2012

Section 2 Enforcement and the Great Recession: Why Less (Enforcement) Might Mean More (GDP)

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ESSAY

SECTION 2 ENFORCEMENT AND THE GREAT RECESSION: WHY LESS (ENFORCEMENT) MIGHT MEAN MORE (GDP)

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The Great Recession has provoked calls for more vigorous regulation in all sectors, including antitrust enforcement. After President Obama took office, the Antitrust Division of the Department of Justice abandoned the Bush Administration's standard of liability under section 2 of the Sherman Act, which forbids unlawful monopolization, as insufficiently interventionist. Based on the premise that similarly lax antitrust enforcement caused and deepened the Great Depression, the Obama Administration outlined a more intrusive and consumer-focused approach to section 2 enforcement as part of a larger national strategy to combat the "extreme" economic crisis the nation was then facing.

This Essay draws on macroeconomic theory and the New Deal experience to examine the relationship between section 2 standards and macroeconomic stability. In particular, this Essay evaluates the claim that more aggressive section 2 enforcement focused on maximizing the welfare of consumers who purchase from monopolists would help forestall and ameliorate economic downturns. While empirical evidence confirms the Obama Administration's claims that New Deal efforts to cartelize prices and wages exacerbated the Depression, this Essay argues that substitution of this novel and more intrusive "consumer welfare effects" test for the Bush Administration's "disproportionality" standard would not stimulate aggregate demand, and may even reduce national output at the margins. Given the ambiguity in the aggregate impact of such enforcement, this Essay concludes that antitrust regulation should abandon any pretensions of being a tool for macroeconomic stabilization, and focus solely on identifying and condemning conduct that on balance results in a misallocation of resources and a reduction in total economic surplus. By keeping its microeconomic focus, antitrust regulation can help maximize the potential value of the gross domestic product, while monetary and fiscal policy produce sufficient aggregate demand to ensure full employment of society's resources and to achieve that potential value.

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INTRODUCTION

The Great Recession has led to reconsideration of the appropriate scope of federal regulation, and antitrust regulation is no exception. Upon taking office, President Obama's chief antitrust official opined that the Bush Administration's lax enforcement of section 2 of the Sherman Act,[1] which bans unlawful monopolization, had helped cause and exacerbate the most recent economic downturn.[2] Reasoning that New Deal-imposed cartelization had deepened and lengthened the Great Depression, the Obama Administration argued that the previous administration should have attacked more monopolies under section 2 to encourage competition and reduce prices in monopolized markets.[3] The new administration repudiated the Bush Administration's lengthy report on section 2 enforcement policy, which concluded that section 2 bans monopolistic conduct that imposes harm on consumers in the relevant market that is disproportionate to any

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1. 15 U.S.C. § 2 (2006) ("Every person who shall monopolize, or attempt to monopolize, . . . any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony . . . .").

2. *See* Christine A. Varney, Assistant Att'y Gen., U.S. Dep't of Justice Antitrust Div., Vigorous Antitrust Enforcement in this Challenging Era 4–9 (May 11, 2009), *available at* http://www.justice.gov/atr/public/speeches/245711.pdf; *infra* notes 51–57 and accompanying text.

3. *See* Varney, *supra* note 2, at 2–9; *infra* notes 45–57 and accompanying text.

efficiencies it creates.[4] Ironically, this approach already was a more interventionist standard than that contained in decades of section 2 case law, whereby courts provided a safe harbor for efficient conduct by monopolists, regardless of the impact of such conduct on prices in the relevant market and without comparing the benefits of such efficiencies to consumer harm.[5] Although the Obama Administration did not articulate a precise standard it would employ under section 2, it contended that section 2 enforcement should focus more on the welfare of consumers in monopolized markets, rather than efficiencies that benefit producers.[6] This implied that the Antitrust Division would apply the so-called "consumer welfare effects" standard, which several academics and a progressive antitrust think tank had advocated,[7] but which the U.S. Supreme Court has implicitly rejected on several occasions.[8] The new administration claimed that this more aggressive standard would have prevented the Great Recession, or at least mitigated its severity.[9]

While the withdrawal was no surprise, given *candidate* Obama's 2007 statements criticizing President Bush's antitrust enforcement record,[10] the rationale was both novel and surprising. By comparing Bush's less intrusive "disproportionality" standard to the New Deal cartelization policies that deepened and lengthened the Depression, Obama's antitrust chief suggested that section 2 enforcement can serve as a tool for macroeconomic stabilization, a task usually reserved for fiscal and monetary policy. This Essay evaluates the claim that more aggressive section 2 enforcement implementing a consumer welfare effects test would in fact forestall and ameliorate economic downturns.

