

Remarks by Irwin M. Stelzer\*

at

Kirkpatrick Antitrust Conference: Conservative Economic  
Influence on U.S. Antitrust Policy

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I approach this assignment with very considerable trepidation. First, it is daunting to be on a panel with such distinguished antitrust scholars, and be expected to add anything of value to what they have said. Second, we are here dealing with what the conference's organizers have called "Conservative Economic Influence on U.S. Antitrust Policy."

Let me begin by explaining this second worry. I would very much like to discuss the conservative influence on the economics of antitrust policy, since I style myself a conservative economist, the alternative position in fields such as housing, welfare, macroeconomic policy and other areas having been proven to be rather dismal failures. But

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when it comes to antitrust policy and other aspects of government supervision of markets, I find myself at odds with my conservative friends, and therefore cannot speak for them.

I have always believed that the free market system can be defended in the long run only if it provides fair and open opportunity to all comers, that its principal virtue is its contribution to social mobility, and that anticompetitive practices by dominant firms, and abuses created by the Berle and Means effect -- the ability of managers to pursue their own rather than their shareholder-owners' enrichment -- are the greatest threat to the capitalist free-market system. The best defense of a system that periodically produces increases in the inequality of income and wealth is that those inequalities are transient because the system by and large maintains fair access to upward movement. All of which means that the antitrust laws must be vigorously enforced, and even perhaps -- I am less certain about this, but think it an idea worthy of your consideration -- that the risks of what Professor Hovenkamp calls under-deterrence of anticompetitive acts are greater than the risks of over-deterrence.

Unfortunately, this view is not enthusiastically received by my fellow conservatives, who mainly see government intervention as efficiency-reducing, induced by inefficient whingeing competitors who just can't cut it in open competition, at best useless, at worst counterproductive. Besides, the concept of the dominant firm is simply not in their lexicon -- to them, all market power is transient (the period of transition is of little concern to them), and attempts to cope with anticompetitive practices by recourse to the antitrust laws more likely to result in over-deterrence rather than in efficiency-increasing, consumer-welfare enhancing, equity-producing solutions.

These colleagues have, of course, been much comforted by the emergence of the Chicago School, and not only for the quite sensible reason that its contribution to economic discourse helped move us away from an excessively rigid concentration on static market structure tests. Conservative economists take added joy from the fact that the Chicago School urges concentration solely on the economic goals of antitrust policy, and liberates them from the necessity of considering its social objectives.<sup>1</sup> Because (1) they believe they are capable of quantifying such

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<sup>1</sup> The best statement of this position is in Robert H. Bork, The Antitrust Paradox: A Policy At War With Itself. Edition with new introduction and epilogue. New York: The Free Press, 1993.

concepts as marginal cost, recoupment possibilities, which competitors are efficient and which are not; and (2) that judges are incapable of dealing with non-economic concepts such as equity -- in one case in which I was involved, an Chicago-School devotee was asked about the equity of a certain practice and referred the judge to "his honor's priest". My own view is that the empirical basis for much of what passes for economic testimony should be viewed as considerably less than precise and far from determinative, and that although, as Professor Hovenkamp points out, judges do make mistakes, that does not mean it is good policy to excuse them from attempting to come to grips with all of the aspects of the antitrust laws, including its social goals.

All of this is by way of disclaimer: I do not pretend to speak for conservative economists, most of whom prefer less rather than more enforcement of the antitrust laws, and almost all of whom reject Professor Hovenkamp's suggestion that "The time seems ripe to become more aggressive about structural remedies once again, particularly for repeat offenders". More on that latter point in a moment.

Now to my second worry: that I am not well qualified to comment on my learned colleagues' papers. Ever since I

found that participating in antitrust cases as an expert witness meant forfeiting control of my life's schedule to a cartel of lawyers and judges who arranged schedules to suit their own professional needs, and times such matters of greater importance as their fishing trips, vacations., and daughters' weddings, I have not participated in the many cases discussed in the papers presented at this conference. So if I stumble over some obscure footnote, or fail to understand just how to implement some of the exquisitely phrased tests sprinkled throughout these papers, I do apologize.

But the sponsors of the conference have told me that I cannot allow such atypical diffidence on my part to result in silence, and therefore beg your indulgence while I comment on a few of the points raised at this session.

