



中華人民共和國香港特別行政區

Hong Kong Special Administrative Region of the People's Republic of China



立法會 LEGISLATIVE COUNCIL

葉劉淑儀 議員 GBS, 太平紳士 Hon Mrs Regina IP LAU Suk-ye GBS, JP

Hon Andrew LEUNG Kwan-yuen, GBS, JP
Chairman, Bills Committee on Competition Bill
Legislative Council
8 Jackson Road
Hong Kong

5 July 2011

Dear Andrew

The Myth of Competition Law

Further to our recent discussions at meetings of the Bills Committee on Competition Bill, I attach copies of two articles named "The Myth of Competition Law" and "The Antitrust Emperor's Clothes" which appear in *Best Practice - a Public Policy Journal for Hong Kong* in May 2011 (Vol. 3 No. 2).

The former article clearly sets out numerous reasons why competition law may not create a better business environment as we thought. Higher compliance costs and higher political risk will likely undermine the competitiveness of Hong Kong enterprises. These concerns are echoed by many celebrated economists, such as Alan Greenspan and Ronald Coase.

In the latter article, the writer traces the history of antitrust law in the United States and demonstrates the causal relationship between strict enforcement of competition law and economic downturn. In his analysis, the enforcement of antitrust law is more often than not subject to ever-changing political atmosphere. The object of consumer protection as the emperors' new clothes is rarely achieved in reality. In addition, antitrust lawyers and law consultant companies are often the most active interest groups lobbying and pushing the Administration and the Congress to enforce the law strictly.

These two articles are extremely valuable in reminding us that competition law may not in practice be the best means of promoting competition as many imagine. Although not every member of the Bills Committee may agree with the standpoints, the arguments are well worth our consideration.

Yours sincerely,

Mrs. Regina Ip

The Antitrust Emperor's Clothes

George Bittlingmayer advocates basing policy on what we know

Antitrust policy is on a better footing today than it was 25 years ago, but it still shares some features with the story of the emperor's new clothes. The tailors of antitrust policy tell us that the antitrust laws are the "Magna Carta of free enterprise," that they protect consumers against the conspiracies and depredations of business. Despite mistakes that we can ignore, the proponents say, the well-intentioned antitrust endeavor has improved U.S. economic performance by suppressing collusion and serving notice that firms may use only fair means to attain or protect a monopoly. The courts and the agencies did get a little out of hand in the 1960s and '70s, but a bipartisan consensus has emerged that keeps monopolies in check, they say reassuringly. You do see, ask the tailors, that a broad variety of suspect but otherwise legal business behaviors can hurt consumers? More importantly, you do see that our antitrust laws have increased our standard of living?

"Yes" is a tempting answer for a variety of reasons, none very good.

Stepped-up enforcement also occurs at the end of protracted booms; in fact, it helps explain why booms end.



The fear of powerful, unseen forces and conspiracies runs through human history. In addition, losers and those who fear they may be losers prefer to put the blame on others rather than their own bad luck or bad planning. Finally, as

we know from the story of the emperor's new clothes, only the naïve or courageous are prepared to admit that they do not see what the experts claim as fact. The antitrust bar, law professors, antitrust officials, economic consultants, and firms anxious to see brickbats thrown at their competitors maintain a steady drumbeat for their own versions of vigorous enforcement.

Despite the drumbeat, the

empirical case for antitrust remains weak. We know that polio vaccine effectively eradicated polio; we do not know that the antitrust laws have made us better off. Twenty years ago, George Stigler wrote: "There have been no persuasive studies of the effects of the Sherman and Clayton Acts throughout this century." Little has changed. The antitrust experts may be having fun, but the clothes they have draped on the emperor are threadbare at best.

MAGNA CARTA OR POLITICS AS USUAL?

One myth needs immediate debunking: Antitrust law was not a response to textbook monopoly. Rather, it was a response to disruptive technologies and new forms of business that arrived thick and fast in the late nineteenth century. For example, centralized meatpackers put local slaughterhouses under competitive pressure after the invention of the refrigerated railcar. Similarly, Standard Oil pioneered the use of tank cars to transport petroleum, putting pressure on refiners that shipped oil in barrels. Analogous stories played themselves out in dozens of industries. In a seeming paradox, firms in those industries often formed "trusts," "pools," and other cartel-like arrangements.

Many of the classic "trust" industries also pioneered the modern corporate form. When Congress passed the Sherman Act in July of 1890, fear of disruption, low prices, and new, larger forms

of business organization were as much in the air as fear of high prices. Tellingly, Congress passed the McKinley Tariff (with a rate of almost 50 percent) only a few months earlier – the opposite of what one would expect from a champion of consumer welfare.

Sherman Act as inapplicable to acquisitions via stock purchases. After Teddy Roosevelt attacked an unpopular railroad consolidation, it narrowly reversed itself in 1904. Similarly, the court created the per se rule against price fixing in the mid-1890s, but abandoned it just

The fear of powerful, unseen forces and conspiracies runs through human history. In addition, losers and those who fear they may be losers prefer to put the blame on others rather than their own bad luck or bad planning.