While empirical evidence confirms that the National Industrial Recovery Act of 1933[11] (NIRA) and subsequent New Deal efforts to cartelize prices and wages deepened and lengthened the Depression,[12] the New Deal experience with coercive cartelization and relaxed antitrust enforcement does not support the Obama Administration's call for more aggressive section 2 enforcement. Simply put, any analogy between the massive cartelization of the 1930s and the Bush Administration's antitrust enforcement policy is strained at best. Even its critics concede that the Bush Administration aggressively pursued horizontal price fixing under

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4. *See* Varney, *supra* note 2, at 8–9; *infra* notes 32–38 and accompanying text.

5. *See infra* notes 58–74 and accompanying text.

6. *See* Varney, *supra* note 2, at 9–14; *infra* notes 40–43 and accompanying text.

7. *See, e.g.*, THE NEXT ANTITRUST AGENDA: THE AMERICAN ANTITRUST INSTITUTE'S TRANSITION REPORT ON COMPETITION POLICY 67 (Albert Foer ed., 2008) [hereinafter AAI TRANSITION REPORT]; *infra* notes 23–29, 76–80 and accompanying text.

8. *See infra* notes 58–74 and accompanying text.

9. *See* Varney, *supra* note 2, at 5.

10. *See generally* Barack Obama, *Statement of Senator Barack Obama for the American Antitrust Institute*, AM. ANTITRUST INST. (Sept. 26, 2007), http://www.antitrustinstitute.org/files/aai-%20Presidential%20campaign%20-%20Obama%209-07_092720071759.pdf.

11. Ch. 90, 48 Stat. 195 (previously codified at 15 U.S.C. §§ 701–712 (Supp. 1933)), *invalidated by* A.L.A. Schechter Poultry Corp. v. United States, 295 U.S. 495 (1935).

12. *See infra* notes 190–203 and accompanying text.

section 1 of the Sherman Act.[13] Thus, any argument that more aggressive enforcement would have helped prevent and mitigate the recent downturn must focus solely on the enforcement of section 2, and evaluate the impact of more aggressive enforcement on aggregate demand, aggregate supply, and thus national gross domestic product (GDP).

This Essay argues that substitution of a novel and more intrusive consumer welfare effects test for the Bush Administration's disproportionality standard would not stimulate aggregate demand and may even reduce national output at the margins. For one thing, the economic impact of section 2 enforcement is likely quite modest. The government has brought few such cases in the last two decades, cases that collectively had only a miniscule impact on the overall economy.[14] More tellingly, in the more than two years since the Obama Antitrust Division announced a more aggressive enforcement posture, it has brought only one section 2 case—against a hospital earning less than $300 million per year in revenues and serving a town with just over 100,000 residents.[15] At the same time, the Obama Administration has sought to boost the prerogatives of labor unions, thereby encouraging the cartelization of labor, reducing the flexibility of wages, and counteracting the supposed effect of anti-monopoly enforcement.

In any event, it is by no means clear that the impact of more aggressive enforcement, modest though it may be, would be positive. All section 2 standards will ban some conduct that raises the prices consumers pay in the relevant market. Because the Bush Administration's disproportionality test was already more aggressive than the standard articulated by the Supreme Court, any evaluation of the macroeconomic impact of an even more aggressive enforcement posture implementing the novel consumer welfare effects test must focus on that category of previously lawful conduct that this more intrusive standard would condemn. This kind of conduct bears only passing resemblance to the naked cartel price fixing that New Deal legislation imposed. Such conduct would have survived scrutiny under the less intrusive disproportionality standard only because it produces significant efficiencies.[16] The positive welfare effects of this conduct's efficiencies will almost always outweigh—sometimes by a wide margin—the negative consequences of the misallocation of resources resulting from reduced output in the monopolized market.[17] Thus, unlike a ban on cartel price fixing, which will invariably enhance the allocation of resources and

13. 15 U.S.C. § 1 (2006) ("Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations is declared to be illegal."); *see* AAI TRANSITION REPORT, *supra* note 7, at 21 (praising both President Bush's and President Clinton's enforcement of section 1); *infra* note 220 and accompanying text.

