstrated a significant comparative advantage over the private sector, apparently because its coercive powers are so much greater.

But the reasons avowed for such protective legislation rarely describe honestly the actual motivation of either the industry seeking the protection or the Government officials granting it.

We are always told that Government regulation is adopted to prevent unfair competition, to protect the consumer from shoddy or unsafe products, to avoid monopoly pricing, to prevent fraudulent behavior, to conserve future supplies of goods, to save the environment, or to protect American producers and consumers from a foreign menace.

But we are rarely told the extent to which these regulations are encouraged or later supported for purely anticompetitive reasons.

More likely we are treated to homilies about Government -business partnerships and the social responsibility of corporations.

But who in politics will openly condemn the anticompetitive effects of the restraints Government puts on competition today?

Consider, just for starters, how much the public would benefit from free entry into transportation or the television industry; or from the repeal of tariffs and import quotas; or from a free market price for milk.

Yet the suggestion that we repeal these obvious restrictions on competition brings howls of protest from the interests presently protected and a strange silence from some of the same political representatives who express the most concern about the alleged monopolistic practices of big business.

Another reason that industrial monopolies are unlikely to persist in the absence of Government protection is that most industrial markets today are in reality international markets.

Few significant industrial items today involve such high transportation costs relative to price that the oceans provide a significant natural barrier to competition.

This fact alone makes most of the data presently used to describe concentration in American industries almost useless.

For instance, it is not uncommon to hear General Motors spoken of as having approximately one-half of the U.S. automobile market, with a clear insinuation that this statistic signifies monopoly power.

But the facts do not bear out the insinuation. While General Motors did, until recently, make about half the automobiles sold within the United States, and is naturally afforded some benefit over foreign competition by shipping costs, that does not tell us very much, since locational advantages are an important factor in any competitive situation.

It would be foolish even to try to act as if they did not exist. Still General Motors' fraction of free world vehicle production is approximately 22 percent; a figure that even the most ardent GM-baiters would not claim is sufficient to dominate an industry.

No one can honestly believe that the American automobile industry has not been subjected to intense competitive pressures from new entry in recent years.

In the period since World War II the total number of corporations offering distinctive styles, sizes, and qualities of automobiles in the American market has risen perhaps fivefold, and the survivors now account for over I14 million vehicle sales a year.

Names like Volkswagen, Datsun, Toyota, and Volvo have become more common household words here than DeSoto, Edsel, Hudson, or Corvair.

These then are some of the reasons the various economic arguments against industrial concentration remain unpersuasive. There is, however, a "political" argument that should also be considered.

It is that some corporations are so large that they are able to “control” the Government, presumably as it were, to “buy” the protection, the subsidy, the transportation system, the war, or whatever they want from the Government.

The argument that companies like Standard Oil, du Pont, and General Motors run our Federal, State and local governments like dictators is no longer simply a Marxist myth about the American system.

It has become common fare for television commentators, journalists, self-styled consumer spokesmen, and certain academics, all of whom speak with one voice — and a forked tongue.

Unfortunately, the energy utilized in making these assertions is about the only force behind them, and again it does not require complicated empirical studies to show the error, or perhaps the mendacity, for example, behind these assertions.

Has the automobile industry, for example, been more successful in Washington than the environmentalists?

Have the petroleum companies spent as much money lobbying for protective legislation as has the National Education Association?

Has the steel industry received as much bounty from our seemingly universal Federal welfare system as have the elderly, the uneducated, or those stricken with a strange desire to engage in farming?

One could go on like this almost endlessly. But to ask these rhetorical questions is sufficient to make the point.

There is simply no correlation between the concentration ratio in an industry, or the size of its firms, and the effectiveness of the industry in the halls of Government.

This scare argument about the political power of large corporations is a sham.

We all know that the institutions that influence policies in Washington are those that can deliver the votes or utilize their finances to secure votes.

And these are the very practices that large corporations are relatively weakest in performing, especially as compared to unions, farmers, consumer organizations, environmentalists, and other large voting blocks.

There is even less substance to this political argument about corporate concentration than there is to the economic ones.

Recently Senator Hart stated that "time is running out for those," like himself, "who would like to see competition given a real try in the marketplace."

However, to Senator Hart the reason competition has not been tried appears to lie in what he termed "the evident failure of the existing [structure of industry]."

That is, Senator Hart simply defines competition to preclude firms of a certain size, or industries with a certain concentration ratio.

Having asserted this definition. Senator Hart has, not illogically, proposed S. 1167, the Industrial Reorganization Act, to "make monopoly a per se violation [of the antitrust] laws and establish a special Commission and Court to oversee the restructuring of seven major industrial sectors of the economy."

The restructuring would take the form of super antitrust decrees ordering, among other things, substantial divestitures by firms in affected industries.