A second myth also requires attention. The courts have not interpreted antitrust law – whatever its origins – selflessly and in a political vacuum. Rather, they respond to political pressure and, like all bureaucracies, protect their turf. For example, the Supreme Court originally viewed the

months before passage of the 1933 National Industrial Recovery Act, which encouraged industry-wide agreements. In 1950, Congress closed a loophole in merger law, but did so against background rhetoric about a "rising tide of concentration." The courts listened and came down hard on mergers.



Halting business

Antitrust enforcement is capable of affecting economic activity, and it seems to respond to economic conditions. The most dramatic example involves Teddy Roosevelt. His attack on Standard Oil and other large corporations coincided with the Panic of 1907, and Roosevelt's critics, and indeed many of his friends, claimed that his attacks caused the panic. It was not a farfetched charge – a wildly popular president threatened to dismantle the country's largest corporations and send top corporate officers to jail. In 1911, President William Howard Taft's pursuit of U.S. Steel also coincided with a recession and similar charges. In fact, Taft conceded that his policies "may make business halt."

In the late 1930s, the failure of the economy to come out of the Great Depression led the FDR administration to charge that the

Both books took the then-controversial view that the antitrust laws should promote economic efficiency or consumer welfare, rather than protect small traders and worthy men besieged by more efficient organizations. Both books also employed a crisp intellectual approach.

"bottlenecks of business" – large corporations and their allegedly anti-competitive practices – prevented recovery. The result was Thurman Arnold's legendary antitrust campaign and the Temporary National Economic Condition (TNEC) hearings. Ironically, the attack coincided with the 1938 recession within-a-depression.

Stepped-up enforcement also occurs at the end of protracted booms; in fact, it helps explain why booms end. Examples include Teddy Roosevelt's trust busting after the late-1890s expansion and Hoover's revival of antitrust in 1929 amid cries of "profitless prosperity" from declining sectors. Antitrust revivals also occurred at the end of the 1980s and again at the end of the 1990s.

Economic pain, either from a stagnant business climate or from the dislocations and envy of a tumultuous boom, may generate stepped-up attacks on business, especially successful business. Disruptive antitrust cases may cause a decline in business spending. Finally, stepped-up

attacks on business may simply be a collateral symptom of bad economic policies. None of those possibilities offers support for aggressive enforcement.

FROM WIN-BUTTONS TO MEGA-MERGERS

The most conspicuous economic problem in the 1970s was inflation. It provoked a variety of non-monetary policy responses, some harmful, some merely comic. The responses included wage and price controls under Richard Nixon, "Whip Inflation Now" win-buttons under Gerald Ford, and the "Tax-Based Incomes Policy" that would have conferred tax rebates on corporations that held the line on wage increases under Jimmy Carter.

Both Ford and Carter, clearly grasping at straws to deal with inflation, advocated aggressive antitrust enforcement. Antitrust officials Thomas Kauper and John Shenefield at the Department of Justice (DOJ), Michael Pertschuk at the Federal Trade Commission (FTC), and others invoked the fight against inflation to justify vigorous

Ray Leung



enforcement. The DOJ pursued two major monopolization cases, one filed in 1969 against IBM and one filed in 1974 to break up AT&T. The Justice Department also pursued "price-fixing" cases against manufacturers that tried to keep their products out of discount channels. Levi Strauss was one of the targets. The FTC, not to be outdone, filed a series of "shared monopoly" cases that sought to break up or radically reconfigure the petroleum and breakfast cereal industries. The latter case was based on the proposition that companies could stifle competition by introducing too many brands. The commission also filed a monopolization case against DuPont, charging that the company had built a titanium dioxide plant that was too large and too efficient.

The antitrust agencies also showed a special interest in agreements involving intellectual property. For example, the DOJ sued to break up a cross-licensing agreement among aircraft manufacturers. Ironically, the industry had formed the agreement nearly six decades earlier at the urging of the government because patent litigation had made manufacturers reluctant to build airplanes during the First World War. The Justice Department summarized its approach to patent licensing in its legendary "Nine No-no's," a term the agency used without apparent irony.

One bright spot for business was the Hart-Scott-Rodino Antitrust Improvements Act of 1976, which

provided for pre-merger review. Until then, the agencies often filed suit against consummated mergers and sought divestitures, a costly route for all involved. The filings often came months or years after the merger, and the divestitures years after that. The modern regime eliminated indefinite jeopardy and litigated divestiture in merger cases.

New learning, new policies

The activism of the 1970s did not play well on Main Street and in corporate offices. Complaints moved the Democratic Congress to threaten to shut the FTC down, and the agency had to close its doors briefly in 1980.

Among academics, a steady and growing stream of analysis eroded the near-consensus for strict enforcement. The 1974 publication of *Industrial Concentration: The New Learning*, edited by Harvey Goldschmid, H. Michael Mann, and Fred Weston, reflected the shift in opinion on the economic role of large firms. Legal commentary showed similar changes. Richard Posner published *Antitrust Law: An Economic Perspective* in 1976 and Robert Bork's *Antitrust Paradox: A Policy at War with Itself* appeared two years later. Both books took the then-controversial view that the antitrust laws should promote economic efficiency or consumer welfare, rather than protect small traders and worthy men besieged by more efficient organizations. Both books also employed a crisp intellectual approach.