14. *See infra* notes 221–26 and accompanying text.

15. *See* Press Release, U.S. Dep't of Justice, Justice Department Reaches Settlement with Texas Hospital Prohibiting Anticompetitive Contracts with Health Insurers (Feb. 25, 2011), http://www.justice.gov/opa/pr/2011/February/11-at-249.html.

16. *See infra* notes 81–83 and accompanying text.

17. *See infra* notes 241–45 and accompanying text.

improve overall economic welfare, the consumer welfare effects test will reduce overall welfare by banning practices that create more economic value than they destroy.

Although this conduct will increase prices in the monopolist's market, thereby pushing the nation's aggregate prices in an upward direction, the efficiencies banned by a consumer welfare effects test have economic consequences beyond the monopolized market. These efficiencies free up real resources that the monopolist had previously employed, which then flow to their next best use in other markets. This increases the supply of available inputs in such markets and reduces the cost of producing any given level of output. The result will likely be more output at lower prices in other markets, counteracting, at least in part, the price increase in the monopolized market.[18] In addition, the flow of resources to other markets will also increase the economy's total potential output. Even if output reduction in the monopolized market prevents realization of this full potential, it is likely that output increases in other markets will outweigh the monopolistic output reduction, resulting in higher actual and potential national output than if courts banned the monopolist's efficient conduct.[19] Indeed, straightforward application of the consumer welfare effects test will ban some conduct that produces out-of-market efficiencies that vastly exceed any harm suffered by consumers in the relevant market. It therefore stands to reason that some applications of the consumer welfare effects test will actually reduce national output and increase overall prices.

It would be difficult to determine the overall impact of challenged conduct on the aggregate price level and potential output in any particular case, and antitrust courts should not attempt to do so. This Essay concludes that the consumer welfare effects test's proponents will find it difficult to invoke macroeconomic considerations in support of this novel and more intrusive standard of liability, given the propensity of the conduct it bans to create more economic value than it destroys. Instead, antitrust regulation should focus on what it does best: identifying and condemning conduct that on balance results in a misallocation of resources and a reduction in total economic surplus. Banning additional conduct in the name of macroeconomic stabilization will prevent the movement of resources to their most productive use and, presumably, reduce society's potential output in the long run. By keeping its microeconomic focus, antitrust regulation can help maximize the potential value of GDP, while monetary and fiscal policy produce sufficient aggregate demand to ensure full employment of society's resources and the achievement of that potential.

This Essay proceeds in four parts. Part I reviews the Antitrust Division's rejection of the disproportionality standard articulated by the Bush Administration and its apparent embrace of the more aggressive consumer welfare effects standard, on the grounds that application of this standard could have helped stave off or mitigate the most recent economic downturn.

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18. *See infra* notes 246–62 and accompanying text.

19. *See infra* notes 263–68 and accompanying text.

This part also outlines the so-called consumer welfare effects standard, which would, contrary to Supreme Court precedent, ban all conduct that raises prices in the relevant market regardless of efficiency consequences and satisfy the Obama Administration's singular focus on the welfare of consumers in monopolized markets.

Part II examines antitrust enforcement before and during the Great Depression, with particular attention to the NIRA. The Obama Administration's account of the historical relationship between antitrust and the Depression is basically sound, in that President Roosevelt advocated and enforced a massive scheme of coercive cartelization that governed more than 500 industries.[20] At the same time, this account all but ignores the New Deal's anticompetitive cartelization of labor, first via NIRA codes and then through the 1935 National Labor Relations Act, which both strengthened the hand of organized labor and resulted in a doubling of union membership and vast increases in the number of firms subject to collusive wages.

Part III employs the basic macroeconomic model of aggregate supply and demand to analyze the New Deal experience and derive lessons about the appropriate role, if any, of antitrust policy in stabilizing the macroeconomy. Application of this model, and more recent empirical work, confirms the then-contemporaneous prediction by John Maynard Keynes and others that the NIRA's wage and price fixing provisions would deepen and lengthen the Depression.