1. Professor Hovenkamp seems relieved that economic thinking has progressed to the point where decisions no longer condemn as predatory "prices above any measure of cost." (p.21) I wonder whether that position gives full weight to the fact that an entrenched incumbent, charging monopoly prices, can lower those prices quite a lot without reducing them below some concept of cost -- as a signal not only to potential entrants, but to the venture capitalists who

increasingly finance these entrants, of what might be in store for them if they challenge the incumbent. It seems to me that we have to balance our understandable fear of preventing the price competition that we hope new entry will produce, against the possibility that such entry will not occur if a dominant firm is allowed to signal its intent to crush any newcomer by offering a small taste of the price wars to come. So I think it is worth considering whether predation is possible (or would the lawyers call this more accurately monopolizing behavior?) when prices are lowered to level well above average *total* cost.

Leave aside the question of the difficulty of determining whether the prices with which an incumbent chooses to confront a newcomer exceed some concept of marginal, or incremental, or average variable cost; assume they do. Assume even that they exceed average total cost. As Peggy Lee once asked in a different connection, “Is that all there is, my friend?”

I think not: an examination of the entire range of competitive practices of the incumbent over time, not each one of those practices in isolation, seems to me to provide a better basis for deciding whether or not we are dealing with predation, or with attempts to raise rivals’ costs by depriving

them of an opportunity to achieve economies of scales. True, as Professor Hovenkamp argues (p.22), there is a “risk of chilling procompetitive behavior”, but it is worth discussing whether that risk is, as Professor Hovenkamp characterizes it, “intolerable”, and whether it is really the case that “juries are not able to distinguish such strategies with sufficient clarity to avoid condemning procompetitive behavior.” (p.23).

After all, there is always a risk that cases will be wrongly decided, even by judges, much less the much-maligned juries, often accused of being unable to make sense of economists’ testimony that is so convoluted that it would, in the words of Tevye in “Fiddler on the Roof”, “cross a Rabbi’s eyes”. There is also the ever-present risk that later scholarship will reveal a decision to have been wrongly decided. The question we have to ask ourselves is whether a wrongly decided case that penalizes procompetitive behavior is a greater threat to the free market system than a case that is wrongly decided and allows a potential competitor to be nipped in its incipiency, if I might borrow a phrase used in another connection. That surely is a legitimate task for policymakers.

All of which is why the *Brooke* decision’s conclusion that “the exclusionary effect of prices above a relevant

measure of cost ... is beyond the practical ability of a judicial tribunal to control without courting intolerable risks of chilling legitimate price cutting..." might be worthy of reexamination. Certainly a judicial tribunal that considers itself competent to decide which of the competing measures of cost presented to it by learned economists (and, worse still, by accountants whose concepts of cost are as devoid of economic content as their audits often are of any meaning) is the "relevant measure" and is accurate, is capable of employing all of the evidence unearthed in multi-million discoveries to reach a judgment as to whether a price cut is predatory or not, without being bound by a rigid cost test.

I would suggest that any reevaluation along the lines I have suggested consider the relatively new role of venture capitalists in financing new entrants, especially in the increasingly important high-tech industries to which we look for advances in productivity. These capitalists, the first port of call for a newcomer after he has exhausted his own and his family's resources, are notably hard-headed realists. If they believe that an entrenched incumbent will be allowed to snuff out incipient competition by inducing manufacturers to boycott the new product, or by using technological legerdemain to tie its own competing product to its monopoly

product, or by setting a pricing schedule that in effect results in bundling or full-line forcing,<sup>2</sup> venture capitalists will, at the very least, raise the cost of capital to reflect the enhanced risk, (this is the really important “C” in RRC -- raising rivals’ cost) and more likely suggest to the newcomer that completion of his doctoral dissertation or a job with the entrenched incumbent is his best option. They must always be satisfied, before opening their wallets, that the incumbent does not have sufficient market power to nip the competition in its incipiency. Potential suppliers cannot be threatened with retaliation if they do business with the newcomer; most distributors cannot be fearful of the consequences of dealing with the new entrant; the dominant incumbent cannot manipulate its multi-product price schedule so as to make it uneconomic for its customers to divert part of their custom to a new entrant. Only with the assurance that the law protects their investment from being washed away by such tactics that have nothing to do with the relative merits of the competing products, will venture capitalists write the checks the challenger needs.