The courts also began to reverse some of the restrictive holdings of the 1950s, '60s, and early '70s. Ronald Reagan's victory in 1980 gave new momentum to laissez-faire policies. Reagan's appointment of William Baxter to head the DOJ's Antitrust Division and James Miller to chair the FTC moved the agencies in a new direction.

By any measure, 1982 was the watershed year. In January, the Department of Justice abandoned the IBM case and signed a consent decree with AT&T, stipulating a voluntary divestiture. The FTC dropped its "shared monopoly" case against the cereal companies. The DOJ's 1982 "Merger Guidelines" provided stability and structure for merger review, especially when coupled with the existing pre-clearance process. The Merger Guidelines, since revised several times, have proven crucial in taming merger review. The antitrust agencies also scaled back new large-firm monopolization cases, filing only three over the years 1981-1988, a historical low. Those cases also sought conduct remedies rather than divestiture. Only one area experienced notably greater enforcement – horizontal agreements, often bid rigging and related offenses.

One point deserves emphasis: A new generation of academic

commentary supported and infused the shift in policy in the early 1980s, but the old and the new approach to antitrust analysis shared a defect that plagues policy analysis to the present day. Both approaches used a combination of abstract reasoning and case study. The new Chicago approach strove for consistency and economic rigor. In the battle of theories, it was fortunate in the enemy it faced. However, its advantage soon dwindled. A new generation of mathematical models – often based on game theory – lacked the obvious flaws of earlier ad hoc explanations but was flexible to a fault and could easily explain any type of business behavior as anti-competitive. Because the debate stayed conceptual rather than empirical, the new models ultimately gave new wind to enforcement across a broad variety of alleged offenses.

New policies, new results

The shift in policies in the early 1980s offers a natural experiment with a clear result: Merger activity picked up. For example, a series of mergers previously unimaginable changed the face of the oil industry. T. Boone Pickens drove calcified Gulf Oil into the arms of Chevron, and Texaco acquired Getty Oil in 1984.

Related developments – in particular changes in takeover law and the development of junk bond financing – contributed to the merger wave and also encouraged management buyouts and

leveraged buyouts. The most visible deal was Kohlberg Kravis Robert's \$31 billion leveraged buyout of RJR Nabisco in 1988, an event later portrayed in unflattering detail in the book *Barbarians at the Gate* and in a movie starring James Garner. The buyouts contributed to our understanding of how changes in control can improve economic and financial performance. Additionally, though the other transactions did not raise traditional antitrust flags, they provided fuel for the coming political reaction to mergers and other forms of restructuring.

The simultaneous appearance of less stringent merger policy, a merger boom, and an economic boom is a familiar pattern in U.S. history. Outright suspension of merger enforcement in the late 1890s and effective suspension in the mid- and late 1920s under Coolidge coincided with a merger wave and an economic boom. That raises the possibility that a generous merger policy is good for the economy. Clearly, other related developments had an influence on

the economic climate of the 1980s, chief among them the decline in the inflation rate. But given historical experience, it seems unwise to rule out merger policy.

Several mechanisms are possible. Henry Manne's 1965 article "Mergers and the Market for Corporate Control" argues that companies in the same industry are in the best position to identify and run poorly managed firms. Horizontal mergers and the possibility of takeover would increase output and the value of existing assets. To the same effect, Lester Telser views mergers as facilitating the transfer of intangible capital across firms. Removing the obstacles to transfers leads to greater output. Finally, a less restrictive merger environment opens up more exit strategies for firms, thus increasing entry, investment, and firm value. Although some critics claim that 1980s merger policy was too lax, I know of no systematic body of evidence showing that consumers were harmed.

In each instance, the case for antitrust action was speculative and eminently susceptible to critique. Perhaps more importantly, the cases plausibly signaled to business that the agencies had become or were about to become untethered again, as they had been in the 1970s and at other times.

THE ANTITRUST EMPIRE STRIKES BACK

Antitrust lawyers complained about Reagan's antitrust policies from their very inception, and have consistently lobbied for stricter enforcement. Tellingly, they did not argue that restrained enforcement made consumers demonstrably worse off; rather, they wanted policy that was less "ideological" and that "enforced the law" by filing types of cases that the Reagan officials ignored.

Milton Handler, an influential antitrust lawyer whose career spanned six decades, complained about the "lawlessness of this administration," saying, "The government is not merely failing to enforce the law, it is changing it unilaterally." Ira Millstein incongruously complained, "Business in general feels that no one is going to enforce the antitrust laws anymore. That makes counseling and voluntary compliance with the law much more

Milton Handler, an influential antitrust lawyer whose career spanned six decades, complained about the "lawlessness of this administration," saying, "The government is not merely failing to enforce the law, it is changing it unilaterally."

difficult." Without enforcement, counseling and compliance are not unnecessary. A former Democratic antitrust official, perhaps hoping for more business, called the Reagan administration's record "nothing short of pitiful." Thomas Krattenmaker and Robert Pitofsky lambasted the Reagan administration's antitrust record because it had challenged very few of "an unprecedented wave of mergers." Separately, Pitofsky conceded that those facts alone did not prove or imply that merger enforcement had been misguided.

