Is Antitrust the Villain of International Competitiveness?

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Many people have been wringing their hands in recent years over the supposed decline in the international competitiveness of American companies. As the problems have increased in severity, the number of culprits has also multiplied. Some point to the absence of a “level playing field” for U.S. firms in foreign markets and argue that the trade laws should be stronger; some bemoan the lack of strong protection for intellectual property rights both at home and, even more so, abroad; and some believe that the principal villain is the antitrust law of the United States, written and developed at a time when rivalry from foreign firms was vastly different from what it is today.

My theme is a simple one: it is misguided, and ultimately counter-productive, to blame antitrust for everything that is going wrong. The problem, to be sure, is a real one. Complaints about the endangered or declining competitiveness of U.S. firms in the face of global markets have become a mainstay of political rhetoric. As imports invade the United States at an ever-increasing pace, and exports fail to keep up, many people draw the conclusion that U.S. firms have lost their preeminence, that their products are second-rate, and that the innovativeness needed to regain market position is lacking. Naturally, these troubling conclusions have led to intensive searches for the cure. One of President Bush’s first acts was to establish a Council on Competitiveness, chaired by Vice President Dan Quayle, which is charged with investigating this problem and finding feasible solutions.

In a speech delivered on June 20, 1989, to the National Foreign Trade Council and the National Association of Manufacturers Coalition for Employment through Export, Vice President Quayle blamed the antitrust laws for a significant part of America’s competitiveness problems. He called specifically for reevaluating the private treble damage action, merger law reform, and more lenient rules for intellectual property licenses. It is important to note, however, that he did not lay the entire problem at the feet of the antitrust laws. International competitiveness, he noted, is also affected by the government’s fiscal policies, the way the United States handles research and development of biotechnology, and the country’s educational system.

The Vice President’s remarks reflect what I would like to call the myths about antitrust and its responsibility, or lack thereof, for the international competitiveness of American firms. These ideas are myths, in the true sense of the word. This does not mean that they contain not a grain of truth; certainly, every myth is based in some sense on ultimate truth.

Just as surely, however, most myths are elaborated, somewhat fanciful versions of that truth. I would like to examine more carefully the extent to which we have a competitiveness problem, the myth and the reality of the effect antitrust laws have on that problem, and some of the policy responses that will help us to be vigorous and successful competitors at the global level. This examination shows that today’s competitiveness problems have little, if anything, to do with the U.S. antitrust laws. The
future shape of antitrust may affect tomorrow’s competitiveness, but it is not at all obvious—indeed, it is probably wrong to think so—that the absence of antitrust laws would give rise to strong, efficient, and successful companies.

It does not take the perceptiveness of a newly awakened Rip Van Winkle to see the magnitude of the change over the last several decades in the importance of international trade for the U.S. economy. In 1972, the import penetration ratio for manufactured products (ratio of imports to total shipments plus imports) was 6.1 percent. That figure rose to 7 percent in 1977, 8.5 percent in 1982, and 12.9 percent in 1987. In some industries, the change was even more pronounced. Nonrubber footwear saw a shift from 17.1 percent in 1972 to 62.4 percent in 1987; engineering and scientific instruments changed from 12.5 percent in 1972 to 30.6 percent in 1987; and toys and sporting goods changed from 13 percent in 1972 to 41.8 percent in 1987. Exports, as the trade deficit grimly indicates, have not kept pace. We have watched the deficit grow from $2.3 billion in 1971 to $128.1 billion in 1988. The message seems inescapable: the United States, or more particularly U.S. firms, have not been winning the competitive battle with their Pacific Rim, European, or other foreign rivals.

The explanation for this experience might be found in one or more of four reasons:

Reason 1: “It’s our own fault.” U.S. firms no longer produce competitive products, for several possible reasons, including insufficient innovativeness, lack of attention to quality control, failure to take a long-term business perspective, and lack of understanding of foreign markets.

Reason 2: “It’s the U.S. Government’s fault.” U.S. firms operate at a built-in cost disadvantage vis-à-vis their foreign rivals because of a variety of governmental impediments, including strict environmental laws, worker safety requirements, the expensive U.S. legal system (particularly the products liability regime), and, of course, the antitrust laws.

