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## **Monopolies versus the Free Market, Part 2**

**by Gregory Bresiger**

Why do some think that successful firms are inherently evil? Why do many antitrust regulators actually believe that any firms that report consistently high profits should be under review by government officials?

One part of the regulatory argument is that almost all big corporations can exercise quasi-monopoly powers. Economists such as Joan Robinson and Edward Chamberlain in the 1930s warned of the economics of “imperfect competition.” They also posited what they called “monopolistic competition.” This could happen whenever a company or an owner could give his product a unique advantage, they said, which could be anything, including a particular location.

The New Deal’s chief trustbuster, Thurman Arnold, accepted much of this concept of imperfect competition. “Mr. Arnold’s point,” said fellow New Dealer Raymond Moley, “seems to be that competition becomes unfair if one party has a well-known trade name, whereas a competitor has no such well-known name.”

Arnold, who was responsible for antitrust prosecution through much of the New Deal, also warned of “coercive advertising.” It was from here that one of the mainstays of antitrust thought developed. This is the so-called dependence effect. The most well-known advocate of this concept was the economist John Kenneth Galbraith, one of the most popular economics writers of our time. His writings were facile and often disparaged by many in the economics profession as superficial. Still, Galbraith is an easy read, and he had a remarkable ability to create bestsellers.

Under Galbraith’s celebrated dependence-effect scenario, consumers become suckers for the products of big corporations working in alliance with Madison Avenue. Consumers don’t buy things out of a spontaneous need, he wrote, but because producers “contrive” goods and services to meet their production goals. They trick people into thinking they need increasing amounts of superfluous goods. He wrote,

If production is to increase, the wants must be effectively contrived. In the absence of the contrivance, the increase would not occur. This is not true of all goods, but that it is true of a substantial part is sufficient.

Without salesmanship and advertising, he added, the marginal utility of these corporate goods would be “zero.” Yet it is easy to question whether the dependence effect really gives successful or dominant companies a stranglehold on consumer loyalties.

### **Dominance and the market**

In the high-flying world of mutual funds, it is often said of hot and cold funds, “And the first shall be last. And the last shall be first.” The same is true of any part of the business community in which market forces are allowed to operate with little or no interference.

Examples abound of corporations that at one time seemed to be the Wal-Mart or Microsoft of their time. Big, successful corporations seemed to impose the dependence effect on people. Yet today some big companies, such as GM and some of the airlines, are battling just for survival. Others, such as Woolworth’s and the Pennsylvania Railroad, are gone.

All of these one-time titans were brought low not by trust-busters but by competition, although certainly overregulation and imposed labor costs also played a part in their decline.

If these corporations ever had the quasi-monopoly powers imputed by Galbraith and many others, doesn’t it follow that they should all still be around and prospering? Indeed, Galbraith, whose theories were respectfully listened to by many in Congress and who tutored several presidents, nevertheless later hedged on this idea. Toward the end of his life, in a television interview with C-SPAN’s Brian Lamb, he conceded that he was surprised by the number of high and mighty American corporations that had gone under during the previous 30 or 40 years.

### **The Sherman Act**

Several of these flawed antitrust concepts are embedded in the first federal antitrust law, the Sherman Anti-Trust Act of 1890. It was a law born in nebulosity, which set the precedent for the many other antitrust laws that would follow. The cloudy nature of almost all antitrust law means, depending on the zeal of a particular attorney general, that today’s acceptable business practice can be the basis for tomorrow’s antitrust lawsuit.

The antitrust litigation can run decades and cost tens of millions of dollars, with the government sometimes just abandoning the lawsuit, as we learned with the antitrust case against IBM. The tens of millions of dollars spent on antitrust lawsuits ultimately is taken out of the pockets of the shareholders and the consumers.

Let us look at the language of the Sherman Act and the opaque and paradoxical nature of the wording:

“Every contract, combination in the form of a trust or otherwise, or conspiracy in restraint of trade” is illegal. But what, exactly, is “restraint of trade”? If Jewish storeowners in a neighborhood all agree not to open on Saturday, that will certainly restrain trade. But that won’t stop others from opening. And since this is a voluntary agreement, who is to say that one storeowner, whose business may be on the verge on failing, might not withdraw from the agreement? Moreover, if corporations A, B, and C agree to set a high price for a product, how do we know that a new business, corporation D, won’t suddenly come in and undercut all three?