The American Bar Association summarized the complaints of antitrust lawyers in a 1989 task force report on antitrust enforcement that requested more resources for the DOJ's Antitrust Division, an end to the division's advocacy of reform, and an end to "non-enforcement rhetoric." The report urged more case filings, more monopolization cases, and more vertical-restraints cases, without the least evidence that consumers had been hurt.

Congress was also unhappy with less stringent enforcement and the wave of mergers. Senator Paul Simon (D-Ill.) complained in

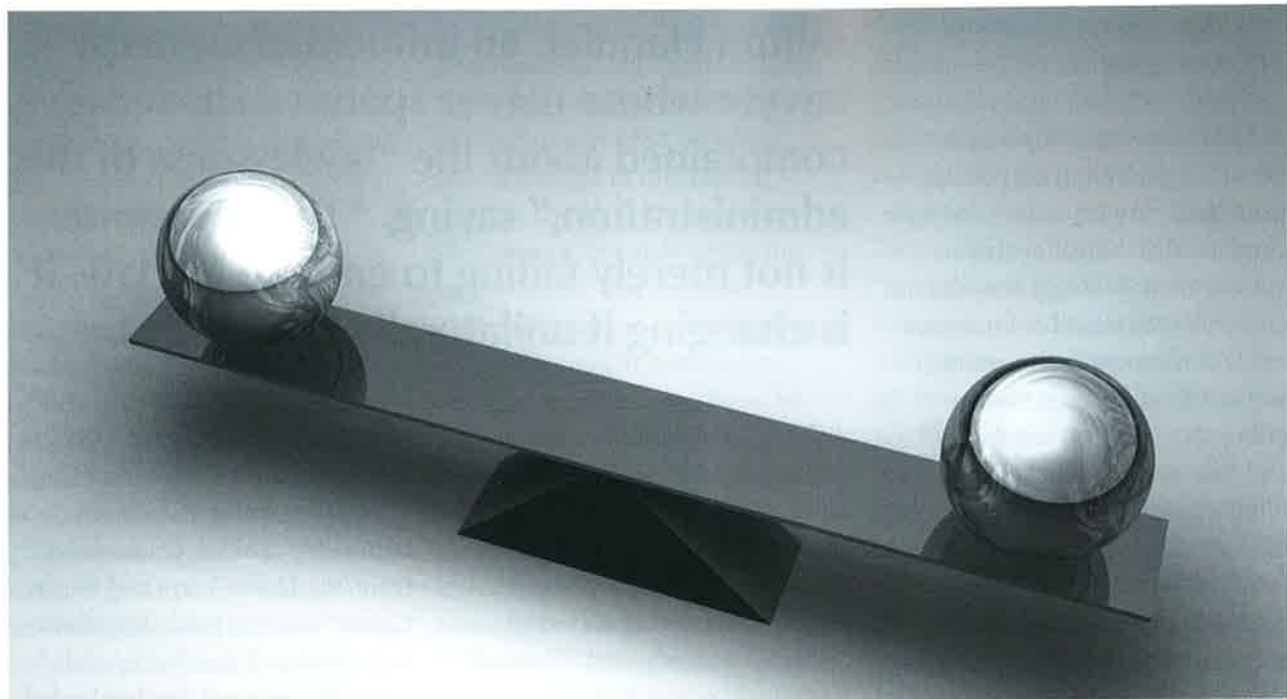
hearings on the Antitrust Division that "antitrust lawyers are closing up shop," seemingly oblivious to possible upsides. On a related front, the House Ways and Means Committee approved anti-takeover legislation and then backpedaled when the proposal was implicated as a precipitating factor in the October 1987 stock market crash – a suspicion later confirmed in academic research.

Billable hours

In the late 1980s, newly elected President George H. W. Bush installed a group of antitrust officials who signaled "more vigorous enforcement." He appointed James Rill, a 25-year veteran of the antitrust bar, to head the Antitrust Division. Sen. Howard Metzenbaum, a critic of Reagan-era enforcement, hailed the appointment as "a signal that President Bush intends to break stride with his predecessor." Bush also appointed Janet Steiger, formerly chair of the Postal Rate Commission, to chair the FTC. She also offered tougher talk.

Cases and investigations soon followed. In many instances,





the harm to consumers from challenged business behavior was speculative at best. The DOJ filed a case against the Ivy League colleges in 1989, claiming that their "Overlap Group" financial aid practices represented a restraint of trade. Twenty schools had agreed to offer identical financial aid packages to commonly accepted students. Upper-middle class parents of very good students were hurt, but plausibly students with less affluent parents were helped. Because the challenged arrangement involved price discrimination by a non-profit, the question of who benefited was a little slippery. (One was suggested that monopoly gains went to administrator salaries.) On any view, elimination of the Overlap Group agreements merely represented a reshuffling of the extensive price discrimination and

cross-subsidization that universities of all types continue to practice.

The Justice Department also began an investigation of airline pricing in 1989 that culminated in a December 1992 case filing. The allegation was "price-fixing," but the airlines had no meeting of the minds. Rather, they had merely posted current and future prices on airline reservation systems, an ambiguous practice at worst.