Reason 3: “Foreign firms are to blame because they don’t play by fair rules.” Foreign firms enjoy an unfair cost advantage because their govern-ments confer generous subsidies on their products, making it impossible for even a more efficient U.S. rival to survive in the market. Alternatively, foreign firms engage in other competitive practices that are branded “unfair,” including dumping, use of exclusionary technical standards, advantageous relationships for government procurement, and insufficient respect for the intellectual property of others.

Reason 4: “Foreign governments are to blame because they protect their home markets.” Finally, closely related to reason 3, U.S. firms may be disadvantaged because foreign markets are deliberately closed to them. Sometimes this is done overtly, by means of quotas or high tariffs, but more commonly it is done subtly, through the myriad nontariff barriers that exist throughout the world. No one would care about a great volume of imports if, at the same time, a great volume of exports were flowing out.

The policy response to the problem of international competitiveness depends entirely on the extent to which each one of these reasons (or others not mentioned here) accounts for the present situation. Nothing could be more self-defeating than to seize on one possibility, whether it is antitrust law, foreign subsidies, or foreign market access, and to attribute most or all of the blame to that factor. I do not accuse the Administration of doing this. I do say, however, that both Congress and the Administration are under tremendous pressure to enact this kind of quick fix and that it is vitally important to continue resisting it.

It is not clear that antitrust law belongs at all in the list set forth above. Nonetheless, I include it because one continues to hear that it has a chilling effect on the kinds of business decisions mentioned in the Vice President’s speech. With that in mind, it is helpful to look more specifically at the ways in which antitrust is alleged to have a negative effect on competitiveness, and to consider the extent to which these charges are true.

Both the existence of strong (at least on paper) antitrust laws and specific aspects of those laws have often been said to put U.S. firms at a disadvantage. Fears of excessive or inappropriate antitrust enforcement led, for example, to the issuance in 1977 of the Department of Justice’s first Antitrust Guide for International Operations. Responding to the con-
continuing demand for reassurance, the Department of Justice issued revised Antitrust Enforcement Guidelines for International Operations in 1988. The late Secretary of Commerce, Malcolm Baldrige, occasionally called for the repeal of Section 7 of the Clayton Act, and one continues to see similar anti-antitrust rhetoric in the academic and popular press from time to time. The prevalence of these statements makes it worthwhile to review what the critics are saying about antitrust in more detail. These are the myths of antitrust and international competitiveness to which I referred above. I will first state the current myths and then analyze them in detail.

Today's competitiveness problems have little, if anything, to do with the U.S. antitrust laws.

Myth 1. Only U.S. firms must conform their behavior to strict antitrust laws. This point is a broadside attack on the antitrust laws. Its proponents assert that foreign firms are unconstrained, or much less constrained, in their business decision making, because their countries do not have meaningful antitrust enforcement. Cooperative arrangements between firms are therefore arranged more easily; mergers and other consolidations may take place in an unregulated atmosphere; and distributional restraints are entirely market driven.

Myth 2. Private treble damage actions, unique to the United States, are diminishing industrial productivity. This accusation links the availability of private enforcement of the antitrust laws to impaired productivity. It focuses in particular on the availability of triple the money damages suffered, although one might also include the private party's ability to obtain a court injunction, and in some circuits, even to obtain divestiture after an unlawful merger. In the final analysis, the argument has to do with optimal enforcement levels. Treble damages, it is argued, lead to overenforcement of the laws. Overenforcement in turn means that U.S. firms (and not their foreign rivals) are spending dollars and time on litigation instead of on more productive activities.

Myth 3. Antitrust scrutiny of mergers and acquisitions is preventing efficient transactions from taking place. According to this myth, the market for corporate control is still distorted significantly by the fear that an otherwise desirable transaction will be thwarted because of antitrust problems. This can happen in one of two ways: either firms will reject a proposed transaction during the planning phase, following advice that the antitrust laws would prohibit it, or firms will go forward with their deal and find themselves sued either by a government agency (usually, though not always, the Department of Justice or the Federal Trade Commission) or by a private party. Excessive caution, for the first type of case, or a misapprehension of competitive consequences, in the second type of case, lead to the harm identified here.

