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COMPETITION POLICY: BETWEEN ECONOMIC OBJECTIVES AND SOCIAL REDISTRIBUTION

ABSTRACT. The goals of competition policy have been long debated among economists, legal practitioners and policy makers. While the vast majority of commentators argue that the fundamental reason in the adoption and enforcement of competition law has been historically an economic one, we argue that even from its start, in nineteenth century United States of America, antitrust law has had the primary goal of social redistribution. Competition policy remains even today a public policy with sometimes implicit political objectives that could not ignore, to say the least, social effects. The protection of small producers against big producers or of consumers against producers is, in fact, a part of a social policy that is underlying the core logic of competition policy. As a public policy, social redistribution always comes at the cost of economic efficiency. We attempt to explore the potential loss in economic efficiency by the operation of competition policy. We argue that the core defining objective of competition policy is social redistribution.

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Introdusction

In an age when the traditional instruments of public interventionism (such as industrial policy or trade policy) seems to be reluctantly and rarely employed, competition policy – sometimes called „*anti-trust policy*" – is expanding its scope and activism. Its role in the mix of public policies has become one of the least controversial. Competition policy is perceived today as almost a technocratic policy. Few commentators raise questions regarding the political and social values underlying its adoption and enforcement. Moreover, economic principles seem to be today the only reason of existence of such a policy: "*the underlying precepts to the dispute are surprisingly homogenous. Both the United States and the European Union couch the relevant policy issues in exclusively economic terms. Both jurisdictions place primacy on consumer welfare...*" (Devlin and Jacobs, 2010, p. 255).

We argue that this perspective is erroneous as competition policy – like any other public policy – is based on a particular set of political values. It is one of the most powerful redistributive mechanisms in contemporary society. Economics exists only in rhetoric.

Market versus state: the logic of public interventionism

We define a market transaction as a freely-entered mutual agreement between two or more individuals through which they exchange goods or services (Rothbard, 1998, p. 40). We could include in this category of transactions both a contract and an act of charity. By the simple act of engaging in the transaction, all parties demonstrate their preference of being a counterpart of the exchange. In consequence, from an *ex ante* perspective, all market transactions maximize social welfareas „*the free market benefits all its participants*" (Rothbard, 1956, p. 28).

As opposed to a market, we define the state as the social institution that claims as being the only legitimate territorial employer of violence or „*a compulsory territorial monopolist of protection*" (Hoppe, 1999, p. 27). As the monopolist of the formulation and enforcement of legal norms, the state could extract resources from its citizens without the consent of the latter and it could also regulate the exchanges between the individuals on the market by limiting the freedom of exchange between them and even the behaviour of the isolated individual (Rothbard, 1977, p. 10). As several economists have pointed out, there is an intrinsic impossibility of assessing the costs of the state intervention in social exchanges as there is no real meaning of interpersonal comparisons of subjective utility of the citizens of the state and the loss in welfare undergone by aggressive transfers: „*there is no way of making interpersonal comparisons and measurement and no basis for saying that one person subjectively benefits more than another*" (Rothbard, 2009, p. 258).

Distribution versus redistribution

On one hand, distribution is one of the core economic processes. It is the social mechanism through which incomes derived from economic activity are allocated towards individuals acting in society. The theory of distribution differentiates between the conceptual categories of individuals as „economic agents" and recognizes that each of the core factors of production in the economy – namely land, labour and capital – should earn a distinctive form of income – namely rent, wage and interest. For example, Ricardo (Ricardo, 2005, preface) argued that:

> „*the produce of the earth – all that is derived from its surface by the united application of labour, machinery, and capital, is divided among three classes of the community; namely, the proprietor of the land, the owner of the stock of capital necessary for tis cultivation and the labourers by whose industry it is cultivated ... in different stages of society, the proportions of the whole produce of the earth which will be allotted to these three classes, under the names of rent, profit and wages, will be essentially different ... to determine the laws which regulate this distribution is the principal problem in Political Economy*"

The underlying logic of the science of economics is that it is a science of „*catallactics*"or the „*science of exchanges*" (Mises, 1996, p. 3), that is, of free economic processes which are embodied in market transactions. In consequence, the core aspect of distribution is that there is no centralized mechanism through which an authority decides how much income to be allocated to the owners of the factors of production. Income distribution is a result of personal economic calculation and actions of all the individualmembersof a particular society. The actual outcome of the distribution process is a result of a myriad of individual actions and market transactions whose broad picture is impossible to ascertain, from a historic perspective, by a single individual or institution.