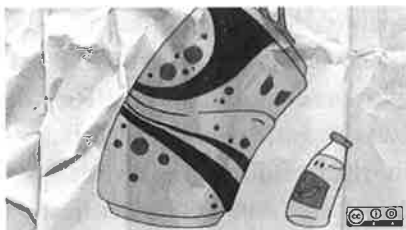
Mere investigations without filings also send signals. In the "keiretsu" probes, both antitrust agencies moved beyond consumer protection by looking at arrangements in Japan that allegedly kept U.S. auto suppliers from doing business there. *The Washington Post* called the probe "loopy and dangerous." A spike in oil prices accompanying Iraq's 1990 invasion of Kuwait led to the inevitable DOJ investigation of the

oil industry, though the industry had been turned inside out and found clean several times over the preceding two decades.

The FTC pursued high tech targets, investigating both Microsoft and Intel. It eventually dropped the Microsoft investigation, and its interest in Intel resulted in a 1999 settlement and a second investigation that the agency dropped in 2000. The FTC filed a case against infant formula makers in 1991 that was reminiscent of 1970s "shared monopoly" suits. Two defendants settled. The third, Abbot, was vindicated in court in 1994.

The FTC also returned to filing vertical-restraints cases, charging swimming pool equipment maker Kreepy Krauly with "price fixing" because it sought to prevent discounting of its pool vacuum cleaners. The market for swimming

Libby Levi



Corporations have been found to use antitrust law to target competitors.

pool vacuums is hardly a prime candidate for monopolization, and an excellent candidate for the "special services argument." Point-of-sale promotion is hard to charge for, and discounters can easily free-ride on the promotional efforts of full-price retailers. The FTC joined state attorneys general in charging Nintendo with "price fixing" in a case settled in 1991. The agency later dropped a separate investigation of Nintendo's product design and licensing practices.

In each instance, the case for antitrust action was speculative and eminently susceptible to critique. Perhaps more importantly, the cases plausibly signaled to business that the agencies had become or were about to become untethered again, as they had been in the 1970s and at other times. Conceptually, it was not a big leap from the investigations' actual cases filed under the first Bush administration to the "shared monopoly" cases filed against the oil and cereal companies.

In general, the Bush administration's domestic policy apparatus appeared to be on automatic pilot, guided by Republican mandarins headed for the revolving door rather than

by an over-arching economic vision. In desperate straits, the Bush administration itself implicitly conceded the point when it imposed a "regulatory moratorium" in early 1992 ahead of the presidential election and at the bottom of the 1991-'92 recession. If that downturn was a "regulatory recession" as some critics claimed, Bush's antitrust authorities may have done their part to bring it on.

BIPARTISAN CONSENSUS OR CONSPIRACY AGAINST THE PUBLIC?

Bipartisan consensus on antitrust is the rule. Unfortunately, consensus is no guarantee against foolishness. In the 1912 election, both Woodrow Wilson and William Howard Taft took the view that the only good trust was a divested trust. The economy suffered until U.S. entry into World War I,

defend and no one would work to recreate today.

Since the struggle to redirect policy in the 1980s, successive leaders in the antitrust agencies have again demonstrated a disturbing coziness. Antitrust officials write papers and give speeches with titles indicating an entrenched and sterile harmony: "The Essential Stability of Merger Policy in the United States" (FTC Commissioner Thomas B. Leary) and "Antitrust Enforcement at the Federal Trade Commission: In a Word – Continuity" (FTC Chair Timothy J. Muris).

The consensus on antitrust arises from both fear and greed. The public fears monopoly, and rightly so. Consensus means neither major party looks soft on monopoly. A cop on the beat has appeal, even if the cop has no idea who the crooks are.

Fear of monopoly is also easily exploited and diverted to serve private interests. In the 1970s, the

The Microsoft case also raises a riddle, discussed by Milton Friedman and others: Why does the business community support policies that seemingly have more long-term costs than short-term benefits.

when the Wilson administration backed off on business in return for help with the war effort. More recently, over the years that span from Eisenhower to Carter, both Republicans and Democrats pursued an aggressive policy, but the result was a policy few would

antitrust cops went too far, pistol-whipping suspects at random. Although the antitrust bar prospered, political support eroded. The reforms of the 1980s showed how the consensus could be rebuilt. The party in power allows the antitrust bar to collect a large part

of its implicit regulatory tax by guiding firms through a structured but complex merger review process and brokering consents. Tamed antitrust also serves other constituents. For example, Jesse Jackson's Citizenship Education Fund initially opposed the SBC/Ameritech deal but then shifted its position after SBC made a \$500,000 contribution to the fund and agreed to sell a seven-percent share of its cellular operations to a black businessman. (The example is slightly flawed because Jackson voiced his complaints at the Federal Communications Commission.) The post-1982 merger process avoids the political and economic costs of bitter battles over divestiture, still allows various influential constituents to get in the loop, and keeps the cop reassuringly on the beat.

Over time, the ratio of public fear to private greed has probably declined. We have learned to live with big business, and have seen by the examples of Microsoft, Wal-Mart, and Intel on the one hand, and General Motors, U.S. Steel, and ITT on the other, that alleged dominance is not all it

was cracked up to be. In addition, with the secular increase in direct or indirect stock ownership, an attack on business has become an attack on the public. We have met the alleged monopolists, and they are us. However, the contrary forces that led to the antitrust adventure of the 1970s remain and have reasserted themselves. Starting with the first Bush administration, both Republican and Democratic administrations have shown troubling initiative. New guidelines, new competitive theories, and new types of cases strengthen the power of the agencies, mollify Congress, offer levers to interest groups eager to use the regulatory process for their own ends, and provide officials and staffers with valuable human capital for future private-sector employment.