Myth 4. Antitrust prevents desirable licensing arrangements for intellectual property. Intellectual property owners invest substantial resources in the development of intangible property rights. Often, the most efficient way to exploit those rights is to confer a limited privilege on others to use them, through a licensing arrangement. To the extent that antitrust law stands as an obstacle to restrictions on licensee use of the property, including price restrictions on resulting products, territorial restrictions, restrictions on grant-backs, or others, it reduces the initial incentive of the licensor to invest in innovative activities.

Myth 5. The U.S. antitrust laws are too insular, condemning concentration in U.S. markets without recognizing the true global nature of markets. Competitive consequences for antitrust purposes must almost always be judged in terms of particular relevant markets, unless the anticompetitive impact can be observed directly. The tendency still exists, however, to think only of competition from within the United States, overlooking the diversity and strength of competition from abroad. This error leads to the condemnation of arrangements that are inherently unable to have an adverse effect on competition, and that might have been efficient.

Most, if not all, of these myths had a solid grounding in reality twenty or thirty years ago; today's reality is quite different. To the extent that these myths do not describe antitrust rules and enforcement practices, "reform" of the antitrust laws is not likely to improve our international competitive position. Only after we set the record straight can we consider what changes, if any, would be desirable.

1. Other antitrust laws. Immediately after World War II, it was true that most other countries did not have laws like the U.S. antitrust law. When such laws existed on the books, as was the case in (for example) Canada, occupation Japan, and occupation West Germany, enforcement patterns were utterly different. U.S. firms were at the same kind of disadvantage that later emerged under the Foreign Corrupt Practices Act: their actions had to conform to standards from which others were exempt.

Today, however, the situation is quite different. The competition rules of the European Economic Community, set forth in Articles 85 and 86 of the Treaty of Rome and implemented by the European Commission, are comprehensive and strong. It is not uncommon, in fact, for practices now to be condemned in the United States that the Commission would condemn. Recently, in the Wood Pulp case, the European Court of Justice took important steps in the direction of asserting the same kind of extraterritorial enforcement jurisdiction as the U.S. does: that is, jurisdiction to regulate arrangements outside the country that are carried out in part within the country or that otherwise directly and substantially affect the country. From a substantive standpoint, European firms face a regula-
tory regime very similar to that faced by U.S. firms.

National laws have also been strengthened all over the world. The competition laws of the Federal Republic of Germany have been regarded as among the world’s toughest for years. Canada, France, and the United Kingdom, to name three other countries, have strengthened their competition laws in recent years. The Organisation for Economic Cooperation and Development (OECD) includes restrictive business practices in its Guidelines for Multinational Enterprises, calling on enterprises to “refrain from actions which would adversely affect competition in the relevant market by abusing a dominant position of market power,” and to refrain from participating in “international or domestic cartels or restrictive agreements.” In fact, the only important exception to this pattern is Japan, and even there, the Japanese Fair Trade Commission has indicated that it is making efforts to achieve effective regulation of restrictive practices. In sum, an international consensus is building about the basic content of competition law, such that it is no longer persuasive to argue that U.S. firms are uniquely burdened (and benefited) by these laws.

2. Private enforcement. In this area, it remains true that U.S. law is different from most of the rest of the world. One can detect a nascent private action in Europe, but it bears little if any resemblance to the famous treble damage suits that have been brought in the United States, challenging cartels in industries such as electrical equipment, plumbing fixtures, and folding cartons. Treble damages can be useful, to the extent that they provide an incentive to detect anticompetitive behavior that would otherwise secretly inflict harm on the economy. Often, however, one suspects that the suit would be brought somewhere even if damages were limited to actual losses, although marginal actions would be discouraged because of the reduced amount in controversy. Suits about distributional restraints, for example, would appear in state court as contract actions if it were not for the antitrust option in federal court. This area is therefore one that requires closer analysis. In a nutshell, one should first look at which private actions are still available in the federal courts. The picture shows that very little overenforcement is left in the system, and much of what remains is in the process of being squeezed out, quite possibly to the point of excess.