On the other hand, redistribution is, as its name highlights, a process through which the original wealth and incomes obtained from market transactions by the owners of different factors of productionarereallocated (Mises, 1996, p. 691). An act of theft or an act of restitution following an act of theft is anexample of an act of redistribution. We may consider that the core dimension of „*redistribution*" is aggression or confiscation. Economists have used however the term „*redistribution*" to denote the process through which the state takes the initiative of reallocation of the wealth or incomes derived from economic activity belonging to its citizens.

A particular form of social redistribution occurs when those who are entitled to a particular income are prevented from getting it through different forms of state intervention. When the most efficient producer of a good is prevented from squeezing out from the market the less efficient producers (which are protected through different forms of „*protectionism*"), the latter are getting incomes that they would not have obtained through the market process. Protectionism in all its forms is a form of social redistribution as the less efficient suppliers of goods and services obtain incomes that they would not have obtained in absence of state intervention.

We define efficiency in economic terms as being the least means needed to obtain the same end. Efficiency considerations come into play only when individuals agree on the ends and also on the ethics of choosing the means. The most efficient producer on a market is the one who succeeds in experiencing the lowest cost in the production of the same output.

Plutocratic versus democratic redistribution

An important distinction which is made in modern social sciences regards the nature of the state and the impact of the existence of different types of political regimes. Without entering other fields of inquiry, we could make a difference in what regards the social and economic impact of the process of redistribution between what could be called plutocratic and democratic redistribution.

In a plutocratic process of redistribution, the decision makers that control the state allocate the resources and the income towards few beneficiaries. Obviously, they are a minority (50% less 1) and usually a super-minority as compared to the number of the citizens of the state. On the other hand, in a democratic process of redistribution, the beneficiaries of the redistributive process constitute the majority (50% plus 1) or a super-majority of those citizens. It is interesting to point that the number of those who provide the resources redistributed by the state does not matter too much in the discussion about the nature of the political system. Redistribution remains democratic in both cases when the state extracts resources from a super-minority or from a supermajority.

One of the core reasons of the emergence of democracy derives from the argument that the majority of the population revolted against a plutocratic system of redistribution. But Hoppe (Hoppe, 1989, page 39) has noticed that, despite its rhetoric, democracy remains a plutocratic system of redistribution in the sense that there aren'tthe majority of citizens who benefit from redistribution. By contrary, from a historic perspective, even in a democracy, there are only minorities who benefit from redistribution. The only difference from a monarchic or autocratic system could be maybe the „*free entry*" into the category of beneficiaries of redistribution.

Broad versus narrow redistribution

The taxonomy of redistribution we develop so far has to be completed with an important further argument. In practice, the state does not extract resources from the society through a single tax and redistribute it through a single subsidy. In such a simple case, any analyst would find no difficulty in ascertaining who the victim and the beneficiary of redistribution are. In fact, given the large number of mechanisms of resource extraction and redistribution by the state, there are real difficulties in calculating the net balance. For example, on the one hand, there are different categories of taxes with different incidence on the population of citizens but also the inflation of the money supply provided by fiat by the state. On the other hand, there are an entire set of resource redistribution like social security, subsidized education, subsidized healthcare, so on and its own list of beneficiaries. It is very difficult, especially in the condition of a lack of market prices, who is a net payer or who is a net beneficiary in such a complex and non-economic system.

So we could further differentiate between what could be called an aggregate (or macro-economic) redistribution and piecemeal (or micro-economic) redistribution. The first type of redistribution is of a rhetorical nature and is a democratic process. The second type of redistribution is of an actual nature and is, in fact, a plutocratic process. In other words, the broad social mechanism of redistribution at aggregate level is in fact composed by multiple mechanisms of redistribution operating at a lower or narrower level. Each of these mechanisms targets its own beneficiary group that could be – and usually is– different according to the logic of the mechanism. The consequence is that a very complex and sometimes contradictory system emerges through which, while the majority of the population benefits from redistribution at macro-level, there are only minorities who benefit from redistribution at a micro-level.

