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Allocating Antitrust Decisionmaking Tasks

FRANK H. EASTERTIBROOK*

Antitrust law has become a branch of industrial organization, itself a branch of economics. Today judges and the antitrust enforcement agencies search at every turn for economic arguments pro and con. This is a staple in academic thought as well—and it makes little difference what stripe. Those who could be called hawks employ economic argument, just as do those who see less scope for antitrust do. Most of the papers delivered at this symposium, like the merger guidelines issued by the National Association Attorneys General (NAAG),1 are grounded in economic rather than political theories. More economics lies ahead. But what shall we do with economic argument, which all too often has no firm conclusion? I add a thought that is old in thinking about economic arrangements but novel in thinking about the application of law to industrial organization: comparative advantage.

I

Until the 1970s antitrust law sorted all business practices into two bins. The practices in one bin were declared unlawful per se; the practices in the other were evaluated under the rule of reason, which as a practical matter meant that they were declared lawful per se, although the attorneys' fees incurred on the way to the ritual absolution were a hefty tax on the lawful conduct. The per se rules came under attack on the ground that many of the condemned practices might be beneficial, making summary condemnation improvident. Throughout the last fifteen years courts have been willing to indulge explanations for conduct formerly condemned.2 Along the way the rule of reason also became a testing ground for explanations, so that three years ago the Supreme Court finally declared an important business arrangement illegal under the rule of reason.3 At the same time, the Court adopted a middle ground, a "quick look" version of the rule of reason under which justifications for business practices might be evaluated summarily.4 Modern antitrust law is a search for economic explanations of problematic conduct.

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4. Id. at 109-10; see also National Soc'y of Professional Eng'rs v. United States, 435 U.S. 679 (1978).
If the explanations show the conduct likely to be in consumers' benefit, then a court stays its hand; if not, a court condemns the conduct.

This approach creates a risk of losing sight of the impetus for the per se rules: a belief that courts are not very good at divining the reasons for and effects of complex business practices. In corporate law the "business judgment rule" insulates most decisions from judicial review because there is little likelihood that systematic judicial intervention would make investors better off. Judges' decrees would increase the riskiness of business decisions without making decisions better. After all, judges are not selected for business acumen and are not penalized for bad decisions. We praise managers who hold the stock of the firms they manage, because this aligns managers' interests with investors' interests; managers and investors do well or poorly together. Self-interest is a powerful spur. If a judge should bet on the astuteness of his business judgments by holding stock in the firms that appeared before him, we would hustle the judge off to jail. An essential ingredient of interest-alignment in the business world is an impermissible lack of disinterest in the judicial world. So we do not trust judges to make business decisions in corporate law. Yet antitrust law now calls for the same sorts of economic judgments. We ought to be skeptical of judges' and juries' ability to give good answers.

There is a difference between corporate and antitrust law. Managers' mistakes generally harm only people who have elected to affiliate with the firms as investors, suppliers, or employees. Managers who injure stockholders can expect to find their salaries falling or to be given their walking papers. Blunders induce automatic penalties, to which legal processes could add little. The market—to personify a set of interactions that involve real people protecting their own interests—is the principal safeguard of investors. Managers who monopolize injure customers, who cannot retaliate readily. There are no automatic penalties. These effects on third parties justify a greater judicial role.

In deciding how much greater, we must inquire into comparative advantage. This means an advantage relative to the cost of the next best alternative. Jones may be better than Smith at both fixing bicycles and baking bread. Jones nonetheless may hire Smith to fix his bike, because Jones is better at baking than at tinkering. Jones is most productive if he spends full time on baking, hiring others with the income from that business. Smith has

a comparative advantage over Jones at fixing bicycles, even though Jones has an absolute advantage.

Judges, no less than Jones, may find that they can do the best for society by confining the scope of their activities. Suppose judges are able to fix markets when they are monopolized. Other social institutions still may have a comparative advantage. The principal competing institution is the actions of business rivals. If there are profits to be made, rivals enter (or expand their production) and undercut the monopolist. If a firm tries to acquire monopoly power and fails, this will not attract entry, but it also will not generate profits. The sums invested in the failed effort are “automatic penalties” for the conduct and deter similar efforts. So markets both undercut successful monopolists and deter putative ones without the help of judges. No one doubts that this occurs—eventually. Competition is the long run solution to monopoly. Perhaps antitrust law speeds up the arrival of the long run; perhaps it does not. Unless we know it does, judges ought to apply their talents in other fields, where they have a comparative advantage over other institutions.