This has happened in part as a result of the elaboration of the concepts of antitrust injury and antitrust standing of the last twelve years. Suits by indirect purchasers and suits by competitors have become more difficult to bring, depending on the violation charged. For vertical arrangements, developments in the substantive law have closed off the antitrust option for a vast number of terminated distributors. We are coming to the point where the treble damage private suit remains available to precisely the people who ought to have it: customers or suppliers who suffer from overcharges, and competitors whose exclusion from a market leads to anticompetitive results. To challenge private enforcement in these circumstances is to challenge the antitrust laws themselves. Frontal assault, however, would be a grave mistake in my opinion.

3. Merger reform. One can hardly take seriously charges that the merger laws were overenforced during the Reagan Administration years. This point must be understood as expressing a concern that the loosely worded Section 7 of the Clayton Act has sometimes been read sensibly, and sometimes not. Few people believe that merger decisions such as Brown Shoe, Von’s Grocery, and Pabst represent desirable policy.1 Fear of a return to the “bad old days” might be inflicting a drag on merger activity (although I am highly skeptical even about that chance). In 1986, part of the Reagan Administration’s antitrust reform legislative package was a bill that would have rewritten Section 7 to reflect more closely the merger policy expressed in the Justice Department’s 1984 Merger Guidelines. Given the extraordinarily healthy, if not frenetic, pace of the M&A business, it is hard to make the case that even this kind of change is a good idea.

4. Intellectual property licensing. Here again, there was a time in the past when the criticisms noted above were well taken: the infamous era of the Nine No-No’s. Today we are living in a different world. Reformers of this field should therefore exercise some caution. Innovativeness is critically important to our future competitive ability, but the case has yet to be made that bigger is better for this purpose. With particular reference to the proposed Joint Production Act, which would either extend the protections of the National Cooperative Research Act to production joint ventures or create a special antitrust

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lematic relationship between markets for innovation and markets for commercialization. The "safe harbor" may give insufficient weight to the risk of undue market power in downstream markets, where consumers are most directly affected. In short, while the political bandwagon may make some change in the antitrust treatment of cooperative production ventures inevitable, any such "reform" should be careful to preserve competitive markets both for technology and for its resulting products.

5. Foreign competition in general. If U.S. courts and antitrust enforcers are actually ignoring foreign participants in U.S. markets when they conduct their antitrust analyses, this would be a scathing indictment of their performance. I doubt strongly, however, that this is true. It would be unthinkable, for example, to evaluate competition in the automobile market without taking into account Toyota, Nissan, Honda, and Hyundai, or Mercedes, BMW, and Volvo, and no one would try to. Evaluating potential competition from foreigners is sometimes hard, especially if capacity that could be diverted to the U.S. market is an important factor, but even here approximations are possible.

The difficult issue for market analysis is the reliability of foreign competition, given the prevalence of trade law restrictions. This becomes important any time the ongoing and future strength of a foreign firm is relevant, which is to say, almost always. Foreign competition for this purpose will fall into one of four categories: (1) totally unregulated, either because of the nature of the product or service, or because of the country of origin; (2) subject to tariffs; (3) subject to quotas or other quantitative restrictions imposed by the United States; or (4) subject to quantitative restrictions or other trade management devices "voluntarily" imposed by the

source country.

Competition from foreign producers whose products fall in the first two categories is basically reliable, in the sense that it can respond to market trends just as freely as competition from U.S. firms. The same cannot be said for the latter two categories.

Given the choice between the vigor of competitive markets and the complacency of monopoly, my vote is squarely with competition and strong antitrust enforcement.

Firm quotas, whether imposed by the United States or the foreign government, do not allow the foreign firm to respond if prices rise or supplies fall short in the American market. Quantitative restrictions themselves vary importantly: some are for a fixed duration, some are indefinite, some are absolute, some depend on quantities imported. As the Department of Justice's 1984 Merger Guidelines and 1988 International Guidelines recognize, it would be a mistake totally to disregard competition from these restricted foreign sources, but some kind of discount factor must be devised to avoid overstating their significance.