Even the principle that the burden of resource extraction falls on „*haves*" and the benefit of the resource allocation of „*have-nots*" is in itself debatable. For example, in a subsidized healthcare system, a high income wage earner with health problems could consume more resources than a healthy low income wage earner. A modest family who lives in an isolated rural area cannot benefit from national highways partly built from taxes levied from its agricultural output sold on the market. The same is true in what regards higher education (always limited to a minority), infrastructure (frequently limited to a geographical minority) and so on.

By the process of extraction of resources and their re-allocation in society, every public policy is, in fact, a process of redistribution. Otherwise, if the market distribution would have been accepted, there would not have been any need for a public policy in the first instance. The concept of redistributive public policy is a contradiction in terms. Every piece of public regulation and intervention redistributes resources from a part of population (as it consumer resources) and favours particular categories of population.

The problem of incentives

The challenge in the analysis of redistribution derives not only from the positive analysis of the transfer of resources but maybe equally important, from the incentives of individuals to engage in a market mechanisms of allocation versus a political mechanism of allocation of resources.

Individuals who engage in market transactions are, first of all, owners of the resources or of the services provided by these resources. As any owner, they have a strong interest not only in maximizing current income – which normally is the objective of any user of a resource – but also in the preservation of the capital value of their resources. Obviously, the fundamental choice derives from their time preference. There can be owners with a high time preference who prefer the rapid exploitation of their resource associated with a depletion of its capital value while there may be owners who ignore the current income in order to preserve (or even augment) the capital value. In theory, there is possible that some owners prefer the maximization of their current income irrespective of the impact on the capital value of their resource but for individuals with a lower time preference, who engage in economic calculation on a longer term, the conservation of the capital value of their assets is critical for the maintenance of cash flows in the future. Such individuals obtain the most from the distribution process when they excel in serving their market partners. This is the classical path of specialization and division of labour.

Wealth redistribution puts a further penalty on economic action on the part of those whose resources are taken over. The extraction of resources from "*haves*" reduces their incentives to save and accumulate wealth on the one hand and, on the other hand, to maximize current income. In fact, social redistribution reduces the propensity to save and increases the willingness to consume as for an individual who consumes everything he earns; there are no resources to be extracted so the personal cost of social redistribution will be minimized (Hoppe, 1988, p. 15 and ff.).

On the other hand, for the receivers of such transfers, the involvement in the division of labour and market specialization is not needed. They will receive such transfers only if the political decision-makers will choose to offer them the redistributed resources. Their welfare will depend on the attention that the state elite will award them. In order to reach that objective, such individuals are ready to build entire capital structures and put political pressures in order to divert the allocation of resources from serving the needs of the consumers to serving the objective of resource extraction. Such a capital structure and human resources are diverted from the fundamental and natural objective of maximizing social wealth (in the sense defined by Rothbard, 1956) by increasing labour specialization and advancing the division of labour in society.

In consequence, redistribution is a process that inhibits the natural incentives of individuals to act in a capital-enhancing and economizing manner for both those whose resources are extracted in order to be redistributed as well as those who benefit from redistribution. Obviously, those who benefit from redistribution will again enter into market transactions in order to fulfil their consumption needs. In consequence, redistribution not only diverts resources from the market to the state allocation but also distorts the building of capital on the market. Because of redistribution, legitimate producers would produce at different quantities of different products than on a market. Redistribution will always come at the cost of social economic efficiency. From an aggregate perspective, redistribution (when the state taxes existing wealth, like land and capital) transforms capital into income and reduces the stock of factors of production (capital goods) in society.

Competition policy in the mix of public policies

Our statement that public policies are always processes of redistribution leads us to the dilemma of how competition policy – as a particular type of public interventionism – determines such a process of redistribution. Furthermore, after we analyse the redistributive dimension of such a policy, we would explore the most probable alteration of incentives generated by this policy. The theoretical challenge is to identify the distorting economic misallocation of resources induced by a policy which claims to follow the objectives of economic efficiency.