Expressing the extent of the law’s comparative advantage over rivalry in undercutting monopoly requires the use of the social scientist’s terms “false positive” and “false negative.” If a judge wrongly condemns as monopolistic a business practice that is efficient and beneficial to consumers, that is a false positive. Consumers would be better off if the judge had decided the case the other way. If the judge wrongly excuses conduct that is harmful to consumers, that is a false negative.

Litigation produces false positives and false negatives. The more complex or unusual the conduct, the more false positives and false negatives there will be. In other words, the greater the complexity, the greater the error rate. And of course the more complex the conduct, the longer the case will take to conclude, and the more it is apt to cost along the way. All the while competitors will be trying to undercut monopolies.

II

Where does the law have a comparative advantage? One requirement is that legal processes be able to beat market processes to a conclusion in assessing novel practices. (Common practices may be governed by rules that deter similar conduct, and the duration of litigation is accordingly less important. I therefore confine this discussion to “novel” practices, the ones that require substantial independent analysis rather than simple application of a precedent ready-made for the case.) If rivals will undo a monopoly or evade a questionable practice before judges can decide the case, there is little point in incurring the costs of litigation and suffering the inevitable mistaken judgments. If the business practices in question may be long-lived, then courts
may have a comparative advantage when false positives are few and when false negatives will survive competitive pressure. Unless there is a strong reason to suspect that a monopoly or monopolistic practice can survive the attempts of other firms to undermine it, the costs of inaction (excusing harmful conduct) are low. Unless there is strong reason to suspect that we can identify harmful conduct accurately, the costs of action (condemning beneficial conduct) are high.

The conditions for useful legal intervention may be met when we know a lot about the practice—for when we know but little, the cost of error goes up, and the risks of false positives may be substantial. People condemn all too quickly what they do not understand. Hasty or uninformed action may undo novel but beneficial practices just because of their novelty. Often it takes a decade or more to determine what a business practice really does; law moves too fast for our own good, because courts act in advance of the arrival of explanation. Judges move slower than markets but faster than the economics profession, a deadly combination.

We must be careful even in coming to conclusions about what we think we “know.” Much of the law of mergers is built on the structure-conduct-performance paradigm, a belief that more concentrated industries are prone to collusion or to monopolization by a dominant firm. This is the basis of the attention to concentration and increases in concentration. It is reflected in the Supreme Court’s cases, in the 1968 merger guidelines, in the 1982 merger guidelines, and in the 1987 NAAG guidelines. The relation between concentration (market structure) and monopolistic conduct is “known” from a combination of neoclassical economic analysis, which suggests that there will be such a relation, and from data collected over a period of decades that seemed to show that concentration is associated with higher profits. The inference—that the profits were “monopoly” profits—seemed irresistible.

This relation between concentration and profit has vanished in studies performed over the last decade; indeed it has been reversed! It is now possible for economists commonly identified as “liberals” on questions of antitrust policy to state: “With most specifications, concentration coefficients turn out to be negative, not positive, in conjunction with market share variables.”7 In other words, when you correct for the profits of the largest firm—which may have become the largest because it was the most efficient—the concentration of the market as a whole seems to be associated with lower rather than higher profits. The empirical foundation on which much antitrust policy was

built has been washed away.\textsuperscript{8} We must consider the possibility that this will happen to other beliefs about the operation of markets, and take this into account in formulating rules of law (as well as in considering requests to alter existing rules).

Sometimes it may be prudent to act when we know little, if a mistaken condemnation can be reversed as easily as the contrary error would be. Yet there is a bias in the error-correction devices of the law. Mistakes of \textit{law} are not subject to competitive pressures. If a judge errs in saying that the NCAA's contract with the TV networks for college football is a violation, there is no way private decisions can undermine the decision, as there might be a way for private competitors to undermine the contract. Once the court speaks, the contract is gone. If the prohibition was mistaken, we shall suffer the consequences indefinitely. So, too, if the Supreme Court announces a rule such as the "filed rate doctrine," under which a cartel price is beyond challenge if reflected in tariffs filed with the ICC, or the rule of per se illegality for resale price maintenance, there are no automatic market pressures that test the wisdom of the rule. Quite the contrary, after some years have gone by, the Court is apt to declare the rule exempt from further scrutiny.\textsuperscript{9}