Some 20 years ago the idea that a company called Microsoft would beat IBM was considered laughable. What was Microsoft? Who had ever heard of it? Yet everyone at that time knew that IBM was the 800-pound gorilla of the computer business. Those days are now long past. Many people who support vigorous antitrust efforts, who advocate more laws, don’t even know that this happened. Restraint of trade can’t envision all of the possibilities of competition today, tomorrow, and next year.

Another section of the Sherman-Anti Trust Act says that it is a crime to “monopolize or attempt to monopolize, or combine or conspire ... to monopolize any part of the trade or commerce among several states.”

One legal commentator, Lawrence M. Friedman, has called the language of this landmark law “vague.” He says the Sherman Act was “something of a fraud.” That’s because the concept of restraint of trade was not clarified. The law, he added, reflected “no particular economic theory.” It was merely designed to respond to complaints about the trusts of the late 19th century, just as some of the enforcement actions have been designed to respond to complaints about the biggest firms of today. Trustbusters tend to respond to political pressures, not to clear legal principles.

### **The fallacies of intervention**

More important, the Sherman Anti-Trust Act set a precedent that would be followed again when Congress confronted what was perceived as a problem, economic or otherwise.

Pass a celebrated law, and then basically walk away from the tricky, politically divisive issue. If the issue becomes politically hot again a few years later, then pass another law. Politics requires that the rulers always seem to be doing something. Doing nothing is never a viable option in the modern democracy.

How do lawmakers accomplish perfection by statute? Write the law in a manner so difficult to understand that administrative agencies can interpret it in countless ways. For example, Sen. John Sherman clearly had no intention of breaking up trusts. He wrote the following of the Sherman Anti-Trust Act:

This bill does not seek to cripple combinations of capital and labor, the formation of capital partnerships, or of corporations, but only to prevent and control combinations made with a view to

prevent competition, or for restraint of trade, or to increase the profits of the producer at the cost of the consumer.

Since there is no economic basis or logic backing the Sherman Act, monopoly law is based on an impossible dream of achieving economic utopia. It presupposes that regulators understand not only results of business activity but also the mindsets and motives of business people. The antitrust police also have the job of separating successful companies that have behaved legally from those that have conducted themselves illegally. At the same time, regulators must do all this in such a way as not to hurt consumers. Good luck!

Why should regulators do anything to combinations, when these often-temporary combinations also provide the consumer with the lowest possible prices? What happens when breaking up or punishing monopolies hurts the consumer? How does one know whether a business that cuts its price to the bone is trying merely to improve profitability or is engaged in a plan to put all competitors out of business? Why should it matter?

Monopoly law has no answer for these questions other than to invoke the repeated phrase “restraint of trade.” In fact, the history of federal regulation of trusts is a strange one. It is a history of the federal government’s helping some businesses at the expense of others. It is a story of the federal government’s actually encouraging some trusts and some businessmen to look to the federal government for favors.

Indeed, without the backing of the federal government, it is questionable whether there would have been as many trusts. For example, seven years after the Sherman Act was passed, a Republican Congress and administration endorsed the Dingley Tariff. This high-tariff law was designed to grant protection for “basic industries.” But what followed has been described as “the golden era of trusts” in America. This was an eight-year period between 1897 and 1904 when 425 trusts were organized, with a combined worth of some \$25 billion.

The federal government was creating trusts by giving favored corporations monopolistic positions. Yet this was an era when President Theodore Roosevelt was publicly celebrated as a trustbuster. More contradictions in American monopoly law were to follow.

There were also succeeding acts to the Sherman Anti-Trust Act, which furthered the contradiction of these confusing rules. For example, later antitrust laws, such as the Clayton Act and the Robinson-Patman Act, were “explicitly intended to restrict price rivalry in the name of competition,” according to one commentator, Dominick T. Armentano. But here again it was the consumer who was paying higher costs, which the original Sherman Anti-Trust Act was supposed to prevent.