Competition policy emerged in nineteenth century in United States of America, a predominantly market economy, as a reaction towards the perceived concentration of economic resources in the hands of a small number of big businesses. While several authors trace the origin of competition policy to the statutes of common law fighting the monopoly licenses awarded by kings, we should mention that the core reason of the adoption of competition policy at that moment in that country was the emergence of economic processes in the alleged market realm that were unacceptable by political decision makers. Economic and legal literature has long differentiated between the two types of monopoly, one awarded by the state through monopoly licenses and one emerged from the market processes, when monopoly is a result of efficiency (Hylton, 2003, pag. 1). To argue that the state legislators simply extrapolated one type of statute from an area of operation to another is misleading.

The core dilemma is whether the effects of the economic concentration were perceived to be a loss of social equality or a loss of economic efficiency. Obviously, different policy makers put a different accent and had a particular focus but we could still wonder which the dominant perspective was. Modern antitrust literature still intensely debate the reasons and the motivations of the political and economic actors that lead to the adoption of the Sherman Act in 1890, the first competition policy in the world.

There has always existed a deep controversy whether the original intent was redistribution-oriented or efficiency-oriented. In the first case, antitrust law was just another form of social redistribution through which the state, irrespective of the costs in efficiency of the enforcement of the policy, wanted to redistribute wealth and income in society in a more „*equitable*" manner. From this perspective, competition policy is a form of social equalitarianism and maybe a substitute for European inspired social security or labor-friendly legislation. In the second, case, it is argued that the competition policy was adopted and is still currently enforced as the state does not accept the loss in the efficiency of the allocation of resources in society because of the so-called anti-competitive conduct of private businesses.

Antitrust asan equalitarian policy

The first perspective on competition policy is apparently largely shared in antitrust literature in what regards the initial period of adoption and enforcement of this policy. And it is somehow obvious that, at a time when there was not a coherent economic theory to link economic concentration of businesses with loss of efficiency in the allocation of resources, the primary concern of policy makers was related to the perceived wealth inequality. Richard Hofstadter argued in 1965 that the core reason for the enactment of the Sherman Act was the goal of the policy makers to limit the economic and political power of big businesses that emerged in the American economy: „*the antitrust principle was intended to block private accumulations of power and protect democratic government … it seems to be no exaggeration to regard antitrust as being essentially a political rather than an economic enterprise*" (reprinted in Sullivan, 1991, p. 23). In consequence, it was considered critical for policy makers that the maintenance of political equalitarianism needed wealth redistribution as the control of economic resources was considered to be directly correlated with the ability to control the political process. Big national businesses could control the federal government while small businesses could not control even local governments. Obviously, the costs in social wealth were ignored.

Another related argument identified in the intent of the original framers of the antitrust lawwas that of a particular form of special interests. Several authors (Richard Hofstadter, Walter Lipmann but also George Stigler) considered that the powerful pressures of rural interests played a critical role in the adoption of the Sherman Act (see Hofstadter, 1964, p. 110). On the one hand, from a political perspective, this legislation was considered a form of reaction of „*sincere rural Toryism*" towards the political impact of the emergence of large industrial entities and, in consequence, of a new class of industrial entrepreneurs. The latter menaced the role of the class of agricultural proprietors on the political scene. From this perspective, antitrust legislation was a form of "*Corn Laws*". On the other hand, from an economic perspective, this rural constituency attacked the large industrial entities (first among them, railroads) for the alleged economic power that it exercised in relation to the agricultural interests. George Stigler highlights the fact that even before 1890, the year of the adoption of a federal antitrust legislation, there were antitrust law sat state level and the vast majority of these states were Southerner (all 5 states that adopted antitrust legislation before 1880 were from South – reprinted in Sullivan, 1991, p. 36). These two perspectives were fundamentally combined as agricultural interests were apparently dominant in America among the citizens with a right to vote.