Law has a comparative advantage over markets, then, when legal processes are rapid, when false positives are few or quickly corrected, and when markets are sluggish about correcting false negatives. These criteria are met for naked cartels (which may be condemned quickly and with great

\textsuperscript{8} This is not to say that people will not try to shift ground. \textit{See, e.g.}, Harris & Sullivan, \textit{Horizontal Merger Policy: Promoting Competition and American Competitiveness}, 31 \textit{ANTITRUST BULL.} 871 (1986). The authors concede that new work may have knocked the stuffings out of the old profit studies but contend that the reason must be that concentration produces inefficiency, which eats up the profits at the same time it injures consumers. \textit{Id.} at 875, 915-23. Now one is entitled to be skeptical when anti-merger folks say for 30 years: "We know concentration is bad and here's the proof" and then say, when the "proof" is demolished: "Just kidding, it wasn't really profits that made the case after all; let's keep the same old policy while we search for a new foundation." Prof. Scherer's work for this conference, \textit{Antitrust, Efficiency, and Progress}, 62 \textit{N.Y.U. L. REV.} 998 (1987) finds no evidence that concentration is associated with inefficiency; data on overhead costs suggest the opposite, and there is no reliable relation between industry concentration and innovation. Some studies show that concentration is associated with higher wages, perhaps inefficiently high wages (to judge from their tumble in the air transportation industry with deregulation), and there may well be other inefficiencies. But the implications for antitrust policy are obscure, since payments to unions or other ways in which profits vanish are automatic losses; the legal system need not impose these losses a second time to obtain optimal deterrence. Managers, too, would like to increase efficiency (or reduce wages or other costs of inputs) to increase profits. Their interests in these instances are automatically aligned with those of the rest of society. Prof. Harris and Sullivan do not discuss the question of optimal sanctions for productive inefficiencies. For an article that does, see Landes, \textit{Optimal Sanctions for Antitrust Violations}, 50 \textit{U. CHI. L. REV.} 652 (1983). An optimal sanction of zero is another way to say that the legal system does not have a comparative advantage in dealing with a problem.

\textsuperscript{9} \textit{E.g.}, Square D Co. v. Niagara Frontier Tariff Bureau, 476 U.S. 409 (1986) (holding the "filed rate doctrine" inviolate—over the protests of the Antitrust Division, which wanted to expand the scope of the antitrust laws).
assurance that condemnation is appropriate) and for large mergers in markets with high barriers to entry (the market power from which may take a very long time to erode through competitive pressure). The criteria are rarely met for novel business practices, those courts are encountering for the first time. The rate of false positives may be particularly high because cases arrive in court ahead of explanations for the practices. It is easier to call practices “abuses” and the like than to understand the real economic effects of novel arrangements. Courts can see the wounded plaintiffs but not the beneficiaries.

How does this approach tally with the prevailing wisdom? Take the *Aspen* case.\(^\text{10}\) The Court held that a jury was entitled to condemn the refusal of one skiing enterprise to issue joint lift tickets with its only local competitor at the resort. I am suspicious of booting to juries, and deferring to their conclusions on, questions that we—meaning judges, lawyers, economists, and other professions taken together—know very little about. And we know very little about joint selling arrangements. False positives are apt to be frequent, and it is difficult to undo mistaken condemnations. It is easy to see, however, how a decision like *Aspen* could discourage businesses from entering into beneficial joint operations for fear that they would be exposed to antitrust liability if they should withdraw.\(^\text{11}\) It is also frightening to contemplate businesses using this threat of liability for increasing competition as a justification for making or retaining monopolistic joint arrangements, as a form of “mandatory cartelization defense.” This is a risk of the “essential facility doctrine,” which penalizes large firms for not cooperating enough with their rivals.\(^\text{12}\)

Indeed, good antitrust scholarship largely consists of one warning after another about the dangers of both simplistic condemnation of novel practices—which increases business risk to an unacceptable degree—and employing highfalutin’ theories to show how apparently beneficial practices, such as price competition, may be harmful. Antitrust law need not contain a bias, with per se rules working only in plaintiffs’ favor. If practices that are harmful in eighty percent of the cases are unlawful per se, then practices that are beneficial in eighty percent of the cases should be lawful per se. More dis-

\(^{10}\) Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585 (1985); see Easterbrook, *Exclusionary Conduct, supra* note 6 (discussing *Aspen*).

\(^{11}\) This fear explains the decision in Olympia Equip. Leasing Corp. v. Western Union Tel. Co., 797 F.2d 370 (7th Cir. 1986) (reading *Aspen* narrowly), *cert. denied*, 107 S. Ct. 1574 (1987).