In my view, the weight accorded to restricted foreign competition should vary depending on three general considerations:

1. How many foreign sources exist, both in terms of firms and in terms of countries of origin? If there are many firms, spread through many countries, the likelihood is strong that some form of foreign competition will be able to exert its influence effectively in the U.S. market. If only a few firms exist, and they are in countries participating in trade management measures, the competitive influence they exert will be correspondingly weaker.

2. How difficult would re-development of U.S. sources be if all foreign trade disappeared, either for political or military reasons, assuming that taken alone the U.S. market is highly concentrated? If, taking into account the type of product, the elasticity of demand for the product, capital requirements for new entry, technical requirements, and distributional needs, it appears that re-development would occur relatively quickly (i.e., within eighteen months), then the foreign competition is not critical to preservation of the U.S. market. If the opposite is true, a higher priority should be placed on maintaining competitive conditions internally.

3. How quickly is technology changing this field? If the market is a rapidly developing one, then the fact that existing foreign firms operate under trade restrictions is relatively unimportant. New entry by other firms or expansion of existing firms may occur despite efforts at managing the trade. If, on the other hand, the market is relatively well established and unlikely to experience technological improvements, the standard skepticism about restricted foreign competition is well taken.

The critical question is whether, for noneconomic reasons, the U.S. market should be assessed in isolation for antitrust purposes, or whether the full extent of international competition can make itself felt, making global market analysis appropriate. Factors such as those suggested above will help provide the answer to that question.

Two points remain that deserve at least a brief mention. The first arises
out of an ambiguity in the criticisms of antitrust. Those who fear the malevolent influence of antitrust law on U.S. international competitiveness may be talking about two utterly different things: the idea that monopoly is not really bad, or the idea that markets are often global and that antitrust should treat them as such. The second deals with the content of antitrust law itself.

Taking the first point first: Some of the arguments about competitiveness and innovation seem to imply that monopoly size and monopoly profits are not the evil we once thought they were, whether enjoyed by a single firm or by a group of firms coordinating their actions. Ma Bell, one might argue, innovated constantly before the break-up; IBM's R&D was second to none. As I noted above, the empirical evidence is far from conclusive on the actual relationship between size and innovation, and much of it seems to point in the opposite direction. Personally, given the choice between the vigor of competitive markets and the complacency of monopoly, my vote is squarely with competition and strong antitrust enforcement. Correct understanding of global markets is an entirely different kind of criticism. There is no doubt that this should be part of every antitrust lawyer's vocabulary, from the day he or she is first introduced to market analysis through the case now sitting on the desk. To urge accurate market definition, however, is just to make an "apple pie" statement that the latest learning should be disseminated. It does not mean that antitrust needs a fundamental overhaul.

On the second point, much of my discussion of the myth and reality of antitrust underscored the changes that have taken place in antitrust analysis. It is worth emphasizing again that we should not change today's antitrust law just because some decisions were issued in the 1960s that we now believe to be wrong. Indeed, if antitrust needs anything today, it is a little reinvigoration, as the Millstein Task Force on the Antitrust Division, on which I served, recently concluded. We surely will not solve our international competitiveness problems by changing laws that are "not broke" at the moment.

Only if one were a firm subscriber to the pendulum theory of antitrust doctrine, which incidentally I am not, would it perhaps make sense to codify some of the developments of the last ten or fifteen years. In fact, we are seeing isolated efforts at codification (or rejection of court decisions), all of which are healthy exercises, in my opinion. Legislative proposals give all of us a chance to air our views on what antitrust ought to be for the future, in light of all the complexities we are able to perceive. We should take care, however, that we do not abandon the flexibility that the antitrust laws have enjoyed for nearly a century. It is that flexibility that allows us to continue to protect competition, to the benefit of American consumers, even as the arena of competition has moved from the local, to the national, to the international.