In fact, an interesting argument emerges from this debate that concludes that competition policy is needed in order to balance the bargaining power of two categories of parties: on the one hand, entrepreneurs-capitalists who, by their ability to allocate resources inside their large firms, seem to have an asymmetrically large negotiating power. On the other hand, the atomized groups of suppliers, customers and employers with whom these large entrepreneurs-capitalists negotiate who, by their inability to mitigate the costs of coordination, experience a „tragedy of commons”. For example, AgnarSandmo argues that antitrust law cannot be enforced even in modern times on the agricultural and labour markets particularly for the reason discussed above: „*if there had been no employers organizations, there would have been a strong asymmetry of power in labour markets in favour of the employers … there are many more workers than firms, so the concentration of power is on the employers side of the market*” (in Hope, 2000, p. 14). It should be pointed out that a trade union is, from an economic point of view, nothing else than a cartel of producers of labour services. In fact, one of the most important debates in the first decades after the adoption of antitrust legislation was whether this legislation should be enforced also on labour markets or not.

Besides these categories of economic agents with whom large businesses interact as counterparts, the originators of the antitrust laws took also into consideration another category. These were the small producers who were the original competitors of those who would later become large businesses. The entrepreneurial discovery and adoption of technologies and business models that exploited the new technologies of communication, transportation and production determined in the last decades of the nineteenth century U.S.A. a significant economic restructuring of the economy. These new communication and transportation infrastructures allowed a multiplying effect in the growth of businesses and menaced the *status quo* of small and, in the new context, less efficient producers.

Even from the start, competition enforcers have argued that antitrust legislation protects „*competition not competitors*”. However, such a claim was not always substantiated in the decisions of the antitrust courts and such a qualification is valid especially before the emergence of the arguments advanced by the Chicago School of Economics. Besides the interests of the rural constituency described above, the urban class of small producers and entrepreneurs was menaced by the efficiency of new large scale businesses focused on standardization, economy of scale and rapid adoption of new technologies. Different authors spoke of the danger posed by big business to the so-called „*industrial liberty*” of such a class. It must be stressed again and again that the problem for the legislators at that moment were not the high prices asked by the new business concentrations from their customers but exactly the opposite: small prices that squeezed out small producers. Several congressmen have warned that „*trusts have made products cheaper ... [they] have destroyed legitimate competition*” (cited in Peritz, 1996, p. 15). The argument of lack of efficiency from the part of big business or that of the exploitation of the consumer through higher prices purely and simply didn’t exist at the moment of the enactment of the antitrust legislation.

Maybe no better example of how important was the protection of small competitors of large businesses was the Court decision in 1946 in ALCOA case, half a century after the enactment of the Sherman Act. It is a proof that for more than half of its existence, protection of small competitors was one of the critical issues in antitrust. In his justification, the judge of this case purely and simply ignored any efficiency consideration and highlighted that the only problem that that company had was that it was too big: "*size was not only evidence of violation, or of potential offense … it was the essence of offense. Size, meaning market control, was what competition and monopoly was about. All other aspects of the case were subordinated to the central and decisive fact that ALCOA … made, and then fabricated, or sold, over 90 per cent of the virgin aluminium used in United States*" (cited in Adams, 1951, p. 917).

So the numbers (beneficiaries versus victims) played a critical role in the adoption of the competition policy. Because of political and social arguments specific to a democratic society, policy makers attempted to limit the economic liberty of the few in order to offer an alleged benefit to the majority. It is obvious that all these arguments highlight the redistributive mechanism of competition policy as the so-called monopolists – frequently the most efficient producers in their industries – experienced a limitation of their freedom of exercise of property rights – and, fundamentally, a loss in welfare. On the contrary, while the "*protected*" beneficiaries an increase in welfare due to the ability to successfully operate under inefficiency. From this perspective, antitrust has been adopted and for a long time enforced as a result of an equalitarian perspective on the economic and political processes.

Economics in antitrust: a revolution?

Starting with the fifth decade of the last century, a slow process of intellectual re-evaluation of the logic of the antitrust policy began. It culminated with the works of the so-called "Chicago School of Economics" whose representatives such as Aaron Director, Robert Bork, Richard Posner or George Stigler questioned the basic assumptions underlying antitrust law (Posner, 1979, p. 926). As opposed to former arguments that related the market structure with anti-competitive behaviour and alleged losses in welfare, the Chicagoan antitrust scholars claimed that the number of participants on the markets was irrelevant to the efficiency of the operation of producers. An industry with only one operator could be qualified as competitive and the organization of capital goods in such an industry the most efficient. At its turn, an efficient industry maximizes economic welfare which, at its turn, is defined as the total welfare. According to mainstream economics, total welfare is the sum of what mainstream economists defines as total surplus, that is, consumer surplus and producer surplus (Motta, 2004, p. 17). According to economic literature, consumer surplus is the difference between the price that a consumer was willing to pay for a product and the price he actually paid – the market price – for that product. On the other hand, producer surplus is the difference between the market price – the price that the producer actually got from market transactions – and the costs of production.