\(^{12}\) A point established in my court by *Olympia*. Not all voices speak as one, however. Fishman v. Estate of Wirtz, 807 F.2d 520, 533-35, 539-42 (7th Cir. 1986), treats the “essential facilities doctrine” as the source of a requirement that monopolists act fairly toward people who might want to buy their product, even when there is no conceivable injury to consumers from the “unfair” conduct. It is not a position to be welcomed. See *id.* at 571-75 (Easterbrook, J., dissenting); P. AREEDA & H. HOVENKAMP, *ANTI.TRUST LAW* §§ 736.2d, 736.2f n.71, 1510c (Supp. 1987).
criminating analysis should be reserved for the rare intermediate case. The harmful practice that is passed over by a rule of per se legality, the false negative, can be taken care of by business rivals. This is the sort of situation for which market forces have a comparative advantage over courts.

Yet as you can glean, I am not entirely happy with the current state of antitrust law, because courts often go looking for answers to questions that should not be answered in litigation. Aspen is one illustration, and the treatment of dastardly business conduct is another. Take the Empire Gas case.\(^\text{13}\) Empire Gas stole business from rivals by lying to customers and selling below cost. Perhaps this is so obviously anticompetitive that we might as well condemn it without proof that Empire could obtain a monopoly.\(^\text{14}\) But of course another alternative is that the court misunderstood Empire's costs of doing business, or confused an introductory discount with predatory conduct, or some such mistake. If we take it as a given that Empire could not obtain a monopoly, because entry into the business of retailing liquid natural gas is easy and rapid, then there are only two plausible explanations for Empire's conduct: It was beneficial to consumers (low prices are usually beneficial), or it was a mistake by Empire's managers that threw away the investors' money. If it was the former, then the law \textit{must} not interfere; if it was the latter, then the law \textit{need} not interfere, because mistakes are self-deterring. This is the lesson of the business judgment cases in corporate law. Managers that injure their firms face their private days of judgment. Only by neglecting the comparative advantage of markets over law in some cases could we think that judicial intervention is always best. It might help to compare Empire Gas with American Airlines.\(^\text{15}\) In Empire the defendant paid a penalty for failure in the market, while in American there was no penalty. A firm that proposes a cartel stands to gain but never lose; a legal penalty is necessary to change the incentives; a firm that sells its product for too little money, as in Empire Gas, stands to lose but rarely gain. This is the explanation for the Supreme Court's thoughtful opinion in the Matsushita case.\(^\text{16}\) Long-term sales below cost are self-deterring. This is no different from designing expensive products that no one buys—a court need not penalize the designers of the Edsel to stop them from wasting money, and a court need not penalize would-be monopolists who fail to achieve their objective.

The same principles should govern our approach to market power in antitrust cases. The Supreme Court has begun to add market power require-\hfill


ments even to categories of conduct once thought unlawful per se.\textsuperscript{17} One could oppose this development along the following lines: Given that we know a practice is harmful, and given the difficulty of proving market power in litigation, why not dispense with this requirement? Now turn the question around: Given that a practice indulged without market power is either beneficial to consumers or, if not, self-defeating to its practitioners, why use the courts to condemn the conduct? Perhaps people are mistaken in believing that the practice in question is harmful. If they are not mistaken and the practice is indeed harmful, then firms without market power will lose business and desist soon enough. Unless courts are very good at separating beneficial from harmful practices, a process of condemning questionable practices pursued by firms without market power will spin the wheels of the courts—at great expense—for no substantial result. Markets have a comparative advantage over courts in dealing with the conduct of firms that lack market power.

The risk of error cuts both ways. Just as courts may err in thinking that a practice is harmful, so they may err in thinking that a firm does not have market power. If they mistakenly dismiss cases on the ground of lack of power, this will inflict a loss on society. So, too, the costs of proving market power are a social loss, when there is in fact power. Yet power often is evident at a glance. In the \textit{Indiana Dentists} case\textsuperscript{18} the fact that the defendants did a substantial portion of all dental work in southern Indiana was enough. Patients would not travel hundreds of miles or turn to barbers in order to escape a cartel of dentists.