Innovation markets

An ever-greater share of economic activity involves intangible assets, technology, and intellectual property. Antitrust authorities, the antitrust bar, and economists eager to establish their credentials have noticed that trend and

adapted their arguments and claims to competence.

Technology and information-based industries lead to situations in which traditional antitrust approaches based on price effects and market shares do not apply. If two firms are engaged in similar research but do not yet have viable products, should the government block or force modifications to their merger, joint venture, or licensing agreement? The agencies and many antitrust theorists answer affirmatively. Under the concept of "innovation markets," they argue that they can predict which deals ultimately will lead to less innovation and some combination of poorer products and higher prices.

Interestingly, some representatives of the antitrust industry – attorneys and economic consultants – are skeptical and argue that the resulting analysis would be slippery and speculative. A sound business reason for that position is that giving advice and litigation support is fraught with hazard in an innovation market. Additionally, enthusiastic application of the concept may lead to a repeat of the "shared monopolies" fiasco and political backlash of the 1970s.

Mergers

As advertised by the agencies, merger policy for bread-and-butter mergers has been remarkably stable. Merger policy was particularly generous in the telecom area. The proximate



origin of that generosity was the 1996 Telecommunications Act, which sought to encourage inter-modal competition (say between telephone companies and cable TV companies). A Washington insider's view is that the Telecom Act put Congress back in the loop and led to an inflow of campaign contributions from the telecom companies. A succession of large deals followed – the consolidation of the Baby Bells, large cable acquisitions by AT&T, and the AOL / Time Warner merger, for example. The AOL / Time Warner merger raised no horizontal issues, but entailed a large and politically



When the agencies opposed mergers, reasonable observers could disagree about the prospective effects. The Justice Department opposed Microsoft's acquisition of Intuit even though Microsoft agreed to divest its own money-management software.

In theory anything is possible, and the blackboard debate about the effects of Microsoft's actions remains a stalemate. Microsoft is hard to love, but software and applications are winner-take-all products, so somebody had to be on top.

sensitive vertical merger. The "open access" debate was in full swing and Internet service providers competing with AOL feared they would be excluded from Time Warner's cable-based broadband. Defense mergers also faced a low hurdle, with the Defense Department often urging and even subsidizing consolidation in the industry. (The exception was the blocked Lockheed Martin / Northrop Grumman merger opposed by both the Defense Department and the DOJ.)

The effects of the deal hinged on whether consumers are better off having Microsoft's deep pockets, execution skills, and aggressive strategy behind the category leader at a time when Internet banker was a possible "killer app." The FTC blocked Staples' move to buy Office Depot although the two jointly had less than six percent of the total office supply market. The strength of the FTC case depends on one's willingness to view office superstores as a separate market. When World-Com proposed to

merge with Sprint in the fall of 1999, fears of monopoly in long-distance seemed quaint. They have become quaint still. The deal was in trouble at the European Union, and U.S. antitrust authorities found an opportunity to oppose a telecom deal without actually affecting its outcome.

Microsoft

The May 1998 case filing against Microsoft represented a return to large-firm monopolization cases. The Justice Department charged Microsoft with a variety of monopolistic practices, chief among them Microsoft's effort to displace Netscape's Navigator as the most popular Internet browser. In theory anything is possible, and the blackboard debate about the effects of Microsoft's actions remains a stalemate. Microsoft is hard to love, but software and applications are winner-take-all products, so somebody had to be on top.

Off the blackboard, the facts favor the "anti-anti-Microsoft" view (Paul Krugman's term). The government's case was marbled with political calculation and posturing. Strong political support came from California and Utah, home to major competitors to Microsoft, and participation of 18 state attorneys general complicated settlement and likely led to the proposed and ill-fated divestiture remedy. Taken as a package, the case generated uncertainty in the industry, consumed time and energy, and raised legitimate fears about where antitrust policy in

general would go. (See "All the Facts that Fit," Winter 1999.)

The stock market provides evidence for that view. Throughout the 1980s, antitrust actions directed against Microsoft pushed down not only Microsoft's stock price, but also the stock prices of its putative victims. Setbacks for aggressive actions against Microsoft had the opposite effect, helping both Microsoft and the rest of the computer sector. That should have been a signal to the DOJ. Disaster struck in April 2000 when settlement talks collapsed and news leaked two weeks later that the government-plaintiffs would seek divestiture. NASDAQ shuddered and began a long descent. Tech stocks probably were oversold and over-believed, but the attempt to break up one

The Microsoft case also raises a riddle, discussed by Milton Friedman and others: Why does the business community support policies that seemingly have more long-term costs than short-term benefits?

THE END OF ANTITRUST HISTORY?