They know what some academic analysts do not: experience suggests that dominant firms are willing to have

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<sup>2</sup> John Vickers, “Abuse of Market Power,” p. 20, notes that a dominant firm can raise rivals’ costs—unduly deny scale economies to rivals—by offering price reductions that are “*conditional* on the buyer not dealing with rivals.”

recourse to tactics that are related to their market power, rather than merely to their efficiency. The use of these tactics turns the battle into one in which the firm with greater market power wins, rather than the firm with the best mousetrap. It is those tactics that the antitrust laws, applied both by the enforcement agencies and private parties, are uniquely equipped to prevent.

I have no doubt that the suggestion that even above-cost price cuts might in some circumstances be found to be anticompetitive flies in the face of what businessmen always claim they need: certainty. I have often suggested that such certainty is easily available: create a long list of competitive practices, and make them *per se* illegal, like price fixing. That is not the certainty they seek: it is the certainty that when they push the outer limits of competitive behavior, that behavior will be deemed *per se* lawful. The better policy alternative is, I fear, a degree of uncertainty, rather like other aspects of decision making -- the future course of interest rates, exchange rates and the like. Businessmen should be as capable of factoring their lawyers' nuanced advice into their pricing decisions as they are their economists' even less reliable forecasts of the economic variables that make the difference between profit and loss.

2. For some of the same reasons I wonder whether it might not be useful to consider carefully the proposition put to us -- and now before the Ninth Circuit, alas -- that a multiproduct firm selling a bundle of products above the incremental cost of producing the bundle should be allowed to price one of those products below the incremental cost of that product, even if it destroys the competitive prospects of a single-product firm. That decision is not one that should be based solely on economic considerations, but on a balancing of the desire to maximize some concept of efficiency and consumers' interests in the lowest immediate prices, against the reduction of opportunities to enter a market by a challenging, small competitor. Of course, economic considerations cannot be ignored, including the possibility that the new single-product entrant, by the very virtue of its specialization, might introduce a hitherto unrealized dynamic into the market.

3. Let me conclude with a point of agreement: that we should resurrect interest in structural solutions. It is increasingly clear that in fashioning remedies we cannot rely on anything requiring ongoing judicial supervision of the practices of a company, especially those specializing in the creation of intellectual property, or involved in industries in

which technology is changing rapidly. This is so for two reasons.

First, we do not want to slow the pace of innovation to accommodate the more leisurely one of the judicial process. Experience with Judge Green's supervision of the telecommunications industry is reason enough for caution.

Second, it is not at all certain that the courts can cope with firms understandably reluctant to comply promptly with their orders, witness the recent confession of the judge in the Microsoft case that the remedies she had ordered are not working terribly well,<sup>3</sup> or the frustration of the EU competition authorities as they attempt to develop and enforce a behavioral remedy for the anticompetitive tactics deployed by Microsoft. This difficulty with behavioral solutions might mean that relief has to be more radical in the case of high-tech violators of the antitrust laws than in the case of lower-tech ones, with divestiture and structural solutions playing a larger role relative to the prohibition of specific practices.

I do hope some of these ideas are congenial to some of you. But I should warn you of two things, which in combination you will not find cheering. The first is that the

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<sup>3</sup> Judge Colleen Kollar-Kotelly of the US District Court for the District of Columbia expressed dissatisfaction but added after a new approach had been agreed upon, "My only wish is that it had been done earlier, so we wouldn't be at this point," that being the point at which "Microsoft still has not provided the documentation to competitors" that the decree demanded, according to Thomas Vinje of Clifford Chance LLP.

weight of conservative economists is on the side of the anti-anti-trusters: they see enforcement of competition policy as government interference in the workings of markets, interference somewhere between unnecessary and downright harmful. The second is that these economists, based in the think tanks of Washington and elsewhere, are far more influential than the legal and economic scholars housed in the chairs of America's universities. It is no coincidence, as the Left was wont to say, that Justice Scalia spent several years imbibing the intellectual climate of the American Enterprise Institute before unburdening himself of *Trinko*.

Many thanks for your attention.