Antitrust law has not been plagued by difficulty in establishing market power. Quite the contrary, there has been a bias in favor of finding power when there is none. So we have “markets” such as downhill skiing in Aspen, Colorado, or football televised on Saturday afternoons in the fall, although these have no economic significance.\textsuperscript{19} The history of merger law in the Supreme Court is a history of finding market power in bizarrely defined “submarkets” that escaped the attention of mortal economists. This long-term bias in favor of finding too much market power reduces the costs of making market power an essential ingredient in every antitrust case.

\section*{III}

Speaker after speaker at this symposium suggested some way to enlarge the scope of antitrust. None talked about comparative advantage; indeed, you would get the impression from many papers that judges are omniscient,

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infallible, and have time available for antitrust cases at zero opportunity cost (that is, that more antitrust enforcement does not mean less enforcement of something else). Would that it were so! Since none of the contributors suggests that other lawyers and economists are omniscient and infallible—since many papers are devoted to exposing the fallibility of almost every other student of the subject—we should treat judges as equally error-prone.

A brief tour through the proposals offered at this symposium does not yield confidence that judges can increase human happiness by implementing any of the programs. Take Professor Goldschmid, who thinks antitrust ought to be used to break up large firms—those with shares large enough to charge monopoly prices without the need for collusion. Professor Goldschmid does not identify any of these firms, but it is possible to think of some: Boeing in airframes; General Electric and Pratt & Whitney in turbine engines; Kodak in film; Motorola in microprocessors; Hartz Mountain in birdseed. Is there any reason to think that prices would fall or quality improve if these firms were dismembered? Most have been successful not only in the United States but also in foreign markets, suggesting that they are competing rather than holding up monopolistic price umbrellas. Maybe they grew because they design good products and sell them for low prices. Is there any reason to think that judges could tell which of these firms is best dissolved, or the lines along which they ought to be fractured? The ability to identify gains in principle from eliminating single-firm monopoly power does not suggest any particular program for antitrust, and it is frightening to contemplate both the difficulties of implementing a dissolution policy and the costs if we guess wrong.

Professor Williamson’s contribution expresses concern about strategies by which firms may make new entry or expansion by rivals difficult. Again this is a possibility that deserves thought. If firms can reduce the elasticity of supply of their rivals, they can raise the price they charge for their products. But can we tell, reliably, when this lies in prospect? Professor Williamson gives a few examples; I concentrate on Whirlpool’s acquisition of KitchenAid, because it is the one Professor Williamson knows best. Even though he worked on that acquisition as an economic expert, which gave him access to data, and even though he has had much more time to mull over his conclusions than the FTC and the district court had to cogitate the case, this is all Professor Williamson is willing to venture:

Whether or not this is a Type C merger [that is, one that reduces the elasticity of supply of rival firms] in which the head-to-head competition of the merging firm had strategic significance depends on whether the upper end

of the dishwasher market constituted a meaningful submarket. This is a difficult question and was never determined. Strategic considerations become important if one assumes that spatial considerations apply and that this is a meaningful submarket.\textsuperscript{22}

"If one assumes?" "Become important," two highly problematic things? Despite having both the data and the time that are unavailable to judges and enforcement agencies, Professor Williamson cannot reach a conclusion about the economic effects of the acquisition. What, then, should the judges and enforcers have done, and what should they do in similar cases in the future? Unless we assume that false positives are unimportant, that questions without answers are sufficient to condemn economic activities, it is difficult to find here a program for antitrust. As Professor Williamson says, "the fact remains that our capacity to evaluate strategic abuses is very primitive," which leads him to conclude that we should engage in study rather than condemnation.\textsuperscript{23} I agree wholeheartedly with Professor Williamson that learning about strategic behavior is one of the most important programs for the future of antitrust; we ought to acquire both knowledge and confidence before using such approaches to undo economic transactions, however.\textsuperscript{24}

Professors Krattenmaker and Salop offer a more general theory of exclusionary conduct.\textsuperscript{25} They deal with all devices by which firms may increase their rivals' costs of doing business, which (by increasing the price rivals must charge) lead to higher prices and the associated losses. Theoretical work such as this contains many insights that improve our understanding of the operation of markets. The question is not whether the theory is useful but whether it should be used to condemn as opposed to study business practices. Their work, however, does not contain a single example that would support a confident conclusion that firms raised rivals' costs in a way that permitted them to increase their own prices and profits. (If firms can't increase their own profits, they will be deterred automatically by the losses, making judicial intervention unnecessary.) Professors Krattenmaker and Salop's central example is from \textit{Klor's v. Broadway-Hale Stores}.\textsuperscript{26} The authors could hardly have picked a case less likely to support their point. Broadway-Hale enlisted the agreement of ten suppliers to cut off a rival re-