Antitrust policy over the last 25 years can claim substantial achievements. First, the stated terms of the debate have shifted to consumer welfare and efficiency, and away from vague and easily misused goals such as dispersion of political and economic power. Clearly, affirmation of the stated goals may still go hand in hand with the misuse of antitrust laws to clobber competitors or extract

Taken as a whole, the 1980s shift yielded dividends. It helped slay the conglomerates, themselves partly the progeny of strict prohibitions against horizontal mergers in the 1950s and '60s. The policy shift also deserves credit for a more efficient corporate sector and quite plausibly an expanding, dynamic economy and a booming stock market. It does not appear to have caused or fostered monopoly.

The antitrust pendulum has swung back since the late 1980s, and a new bipartisan consensus has emerged under the Clinton and the two Bush administrations. The basic merger regime has remained stable, but other aspects of policy – notably large-firm monopolization cases – represent a partial return to the 1970s. That movement took place at the behest of identifiable private and political interests, in particular the private antitrust bar and the managers of aggrieved competitors, but benefits to the general public remain speculative.

More gains are possible if we learn more about what antitrust policy has done in practice, rather than relying on the antitrust tailors to tell us what is fact and what is not.

© Cato Institute. All Rights Reserved. Reprinted with permission.

George Bittlingmayer is the Wagon Distinguished Professor of Finance at the University of Kansas and is a former visiting economist at the Federal Trade Commission.

Under the concept of "innovation markets," they argue that they can predict which deals ultimately will lead to less innovation and some combination of poorer products and higher prices.

of the big names was a totally unnecessary and costly blow. As in other historical episodes in which downturns and trust busting coincided, it is hard to quantify the financial and economic effects. But it seems unlikely that the Microsoft case has made the U.S. economy wealthier and more productive. (See "The Benefits of MS-Settlement," Spring 2002.)

tribute. Second, the 1982 and subsequent Merger Guidelines and the Hart-Scott-Rodino review process provide safe havens, comparative predictability, and effective protection against suits filed after a deal is done. Third, the agencies still file large-firm monopolization cases as illustrated by the Microsoft case, but they have done so less frequently.

The Myth of Competition Law

The Lion Rock Institute argues that behind the curtains, there is no empirical proof that Competition Law can deliver a better environment

Phil Roeder



The nine chairs of the Justices lined up in the Court Chamber.

Ronald Coase [1991 Nobel Prize in economics] said of competition law, “when the prices went up the judges said it was monopoly, when the prices went down, they said it was predatory pricing, and when they stayed the same they said it was tacit collusion.”¹

William M. Landes in “The Fire of Truth: A Remembrance of Law and Economics at Chicago,” JLE (1981) p.193.

WHY COMPETITION LAW ISN'T ALL THAT IT SEEMS

Not one would disagree with the objectives that competition promotes a flexible, innovative, efficient economic structure, but there is no reason to believe that competition law can deliver these outcomes. Whether broad or limited, competition law faces the following challenges:

- 1 It is unclear whether competition laws have actually aided residents, businesses and consumers, but it is clearer that the laws can become sclerotic and politicized. The benefits to residents remain unclear while there are considerable risks and high costs.
- 2 The implementation of competition law in advanced economies are often cited as an ideal to be emulated,

but it should be noted that these same economies do not receive as high rankings in renown international indexes of economic freedom as Hong Kong, which does not have a widely-applied competition law.

- 3 The cost of doing business in Hong Kong has remained relatively low. However, the costs of compliance, with a broad and by its nature expansionary competition law, are very high. Competition laws must be studied by legal professionals and economists, and businesses will need to seek legal advice to ensure compliance, necessitating large cost increases.
- 4 Other jurisdictions such as the UK and the EU maintain their competition regimes at a cost of millions of dollars a year in their respective currencies. A more expansive competition law will inflate both the size of the Hong Kong Government, and costs to maintain the new policy regime.
- 5 The Competition Bill contains numerous broad and vaguely-

drafted provisions pertaining to economic terms, however these terms cannot be confined to strict definition as they describe innate, ever-changing and dynamic activity in open and free markets like Hong Kong. Vague laws dramatically increase uncertainty, litigation, bureaucratic power, and compliance costs because businesses do not know precisely what behavior is permitted until put on trial.

- 6 In Hong Kong, the biggest monopolist is the Government itself. A Competition Bill would have no effect, given that distortions in competition are created by the Government.

Without empirical proof of benefits from the law, the opportunity and compliance costs, along with the legal and defense costs, are unfair to impose on a public who is increasingly skeptical that such a law can enhance their lives. The discussion considering competition should focus on dismantling Government interference in the economy to improve competition--

not exempt it. The Government is the designer of Hong Kong's Competition Bill, yet at the same time, fears becoming one of its casualties. Coupled with this fickle position, the Government's stance, that competition law will benefit Hong Kong residents, is very unconvincing.

THOUGHTS ON COMPETITION LAW

The quotes below, from history to the present, expose the ambiguity inherent in competition laws.

"For more than a century, American antitrust laws have been used as a protectionist tool to stifle competition. They have always been used to protect competitors from competition and not to protect consumers, as the American public has been told. The end result has been reduced productivity and diminished international competitiveness. It saddens me to see other countries such as Hong Kong imitating some of our most disastrous economic policies."

— Dr. Thomas DiLorenzo, Professor of Economics, Sellinger School of Business and Management, Loyola University Maryland USA

"Given the openness of the Hong Kong economy, I am surprised that Hong Kong would be considering a competition law."