Finally, Part IV evaluates the claim that more aggressive section 2 enforcement pursuant to a consumer welfare effects test would have helped stave off the Great Recession, or at least have hastened recovery. This part demonstrates that the impact of more aggressive enforcement is likely quite modest; more than three years through its first term, the Obama Administration has brought only one section 2 suit against a local monopolist with no impact on the national economy. In any event, it is by no means clear that the impact of more aggressive enforcement, modest though it may be, would be positive. Unlike New Deal wage and price cartels, conduct uniquely condemned by the consumer welfare effects test produces significant efficiencies, which more than outweigh the deadweight loss resulting from such conduct. As a result, condemning such conduct will likely reduce the income of producers more than it will increase the income of consumers, thereby undermining any claim that banning such conduct will increase overall consumer spending. Moreover, while banning such conduct will reduce prices in monopolized markets, such condemnation will also eliminate significant efficiencies that would free up resources available to other markets and thus increase output and reduce prices in other sectors. Such efficiencies would also impact the aggregate supply curve and increase the economy's potential output. Thus, while application of a consumer welfare effects test would reduce prices in monopolized markets, the destruction of efficiencies and thus prevention of

20. *See* Varney, *supra* note 2, at 2–4; *infra* notes 111–24 and accompanying text.

potential price reductions in other markets would attenuate any effect on aggregate demand in the short run and reduce the economy's potential output in the long run.

I. TOWARD A NEW SECTION 2 STANDARD: PROTECTING (SOME) CONSUMERS FROM MONOPOLY TO STABILIZE THE ECONOMY

The 2008 election of Barack Obama signaled that the federal government would take a more aggressive regulatory posture, and antitrust regulation was no exception. This part reviews the Obama Administration's repudiation of the Bush Administration's section 2 enforcement policy. This part also explores the new Administration's promise to attack monopolies more aggressively under a novel and more intrusive standard of liability, based on the claim that such enhanced enforcement could have helped stave off—or at least mitigated—the Great Recession. Finally, this part examines the content and effects of this new standard.

A. The Antitrust Division Takes on the Great Recession: President Obama's New Section 2 Standard

By 2008, it was commonplace among progressives to say that President Bush's Antitrust Division had been too easy on monopolies. While campaigning for President in 2007, Senator Obama claimed that the Bush Administration had "what may be the weakest record of antitrust enforcement of any administration in the last half century."[21] In particular, he focused on the fact that "in seven years, the Bush Justice Department has not brought a single monopolization case" under section 2 of the Sherman Act, which bans unlawful monopolization.[22] Shortly before the 2008 election, numerous former enforcement officials, known for their pro-regulation views, contributed to a report published by the American Antitrust Institute (AAI), a pro-regulation think tank, which echoed candidate Obama's concerns.[23] The AAI report was sharply critical of the Bush Administration's purportedly "lax" approach, which it characterized as a "virtual interment of Section 2."[24] It repeated the claim—made previously by some of its academic co-authors and a former chairman of the Federal Trade Commission[25] (FTC)—that section 2 law should ban conduct

21. *See* Obama, *supra* note 10, at 1; *see also* Daniel Crane, *Obama's Antitrust Agenda*, 32 REGULATION, Fall 2009, at 16 (describing then-candidate Obama's rhetorical commitment to a more interventionist antitrust enforcement posture).

22. Obama, *supra* note 10, at 1; *see also* Sherman Act, 15 U.S.C. § 2 (2006).

23. *See* AAI TRANSITION REPORT, *supra* note 7, at vii–ix (listing numerous contributors to the report, many of whom previously served at the Federal Trade Commission (FTC) and/or the Antitrust Division of the Department of Justice (DOJ)).

24. *See id.* at 58–65.

25. *See* Jonathan B. Baker, *Competition Policy as a Political Bargain*, 73 ANTITRUST L.J. 483, 523 (2006) (contending that antitrust law should ban all practices that injure consumers in the relevant market unless doing so would sacrifice very large efficiencies in a particular case); John B. Kirkwood & Robert H. Lande, *The Fundamental Goal of Antitrust: Protecting Consumers, Not Increasing Efficiency*, 84 NOTRE DAME L. REV. 191, 201, 203 (2008); Robert Pitofsky, *Past, Present and Future of Antitrust Enforcement at the Federal*

that injures the welfare of purchasers or "consumers" in the relevant market, even if such conduct would increase total welfare by creating more wealth than it destroys.[26] Like Obama, the AAI lamented the fact that the Bush Administration had initiated no monopolization cases, compared to the at least seven[27] such cases brought during the Clinton Administration.[28] Around the same time, three FTC commissioners issued a joint statement repeating the AAI's ahistorical claim that section 2 case law focuses exclusively on the welfare of consumers in the monopolized market, without regard to whether efficiencies benefitted other consumers, such as the owners of the firms charged with monopolization.[29]