Obviously, the statement that businesses obtain a producer surplus every time they perceive a profit is somehow clearly over passing the borders of anti-capitalistic ideology. It grossly ignores the problem of contractual liberty and the problem of incentives. It cannot accept the perspective that market transactions demonstrate, by the simple ability of the parties to enter or boycott contracts, an increase in social welfare as the parties gain from engaging in exchanges.

In fact, the correct statement of Chicagoan economists that market structures tell nothing about economic efficiency of the operation of businesses fell in derision when paired with the new objective of competition policy: consumer welfare. In other words, according to this wisdom, public authorities should maximize by their regulations and by the enforcement process only consumer surplus. According to Bork, "*consumer welfare is the only legitimate goal of antitrust*" (Bork, 1967, p. 244) and this economist even went further to reinterpret the original intent of the Sherman Act as being consumer oriented. Even some economists differentiate between the goals of enhancement of efficiency and consumer welfare, these standards are fundamentally similar as only efficient businesses succeed in maximizing consumer surplus.

Moreover, the normative recommendations of economics, namely that every time a business obtains a profit it does at the expense of the consumer (whose own surplus is reduced so his welfare experiences a loss) also has a strong underlying ideological prejudice. Contemporary economists attempt to advance values for transactions that should be qualified as fair or socially maximizing. It must be stressed that such attempts – calculating values for transactions that are different from mutually agreed prices – are futile and long ago compromised by the socialist experiment. Moreover, the ignorance of the problem of incentives for entrepreneurs-capitalists cannot lead but to the failed experiment of planned economies where governments were truly interested in consumer welfare and ignorant of the capitalist profit.

In fact, the enterprise of calculating the value that producers expropriate from consumers through the capture of as much as possible of the consumer surplus is nothing but the centuries old quest for a "*just price*". It was abandoned as naturally impossible. The same quest failed in the experiment of the planned economies where the simple lesson of the impossibility of the economic calculation in a socialist commonwealth (Mises, 1996, p. 698 and ff.) was ignored. Competition policy is nothing but a redistributive policy specific to a democracy. Its goals are buried under the alleged objective of "consumer welfare". We should mention that the term of "*consumer welfare*", which is fundamentally misleading, was advanced during one of the most redistributive and socialistic experiments of America, which was the New Deal: "*the later New Deal established "the consumer" as the unifying image for public discourse about political economy in America*" (Peritz, 1996, p. 6). Differentiating between consumers and producers is as wrong as differentiating between aggregate demand and aggregate supply. Every consumer has to be a producer (or an employee of a producer) in order to buy goods on the market. Every producer is, fundamentally, a consumer. The difference between them is given only by the point of reference. Claiming to follow consumer welfare is just an exercise of public rhetoric.

Conclusions

Several commentators have argued that competition policy is maybe the most „*economic*" public policy of the modern state. Its stated aim is to insure a state of competition in the economy in order to put pressures on firms to innovate, reduce costs and accept a „*normal*" rate of return. Lack of competition and the consequent existence of a concentrated market structure leads to ability of the producers to capture the consumer surplus. The origin and the dynamic of the competition policy could be better interpreted if we adopt as its underlying goal redistribution. Competition policy has always put in antagonism big producers against small producers and all producers against consumers. From this perspective, competitive policy has always preferred big numbers against small numbers and its core claim is that of a democratic redistribution of resources.

At the moment of the adoption of the original antitrust legislation in the U.S.A., Senator Henry M. Teller (Republican, Colorado) stated that *"I do not believe that the great object in life is to make everything cheap"* (cited in Peritz, 1996, p. 15). At that point in time, the American congressman derided the alleged objective of the large business trusts. Today, his statement is perfectly valid as regards the quest of the competition policy to increase consumer surplus by reducing, *per a contrario*, producer surplus so by making consumer prices as cheap as possible.

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