\textsuperscript{22} Id. at 296-97.
\textsuperscript{23} Id. at 297.
\textsuperscript{24} In addition to discussing strategic interactions, Prof. Williamson also suggests qualifications to the five filters that I proposed for antitrust claims in \textit{Antitrust Limits}, supra note 6, at 19-39. Williamson, supra note 21, at 281-89. I generally agree with his observations about these filters.
\textsuperscript{25} Krattenmaker & Salop, \textit{Anticompetitive Exclusion: Raising Rivals' Costs to Achieve Power Over Price}, 96 YALE L.J. 209 (1986). For an assessment of the extent to which this approach is different from more traditional inquiries into horizontal market power and exclusionary conduct, see T. Brennan, \textit{Understanding Raising Rivals' Costs}, U.S. Dep't of Justice Working Paper EAG 86-16 (Sept. 26, 1986).
\textsuperscript{26} 359 U.S. 207 (1959).
There were at least a thousand more retailers in Los Angeles unaffected by this agreement, so if Klor's costs went up, it is still impossible to see how Broadway-Hale's prices could rise or why manufacturers would cooperate in any practice that raised the dealer's margin and therefore reduced the manufacturers' own sales. The merger in *United States v. Von's Grocery* produced stupendous market power compared with the arrangement in *Klor's*.

The Krattenmaker-Salop treatment of *Klor's* is notable principally for its neglect of competing explanations of the "boycott," such as a desire to cut off a hole-in-the-wall store that invited people to shop at Broadway-Hale and buy next door at a firm that had fobbed off costly display and selling services on an uncompensated Broadway-Hale. It does not help the understanding of antitrust to focus attention on practices that cannot raise prices, yet might be beneficial—especially when a principal effect of the "new" focus is to direct attention away from trying find out whether there were indeed benefits. Even if Broadway-Hale had the power to raise prices, we could not decide whether to condemn or praise its conduct until learning whether B-H's actions enabled it to realize some economies.

The inquiry into rivals' costs simply repackages old questions. If Alcoa gets the agreement of some generators of electricity not to sell to rivals (another of the Krattenmaker-Salop examples) we shall have to ask some standard questions. Did Alcoa sign up *enough* generating firms to create market power at the generating level? If not, rivals' costs will not be raised; but if so, we could look at the arrangement as one producing horizontal market power among generators without thinking of rivals' costs. Did the arrangement yield more profit to Alcoa than the cost of paying for the exclusivity? Alcoa might have to line up 100 generating stations to affect rivals' costs, yet rivals could enter by finding a single supplier, which suggests an unfavorable outcome for Alcoa. Did Alcoa's contracts raise rivals' costs or lower Alcoa's? If the former, there is a problem; if the latter, Alcoa should have our thanks. Contracts of this character could do either.

To illustrate this last point, suppose Alcoa wants to expand its output. To do this it needs electricity. Generating plants take a long time to build, and Alcoa's needs might not consume the output of a whole plant. Alcoa might be best off if it could induce suppliers to build plants that are slightly larger, creating low-cost generating capacity on which it can draw to make aluminum later. Generators of electricity, however, are unlikely to speculate on Alcoa's plans or to build excess capacity (for which state regulators will not

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28. This is an application of Robert Bork's insight that theories of vertical foreclosure obscure the appropriate question: whether the "vertical" ploy has lined up horizontal power at some stage of production. *R. Bork, The Antitrust Paradox* 237-38 (1978).
let them charge). So Alcoa might decide to finance the construction of additional generating capacity, which will be “idle” for a time but ultimately reduce the cost of making aluminum as Alcoa grows. If Alcoa puts up money to enlarge a plant’s capacity, it will not want rival firms to reap where they have not sown; it will insist on exclusivity or preferential treatment. So when we see Alcoa paying money for exclusive dealing contracts with firms from which Alcoa is not yet buying electricity, are we looking at higher current costs for rivals or lower future costs for Alcoa? Nothing in the framework Krattenmaker and Salop have offered helps us answer this essential question. We might be able to answer it by asking whether Alcoa tried to line up a large fraction of all suppliers of electricity—if yes, it looks less like Alcoa is providing for its own growth, but this is also the inquiry into market power Krattenmaker and Salop want to avoid. We also could ask in retrospect whether Alcoa started to buy from these generating firms within ten years of the signing of the contract, or whether Alcoa’s net prices of electricity from these suppliers turned out to be lower than its costs from other firms with which it did not contract in advance, but information of this character is almost always unavailable to courts asked to determine at the outset whether contracts should be condemned. The comparative advantage in resolving these issues lies elsewhere, at least on the demonstrations so far.