Thus, President Obama's approach to antitrust enforcement after his election was hardly surprising. Days after his inauguration, the President nominated Christine Varney, a former FTC commissioner during the Clinton Administration, to serve as head of the Antitrust Division in the Department of Justice (DOJ).[30] Just three weeks after her confirmation in

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Trade Commission, 72 U. CHI. L. REV. 209, 217 (2005) (endorsing a comparison of efficiency effects with adverse impacts on consumers in the market served by the monopolist); Steven C. Salop, *Exclusionary Conduct, Effect on Consumers, and the Flawed Profit-Sacrifice Standard*, 73 ANTITRUST L.J. 311, 355–56 (2006). Professors Baker, Kirkwood, Lande, and Salop were contributors to the AAI Report. *See* AAI TRANSITION REPORT, *supra* note 7, at ix. Professor Pitofsky was Chairman of the Federal Trade Commission during the Clinton Administration. *See Commissioners and Chairmen of the Federal Trade Commission: 1915–2010*, FTC, http://ftc.gov/ftc/history/commisioner chartlegal2010.pdf (last updated Oct. 2010) [hereinafter *FTC Commissioners*].

26. *See* AAI TRANSITION REPORT, *supra* note 7, at 67 (claiming that "net consumer welfare is ordinarily the touchstone of antitrust analysis" (citing Salop, *supra* note 25, at 329–31)). As I have explained elsewhere, Professors Salop, Lande, Kirkwood, Pitofsky, and Baker equate "consumer welfare" with the welfare of purchasers in the market served by the purported monopolist, thereby ignoring the welfare of consumers who do not happen to purchase items produced by the monopolist. *See* Alan J. Meese, *Debunking the Purchaser Welfare Account of Section 2 of the Sherman Act: How Harvard Brought Us a Total Welfare Standard and Why We Should Keep It*, 85 N.Y.U. L. REV. 659, 662–63 (2010). The U.S. Supreme Court has implicitly rejected such an approach on numerous occasions. *See infra* notes 58–74 and accompanying text (explaining that the Supreme Court has repeatedly articulated a standard of liability inconsistent with the consumer welfare effects test endorsed by these scholars).

27. One scholar has reported that the Clinton DOJ brought only seven section 2 cases. *See* William Kovacic, *The Modern Evolution of U.S. Competition Policy Enforcement Norms*, 71 ANTITRUST L.J. 377, 449 (2003). An independent review of the record reveals twelve such cases, a list of which is on file with the author. *Cf.* Crane, *supra* note 21, at 16–18 (contending that then-candidate Obama overstated the laxity of the Bush Administration's antitrust enforcement).

28. *See* AAI TRANSITION REPORT, *supra* note 7, at 58–59. As the report noted, the Bush Administration continued to pursue two of these seven cases by appealing adverse rulings. *See id*. at 59 n.6.

29. *See* Pamela Jones Harbour, Jon Leibowitz, & J. Thomas Rosch, *Statement of Commissioners Harbour, Leibowitz and Rosch on the Issuance of the Section 2 Report by the Department of Justice*, FTC, at 1 (Sept. 8, 2008), http://www.ftc.gov/os/2008/09/080908 section2stmt.pdf.

30. *See* Eric Lichtblau, *Obama Picks Critic of Warrantless Wiretapping for Slot at Justice Dept.*, N.Y. TIMES CAUCUS (Jan. 22, 2009, 7:10 PM), http://thecaucus.blogs.nytimes.com/2009/01/22/obama-picks-critic-of-warrantless-wiretapping-for-slot-at-justice-dept/.
Ms. Varney served on the FTC from 1994 until 1997. *See FTC Commissioners*, *supra* note 25.

late April 2009,[31] the Antitrust Division issued a press release announcing a change in its section 2 enforcement policy.[32] In particular, the release withdrew a lengthy report entitled *Competition and Monopoly: Single Firm Conduct Under Section 2 of the Sherman Act*[33] (Section 2 Report), which President Bush's Antitrust Division had issued in September 2008.[34] Adopted after twenty-nine panel discussions and copious written testimony, the ten-chapter Section 2 Report consumed 180 pages, covering topics such as how to define monopoly, standards to govern various categories of conduct alleged to constitute unlawful exclusion, and appropriate remedies for conduct found to violate section 2.[35] Among other things, the report announced the Division's belief that a monopolist's conduct that produced significant efficiencies would nonetheless contravene section 2 if it imposed harm on consumers in the relevant market that was "disproportionate" to the efficiency benefits of such conduct.[36] In so doing, the Division had rejected the less intrusive "no-economic-sense test," under which a monopolist's conduct avoids condemnation, regardless of its impact on market consumers, if it produces economic benefits for the monopolist unrelated to any exclusionary impact on rivals.[37] The Division had also rejected the more intrusive "consumer welfare effects test," which would ban any conduct that resulted in higher consumer prices, even when such