— Robert W. Crandall, Senior Fellow, Economic Studies, The Brookings Institution, USA

Steve Punter



Can Judges second guess a market?

ON COMPETITION

"My reaction to the current discussion about competition law in Hong Kong is that it appears to lack any empirical grounding. I don't see any discussion of the efficiency costs of alleged anti-competitive behavior and I don't see any estimates of the welfare gain that the proposed competition law will provide to consumers."

— Clifford Winston, Senior Fellow, Economic Studies, The Brookings Institution, USA

"No monopoly can survive for long without government regulations to protect it."

— Alan Reynolds, Senior Fellow, CATO Institute, USA

"Hong Kong gets top rankings for economic freedom in part because it does not have intrusive laws that cause market uncertainty and hinder economic dynamism. Adopting a competition law invariably will hurt Hong Kong's economy and tarnish its global reputation. Lawyers and bureaucrats will benefit, but the people of Hong Kong will enjoy less prosperity if the law is adopted."

— Daniel J. Mitchell, Senior Fellow, CATO Institute, USA

"The proposed legislation in Hong Kong government's 'Detailed Proposals for a Competition Law' would be disastrous for business, government and the consumer alike. It would have the opposite to the intended effect, because it would open the door to lobbying by vested interests. The consumer would

lose out due to a less competitive business environment, as stronger businesses are discouraged from acquiring or driving out of business the weaker ones. But even worse, the government's new role of deciding who is competing 'fairly' will expand the opportunities for corruption and encourage the private sector to seek advantages through government action rather than their own efforts. Hong Kong has clearly benefited from government staying out of the business realm, so it is a mystery why it would want to throw away this competitive advantage now."

— Hugo Restall, The Wall Street Journal

"The antitrust laws provide a vehicle for the antitrust community to carry on a useless, mischievous activity portrayed as law enforcement. . . . Although today's antitrust community is alive and well, antitrust is atrophying. It is becoming a relic, an anachronism, the irrelevant debris of past political demagoguery. Education in the antitrust facts of life could accelerate the process."

— Edwin S. Rockefeller, *The Antitrust Religion*, Cato Institute, USA

"When buying and selling are controlled by legislation, the first things to be bought and sold are legislators."

— P. J. O'Rourke, H. L. Mencken Research Fellow, Cato Institute, USA

"The constant animating force

behind all human action, and the creativity it unleashes, cannot be captured in predictive models or in mathematical formulas. It is precisely this fact that precludes employing the methods of the natural sciences to solve problems of human action."

— Ludwig von Mises, Austrian economist, historian, philosopher, and influential author

"Why is there only one Monopolies and Mergers Commission?"

— David Edward Sutch, Politician and Musician, United Kingdom

"We are increasingly governed not by law or elected representatives but by an unelected, unrepresentative, unaccountable committee of lawyers applying no will but their own."

— Robert Bork, Legal scholar and best-selling author, Served as Solicitor General, Acting Attorney General, and judge for the US Court of Appeals for the District of Columbia Circuit

"The more corrupt the state, the more numerous the laws."

— Tacitus, 56 - 120 A.D., Senator and historian of the Roman Empire

"It will be of little avail to the people that the laws are made by men of their own choice if the laws be so voluminous that they cannot be read, or so incoherent that they cannot be understood."

— James Madison, Fourth President of the United States (1809-1817), A Founding Father of the USA



“We have here the problem of bigness. Its lesson should by now have been burned into our memory by Brandeis. The Curse of Bigness shows how size can become a menace--both industrial and social. It can be an industrial menace because it creates gross inequalities against existing or putative competitors. It can be a social menace...In final analysis, size in steel is the measure of the power of a handful of men over our economy...The philosophy of the Sherman Act is that it should not exist...Industrial power should be decentralized. It should be scattered into many hands so that the fortunes of the people will not be dependent on the whim or caprice, the political prejudices, the emotional stability of a few self-appointed men...That is the philosophy and the command of the Sherman Act. It is founded on a theory of hostility to the

concentration in private hands of power so great that only a government of the people should have it.”

— Justice William O. Douglas, *United States vs. Columbia Steel*, Associate Justice of the US Supreme Court

“No one will ever know what new products, processes, machines, and cost-saving mergers failed to come into existence, killed by the Sherman Act before they were born. No one can ever compute the price that all of us have paid for that Act which, by inducing less effective use of capital, has kept our standard of living lower than would otherwise have been possible.”

— Alan Greenspan, Economist and Chairman of the Federal Reserve of the USA

“The world of antitrust is reminiscent of Alice’s Wonderland:

everything seemingly is, yet apparently isn’t, simultaneously. It is a world in which competition is lauded as the basic axiom and guiding principle, yet ‘too much’ competition is condemned as ‘cutthroat.’ It is a world in which actions designed to limit competition are branded as criminal when taken by businessmen, yet praised as ‘enlightened’ when initiated by the government. It is a world in which the law is so vague that businessmen have no way of knowing whether specific actions will be declared illegal until they hear the judge’s verdict — after the fact.”

— Alan Greenspan, Economist and Chairman of the Federal Reserve of the USA

The Lion Rock Institute is a free market think tank in Hong Kong, www.lionrockinstitute.org.