Senator Hart has argued in defense of this bill that it would allow the Government to intervene "only on a one-shot basis. It would," he continued, "restrict industries where this would not sacrifice efficiencies.

"Then it would get [the Government] out of the market."

I should be the first to congratulate Senator Hart on the statement of this worthy goal of getting the Government out of the market.

Unfortunately, however, I do not think that the vehicle chosen will ever carry us to this brave new world. To be successful in this stated aim the following dreams would have to come true: The members of both the special commission and the court established by the bill would have to be satisfied merely to complete their assigned task and then abdicate their tremendous power and authority; they would have to know how to satisfactorily define and identify the limits of the industries to be restructured; the Government's regulation would not sacrifice significant efficiencies or economies of scale; and the incentive for new firms to enter an industry would not be diminished by the threat of a punitive response to success.

The lessons of history, economic theory, and practical politics argue overwhelmingly against every one of these assumptions.

No one can seriously believe that a Federal agency that has once tasted the addictive power of dissolving or restructuring the largest industries in America would quietly abdicate its political power when that job was done.

Such a group will develop its own political interests, alliances, obligations, and claims, and the very absence of concrete, objective economic standards of performance will guarantee that political criteria will prevail in their determinations.

By an iron law of bureaucracy this agency would do all in its power to perpetuate itself and expand its authority. And by a subsection of the same iron law, it would succeed.

We have yet to see in the history of American industrial regulation an agency dissolved or liquidated after its initial task was accomplished.

I see nothing in the proposed legislation suggesting that it is likely to happen here.

In the same recent speech, Senator Hart alluded to the tremendous amount of resources that the petroleum industry has expended in gaining protection and subsidies from Congress.

He is correct, of course, but he seemed to overlook the fact that it takes two to make that bargain. And as we look around at various industries we are constrained to ask who has not done this. And more to the point, who has not succeeded?

It is unhappily almost impossible to name a significant industry in the United States that has not gained some degree of protection from the rigors of competition from Federal, State or local governments.

It appears, therefore, that the real costs of securing Government assistance or protection from competition are not very large, even though the economic costs to the public may be enormous.

Whatever the process is by which industries and firms achieve this governmental assistance we can only be certain that if it were made more difficult or more costly to obtain these favors, less of this "political good" would be demanded in the political marketplace.

But the solution to inefficiencies created by Government controls cannot lie in still more controls. The politically responsible task ahead for Congress is to dismantle our existing regulatory monster before it strangles us.

We have spawned a gigantic bureaucracy whose own political power threatens the democratic legitimacy of government.

We are rapidly moving toward the worst features of a centrally planned economy with none of the redeeming political, economic, or ethical features usually claimed for such systems.

It is, as Senator Hart has stated, already late. In fact it may be too late. I have futilely urged the business community itself to stop seeking economic favors from the Government.

But, as should perhaps be expected by anyone who urges corporate social responsibility, I have gotten nowhere with this argument.

Now with a fearful sense that there may in fact be no one left to listen or to act, I would still urge this committee to forcefully reject any new regulatory gimmicks and to get down to the much more serious task of freeing American competition from its single most serious opponent, the U.S. Government.

Thank you.

* * *

Senator HART. Thank you very much. You held no punches. I am grateful for it. You say that except where organized criminal musclemen have moved in, private firms are incapable of perpetuating a monopoly or cartel by private means.

Well then, do we need any antitrust laws?

Dr. MANNE. Well, to follow the response of that question by Professor Demsetz, there certainly may be cases in which temporary monopoly and illicit gains may be made as a result of collusive efforts.

We don't find much evidence, as I suggested, however, that these collusions persist for any long period of time. Now, that is not to justify them and I think that some degree of warning in the form of something like the Sherman Antitrust Act certainly has a place in our spectrum of legislation.

Senator HART. You would agree that it would be better to have Government include rather than wait for, what you describe as the natural course, the collapse of the monopoly?

Dr. MANNE. Well, it is a tough question for me. I am not completely certain in my own mind. I think that the evidence to date on how the courts and the Antitrust

Division and the Federal Trade Commission have behaved in relation to our existing antitrust laws is not reassuring.

If I were completely convinced that that legislation would be enforced in the future then I would probably have to conclude that we would be better off with no antitrust laws rather than that kind of enforcement of laws that might otherwise be justified.

Senator HART. If you were to name one conspicuous example of — I forget the word you have used — inappropriate Trade Commission or Justice Department or court application of antitrust, what are those at the top of the list?

Dr. MANNE. Well, I think that we have certainly gone much, much too far, on almost any defensible theory, in our attack on mergers.

I think there are a number of perfectly valid reasons for mergers. I think that the extension into the general antitrust gambit of restrictions on tying arrangements, resale price maintenance, matters of that sort are not economically defensible.