Professor Scherer’s essay observes that many conglomerate mergers do not work out, are inefficient. Conceded. He also finds that many of the unsuccessful acquisitions are spun off again. This is divestiture without antitrust, an example of market processes working at low transaction costs. Managers learn first about the failure of a merger, because they get the message in reduced profits. This picture of acquisitions and voluntary divestitures suggests the comparative advantage of markets over courts in dealing with unsuccessful combinations. We should also consider that upwards of ninety percent of all new products are flops, that most research projects do not produce useful innovations, that most patents are never put into production, that most new firms fold up within five years, and that few restaurants last even that long. Do we infer from these data that new products, research projects, patented inventions, corporations, and restaurants are detrimental, or that it would not be troubling to suppress them through antitrust? Managers want profits, yet fail to produce them through mergers and inventions alike. The right system of incentives is one that uses the losses of unsuccessful ventures to deter inappropriate risk-taking; a system that magnified these losses would make things even worse. Antitrust could be such a loss-magnifier.

The data Professor Scherer presents do not lead to any strong conclusion

about merger policy. We still have four principal hypotheses about any given merger: (1) that it reduces the costs of production (is "efficient") and therefore is profitable; (2) that it is indifferent or mistaken and therefore leaves profits unaffected or lower; (3) that it increases the probability of cartelization or dominant firm behavior and therefore is profitable (but should be condemned); and (4) that it reduces the elasticity of supply of rival firms and therefore is profitable (but should be condemned). To show that a significant number of mergers fall in category (2) is not to show what proportion of the remaining mergers fall into categories (1), (3), and (4), or whether courts can tell them apart. Courts should ignore category (2) as self-deterring; it is both unnecessary and unwise to add to these losses, for adding to the losses of failure makes risk-taking less common even if the risks are, on balance, likely to be beneficial.30 Categories (3) and (4) should be condemned, but only if condemnation does not drag down category (1) mergers and even then only if—as I keep emphasizing—judges can find and undo category (3) and (4) mergers faster than rivalrous forces will.

Professor Comanor is concerned, like Professors Scherer and Spence before him, with vertical restrictions on dealers' conduct that increase output yet may reduce consumers' welfare.31 This may occur if the change in product attributes and quality accompanying the restraint (such as increased point-of-sale service) is more beneficial to the marginal consumers than to others who would buy anyway. The accompanying figure shows one such possibility, in which the vertical restraints lead the prior demand schedule ($D_1$) either to shift straight up (to $D_2$) or rotate (to $D_3$).

30. The identification of apparently losing mergers is of ambiguous significance for efficient organization of production. Mergers, whether or not "successful" from the buyers' perspectives, permit entrepreneurs whose product and plant gambles do not pay off to withdraw without bankruptcy. They also enable entrepreneurs to cash out and diversify their holdings. Both effects make people more willing to start new ventures, which on balance is highly beneficial. One cannot affect the way firms leave the market without influencing how many enter and how fast they will grow.

In either case quantity increases from \( q_1 \) to \( q_2 \), and price rises from \( p_1 \) to \( p_2 \). But the effects on social wealth are different. If the demand schedule shifted up to \( D_2 \), the change is efficient; if the demand schedule rotated to \( D_3 \), the change is inefficient because the inframarginal buyers, whose purchasing decision was unaffected by the change, did not find the incremental value of the new mix of product and service worth the higher price. If the vertical arrangement produced, say, more and better demonstrations by the retailer, the inframarginal buyers who relied on *Consumers' Reports* may get no gain yet suffer the higher price.

What do we make of this possibility? The two moves (to \( D_2 \) and \( D_3 \)) look identical to all econometric inquiries. Without full knowledge about the preferences of the inframarginal buyers, we are lost—yet we shall never have such knowledge. To learn whether the plight of the inframarginal buyer is a concern of antitrust, we shall have to ask different questions. For example, will such buyers be stranded without rescue by another firm? They should be easy pickings for manufacturers who emphasize barebones operations. Think of the market in small computers, for example. Apple has picked a strategy with restrictions on its dealers’ conduct, one aimed at inducing high volumes of service and information from dealers. Commodore, a rival, has picked the opposite strategy of putting a computer in a box and aiming for knowledgeable buyers (or those who can slake their desire for information
from other sources). The Macintosh and Amiga computers these firms make are substitutes, though not perfect ones. So long as the inframarginal buyer has somewhere else to go, we need not worry. Moreover, courts would lack a comparative advantage even if these buyers had nowhere else to go.