These would-be monopoly-destroying laws appear to be based on a mistaken understanding of the nature of competition. Competition is no more perfect than human beings. Yet competition can take many forms. It can take place within an industry. It can take place

within a sector of an industry. It can take place within different parts of a firm. It is part of a discovery process that can include various firms that cooperate in the temporary pursuit of a common goal.

But even in the case of cartels that have been created without the support of the government, it is impossible to expect that all firms will agree at all times.

This was, for example, the case of several Eastern railroad executives who met in New York City in what would turn out to be a futile effort to fix prices. The so-called St. Nicholas Agreement of 1854 lasted barely six months because of “the inability of the roads to abide by the provisions,” according to one railroad historian. These railroads had sought to impose a dependence effect on their customers, but they failed.

### **Genuine monopolies**

Genuine monopolies are those enterprises that are protected from competition by force of law. If a competitor attempts to enter the market against the government-sanctioned enterprise, the government shuts him down.

A diligent student can search through history to find endless examples of pernicious state monopolies or government entities with quasi-monopoly powers.

For example, in the Case of the Monopolies of 1602, a British court ruled that an exclusive monopoly conferred by Queen Elizabeth for the manufacture of playing cards was against the common law, which protects freedom of trade and liberty of the subject.

Eight years later, in the celebrated Case of Dr. Bonham and four years after that, in the Case of the Tailors of Ipswich, the Court of Common Pleas ruled against a state-sponsored guild that tried to prevent people from practicing a trade.

“The Common Law doth abhor all Monopolies, which forbid any one to work in any lawful Trade; ... That at the Common Law no man might be forbidden to work in any lawful Trade, for the law doth abhor idleness, the mother of all evil,” wrote Lord Edward Coke. Coke’s ideas of government under law helped defeat divine-right monarchy and led to the constitutional settlements of the Glorious Revolution of 1688.

America’s Founding Fathers were astute students of Coke and the English Whig tradition. But this suspicion of state control of the economy — like the rest of the American classical-liberal tradition — has obviously been in retreat for more than a century. In part this is because millions of state-educated Americans know little or nothing about the libertarian tradition that enunciated and guaranteed the freedoms associated with the right to own property, a basic human right. So Americans simply take liberty for granted, or don’t understand its myriad virtues.

Perhaps the granddaddy of the American state monopoly is the United States Postal Service. The system is in reality devoted to the principle of not allowing others to do a better job. Or as James Bovard has written,

America's postal system is based on the idea that it is better to trust a public monopoly to provide service out of its sense of obligation than to trust companies to provide good service out of sheer necessity — that an organization is more likely to serve the public when it has no competition and a guaranteed income than when it must fight for customers.

The Postal Service zealously protects its legal monopoly in the delivery of first-class mail. And woe unto the children who deliver Christmas cards for less than the government monopoly price. The police powers of the state will come down on them heavily.

A Chinese economist has labeled a government-backed monopoly as an “administrative monopoly.” He says it is “a group-based corruption” protected by laws. Many people can agree with this sentiment in theory but carrying it out is another thing. Expecting a state monopoly to break itself up is as logical as expecting a tyrant's mea culpa. It isn't just the state monopoly itself that is the problem; it is also the friends in high places that ensure that state monopolies go on and on.

When, for example, can one remember a recent serious effort in Congress to take away the monopoly powers of the postal service? That's because many of the members of Congress receive financial help from the postal unions, whose membership numbers in the hundreds of thousands. Those unions represent a formidable force against competition. As is customary with monopolies, the status quo is beneficial for monopoly employees — it provides them better pay and benefits than they might obtain in the competitive private sector. And those who work for the Postal Service know that if first-class mail delivery were ever opened to the private sector, the postal monopoly's stability and viability would inevitably be threatened.

In the end, anti-monopoly laws are more than counterproductive. They are, and will always be, harmful to a free-market economy and, more fundamentally, to a free society. There is only one reasonable anti-monopoly policy: End government monopolies and repeal anti-monopoly laws.

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