Senator HART. What about reciprocity?

Dr. MANNE. I can't find any strong reason for believing that there is a significant monopoly problem with reciprocity.

Senator HART. Is there a problem with reciprocity?

Dr. MANNE. Not that I can see.

Senator HART. What if you were a guy trying to sell a product?

Dr. MANNE. One of the peculiar questions is why industry finds, in some instances, that a resort to barter rather than utilization of more direct and simple contractual forms, using money as the medium of exchange occurs.

I don't know of any good theories about that. I would suggest in some cases it may be as I have suggested in my statement, that regulatory impacts on certain kinds of contracts may make these arrangements the cheaper way for corporations to behave.

These reciprocal contracts can also be a kind of short term, temporary, or abbreviated form of merger or other arrangement with perfectly normal business connotations.

I don't see the argument in connection with reciprocity that certainly can be made about mergers, that any of them, prima facie, could be logically construed as the equivalent, as you suggested earlier, of a collusive arrangement.

I don't see that possibility with reciprocity.

Senator HART. Mr. O'Leary?

Mr. O'LEARY. I have no questions, Mr. Chairman.

Senator HART. Mr. Chumbris?

Mr. CHUMBRIS. I have just a couple of comments here, Mr. Chairman. You noted in your statement that General Motors had 22 percent of the free world production of vehicles.

The testimony we had in the last few days of our hearings showed also that General Motors has only 37 percent of the automobiles that are produced either in this country or in foreign countries and imported to this country, and at the present time General Motors has only 44 percent of the cars of American-produced corporations, down from the high of 52 percent that it had in the previous years.

Dr. MANNE. The figure that I asked my research assistant to dig up was total vehicles, so that this includes trucks, where the figure—

Mr. CHUMBRIS. I was just adding to what you had already put down. In other words, what you are saying is what General Motors produces both in this country and around the world amounts to about 22 percent of the free- world market?

You had a very interesting point, also on the political power of big business. It is a subject that comes up repeatedly in our hearings because we always are dealing with so many different industries. I don't know whether you have ever read his book but Professor Engler wrote a book on the "Politics of Oil."

It goes back into the early 1930's, and goes back into the early history of oil. I think your point is well taken that if there is this so-called political power in this country it is stronger in the hands of the labor unions — and for good reason as has been explained time and again — and more lately in the hands of consumers.

Take Ralph Nader, and Mr. Gardner of Common Cause. They have a tremendous clout not only on Capitol Hill but I would say in the operation of the National Government and even on the State level. I have always felt that business was really a bad fourth place, with Government being the largest, with labor unions giving them a good close run, consumerism coming in third, and big business a bad fourth.

Dr. MANNE. I am sure we are not in disagreement when I add for emphasis that I see nothing wrong with that. I think it is quite healthy to have all of these varied forces competing for political power in a system such as ours.

On the other hand, this bad fourth as you call it, has, I believe, received undue attention from the press and perhaps other avenues of publicity. There is commonly thought to be some sort of overwhelming power industry has almost to reach in, as one does at a retail counter in a department store, and buy any legislation or ordinance or rule that they want. I think this is terribly misleading and, incidentally, destructive of the public confidence in a system the public should perhaps have more confidence in.

Mr. CHUMBRIS. Just one other point. You refer to the eight Federal agencies. First let me preface with this remark:

Over the past 5 years. Senator Ervin, as chairman of the Separation of Powers Subcommittee, has held numerous hearings on the Federal agencies which the subcommittee felt were going beyond the scope of their legislative authority. Congress created those agencies for a specific purpose and some have gotten too independent.

Do you think that that might be a reason for some of the problems that you related in your paper, and as Professor Demsetz has also related?

Dr. MANNE. I think it is a tremendous problem. Agencies of various sorts developed, as I suggested, a kind of life and a lifestyle of their own.

They have become the most significant lobbyists, or at least among the most significant lobbyists, for their own interests and it is foolish not to think that agencies and the individuals within these bodies, do not have political interests just as clear as General Motors, or the UAW, or the petroleum industry, or anyone else.

They certainly do, and as they grow they tend to use their political power to improve their interest as they see it.

The effect of this, I find, is very often to go beyond what Congress normally intended. It is very difficult, then, for Congress to closely supervise the behavior of such agencies.

I happen to have studied most closely and do a great deal of my own research and writing in connection with one of the more obscure of the major agencies that; is the Securities and Exchange Commission.

I think in case after case I could document that that agency has gone beyond the powers that were given to it in the enabling legislation. And yet the cost to committees and to the Congress to constantly supervise and correct these departures from the power granted and intended in the initial legislation is far too great to warrant the policing.