A seller desiring to supply additional information with its product can choose from several strategies. It may impose vertical restraints on dealers. It may vertically integrate, supplying services in its own stores and fixing the price there. It may change the contents of its “product.” To use small computers, again: an alternative (or supplement) to information from dealers is information in the box. Apple puts comprehensive (and expensive) manuals, tutorials, self-teaching programs, and tape recordings in the box with its computers. The informational function could be built right into the computer (the Macintosh is easier to learn and use than the Amiga because of fundamental design decisions). These, too, may be valuable only to the marginal buyer and therefore may reduce social wealth as they increase output; worse yet, they may be inferior in this regard to information delivered in retailers’ showrooms. If antitrust stifles vertical restraints on dealers, manufacturers may turn to vertical integration or product changes that are worse from consumers’ perspective yet outside the control of antitrust. This is not a welcome result of increased intervention in private arrangements between manufacturers and dealers, yet it is a possible, even a likely, one.

We need not think that things can get worse to be skeptical of the comparative advantage of courts in helping inframarginal buyers, however. I have shown that the mechanism by which these buyers lose out is the same whether the manufacturer alters the dealers’ behavior or the contents of its boxes. The economic inquiry would be the same in either case. How many people think that courts could produce a net improvement in social welfare if they were given statutory power to examine manufacturers’ decisions about what products to design? The answer must be “no one.” Yet since judicial control of design decisions is economically identical to judicial control of the retail service decisions, there is no reason to believe that judges have a comparative (or absolute) advantage at that task either. If we would not want courts to have power over design, why should we entrust courts with power over functionally identical economic matters?

Several of the presentations at this symposium, in addition to those I have mentioned, discuss mergers. All of us worry about mergers that create market power. Many at this symposium have condemned the Antitrust Division’s recent handling of mergers. Yet the last six years also created a rich vein of data. Mergers in many industries, with many degrees of concentration, now may be examined. Is there a correlation between increase in the HHI and changes in price after a merger? The structure-conduct-performance paradigm on which merger policy is based predicts yes; those who favor
more enforcement predict yes; what do the data show? Is there a correlation between increased concentration and increased managerial slack? Many who favor more enforcement predict yes, but Professor Scherer's data show that overhead is less, by about one percent, in more concentrated industries. The NAAG guidelines offer an extra invitation to collect data. Let's find the mergers of the last six years that were allowed under the federal guidelines but would have been stopped by enforcement of the NAAG guidelines. Is there a significant difference between these and the mergers allowed under both, in terms of output, price, profit, innovation (percentage of income invested in research and development), changes in imports, or other potential ways to evaluate their economic consequences? This may be a hard test to perform not only because data are scarce but also because there will not be many mergers to study. Perhaps the most interesting thing about the NAAG guidelines is that they are almost identical to the federal guidelines—they use HHI indices, with the same breaks (less than 1000 is unconcentrated, over 1800 is concentrated), the same indifference to vertical and conglomerate mergers, and the same increase-in-concentration triggers. If the federal guidelines trace their parentage to the Chicago School, then we are all Chicagoans now.

IV

I do not deny that some acts may be condemned without evidence of market power; I do not doubt that much antitrust enforcement is beneficial. My point is that we cannot simply assume that an institution of government always does more good than harm. This lesson was learned long ago about the Civil Aeronautics Board. The deregulation of the airline industry has led to decreases in air fares. Each time someone proposes that the government try to improve the results of markets, it is necessary to ask whether this form of intervention is superior to the costs of always-imperfect markets. Courts are the regulatory agencies with the most comprehensive portfolios. As they do more, they know less about each thing they influence. Courts are decentralized and have no way to assess the effects of their decisions. They do not commission empirical studies or coordinate responses to new work by social scientists. The FTC and Antitrust Division can react quickly, while courts may not even discover the data suggesting a need for reaction. Appointing officials rarely scrutinize putative judges' competence in or attitudes toward antitrust. As antitrust becomes more sophisticated, these comparative disadvantages become more important.

32. Scherer, supra note 29, at 1002.