It is a cost problem not totally unlike the matter of entry into an industry. As a result, these agencies can persist in a kind of war against one faction or another in the private sector.

Mr. CHUMBRIS. Thank you very much. Dr. Manne. There are many other things I would like to take up with you but we have a time limitation and we have more witnesses.

I would like to yield briefly, Mr. Chairman, to Professor Granfield for some questions.

Mr. GRANFIELD. Dr. Manne, you tell us in your paper that you see monopoly power in certain professional service organizations, grafting in the medical profession specifically, and you list some others.

Is there one aspect of this monopoly power that they all seem to have in common, or what is it that leads to the pervasive monopoly returns for them?

Dr. MANNE. I think it is quite clear. There is a single thread that runs through every one of the examples that I gave here and many others that I can name and that is a restriction on entry into the industry.

Now, in general, those restrictions will never survive without the force of the Government behind them, and in most cases they simply take the form of licensing of a profession or the necessity of a certificate of convenience and necessity or something of that sort.

However, in some cases it becomes somewhat more complicated, though the effect remains the same. Often, for instance, the Government, either through action or inaction, simply provides a situation in which private, coercive power may be used to restrict entry.

Mr. GRANFIELD. So you would agree with Professor Demsetz that one test of the pervasiveness of a monopoly is in terms of their entry.

I want to relate now, to this: to exit and entry. Economists tell us when there are true monopoly returns taking place, even in the short run. you should expect entry into the industry.

Similarly, if we see exits from the industry it must mean that monopoly returns, no matter what the accounting figures tell us, must not be occurring.

I refer specifically here to the computer industry. Recently it has been alleged that monopoly profits were being earned in the computer industry, yet we have seen significant exits from the industry on the part of ECA and GE, who when they exited claimed they were earning something less than monopoly profits.

Would you agree that this is an indication that there are probably not profits occurring in that industry?

Dr. MANNE. I think that is so.

An entire industry may decline to the point where only one firm is left. Well, by a somewhat older and I think today somewhat outdated definitions of monopoly, we would say that was a monopoly industry simply because there was only one firm left.

On the other hand, that would certainly be no cause for concern, since indeed, by hypothesis here, we have stated that the entire industry was declining to the point that it could only support one Industry.

If I recall correctly, there is, in fact, only one buggy whip company of any significance left in the United States.

Mr. GRANFIELD. One final question, which I think poses a very intriguing problem, is the relationship between political power and economic power and the purchase or the control of political influence, even with respect to partial monopolies such as tariffs or quotas.

Can you offer this committee an insight as to how a group effectively organizes itself to gain this kind of political power, what are the attributes of such a group, and what can it offer the political arena to gain this type of influence?

Dr. MANNE. I wish I knew the answer to that. I have no aversion to making money and I think if I knew how to do that I could become very wealthy.

We have seen some examples in recent years that are quite extraordinary in the methods used and the success they have had.

I have particular reference to the phenomenon known as Ralph Nader. Again, I think this is a demonstration that it is possible, when you have a powerful and unique individual with tremendous skill and confidence, to develop this kind of political organization.

One of the difficult problems, however, seems to be that the organizations tend to occur on one side of the political spectrum.

Again, I have not given much thought to this, but it is a matter that certainly would deserve greater attention.

It would seem to me that the interests of the public in gaining freedom from regulation and the inhibition of competition that both I and Professor Demsetz have referred to, somehow aren't protected.

Now, whether that is simply because the benefits are too diffused and the organization costs too high I don't know.

Mr. CHUMBRIS. Thank you, Mr. Chairman.

Senator HART. Your hesitancy to attempt to explain why any political force either succeeds or fails, your inability to answer that, I am sure doesn't give you any discomfort or shouldn't.

Nobody has ever really figured out how it works. I am trying to think of a relatively neutral area.

Dr. MANNE. I might even add that perhaps it is politically safer that we don't know how that happens. It seems to occur in almost random fashion, where organizations at some point, certainly are formed to answer felt-or-expressed public concern.

It might be unfortunate if we knew how to manipulate the public so skillfully that anytime anyone could specify an interest, he could formulate such a group.

Senator HART. Well, I have gone in many audiences and asked if anybody was in favor of permitting children to go hungry and nobody has. Are you in favor of feeding the hungry children? Everybody is, so we aren't even able to do that which no one opposes and everybody favors. Why is that?

Dr. MANNE. Well, of course, there are still numerous questions of the methods to be used in allocating resources, the definitional problems, the responses of the individuals who are not involved directly in the process.

It is easy to say what you are in favor of.

Senator HART. Well, I cite the example only to highlight the enormity of defining what happens when you get into areas where there are people strongly for and strongly against.

When you move into that area then it is a small wonder we don't really know what makes it tick. Thank you very much, Professor.

Dr. MANNE. Thank you, sir.