31. *See* Kate Phillips & Bernie Becker, *Early Word: Tree-Planting Reunions*, N.Y. TIMES CAUCUS (Apr. 21, 2009, 9:19 AM), http://thecaucus.blogs.nytimes.com/2009/04/21/early-word-tree-planting-reunions/ (noting under the heading "Up in Congress" that "the Senate confirmed . . . Christine Varney [to head] the Antitrust Division").

32. *See* Press Release, U.S. Dep't of Justice, Justice Department Withdraws Report on Antitrust Monopoly Law (May 11, 2009), http://www.justice.gov/opa/pr/2009/May/09-at-459.html.

33. U.S. DEP'T OF JUSTICE, COMPETITION AND MONOPOLY: SINGLE-FIRM CONDUCT UNDER SECTION 2 OF THE SHERMAN ACT (2008) [hereinafter SECTION 2 REPORT], *available at* http://www.justice.gov/atr/public/reports/236681.pdf (withdrawn May 11, 2009). The Federal Trade Commission had never joined the report. *See* Harbour et al., *supra* note 29.

34. *See* Press Release, U.S. Dep't of Justice, *supra* note 32.

35. *See, e.g.*, SECTION 2 REPORT, *supra* note 33, at ch. 2 ("Monopoly Power"); *id.* at ch. 4 ("Price Predation"); *id.* at ch. 5 ("Tying"); *id.* at ch. 6 ("Bundled Discounts and Single-Product Loyalty Discounts"); *id.* at ch. 10 ("An International Perspective").

36. *See id.* at 46–47; *id*. at ix ("[T]he [disproportionality test] focuses on the consumer-welfare goals of antitrust and represents the best combination of effectiveness and administrability . . . .").

37. *See id.* at 39–40 (describing the "no-economic sense test"); *id*. at viii–ix (claiming that the no economic sense test would immunize conduct that produced trivial benefits even if it was significantly harmful to consumers); *id.* at 43 (claiming that, under a no economic sense test "conduct could be protected even if it contributed virtually no profits (for example, only $1 of profit) apart from its exclusionary effect but caused tremendous harm to the competitive process"); *see also* Gregory J. Werden, *Identifying Exclusionary Conduct Under Section 2: The "No Economic Sense" Test*, 73 ANTITRUST L.J. 413, 413 (2006) (explaining that, under the "no economic sense" test, a monopolist only violates section 2 if its conduct "would make no economic sense for the defendant but for the tendency to eliminate or lessen competition"); *cf.* A. Douglas Melamed, *Exclusive Dealing Agreements and Other Exclusionary Conduct: Are There Unifying Principles?*, 73 ANTITRUST L.J. 375, 389–403 (2006) (advocating adoption of the "sacrifice," also known as the "no economic sense," test).

conduct creates efficiencies that outweigh any economic losses from such conduct.[38]

On the same day that the DOJ withdrew the Section 2 Report, Ms. Varney explained the Antitrust Division's action in a speech to the Center for American Progress.[39] Among other things, she claimed that the Section 2 Report, particularly its "disproportionality" test, leaned too far in the direction of fostering efficiencies and "understate[d] the importance of redressing exclusionary and predatory acts that result in harm to competition, distort markets, and increase barriers to entry."[40] The "ultimate result" of the disproportionality test, she said, was that "consumers are harmed through higher prices, reduced product variety and slower innovation."[41] This undue focus on mere "efficiencies" at the expense of consumers injured by high prices, she said, reflected a departure from tried and true antitrust principles contained in major section 2 decisions, which she claimed required a more aggressive stance toward monopolists' exclusionary conduct.[42] Ms. Varney did not express concern for all consumers, but only those who happened to purchase the product sold by the monopolist in question. Thus, her argument prioritizes the welfare of these particular consumers over that of, say, the monopolist's shareholders, who are also consumers and would reap the benefits of lower costs and higher prices that result from practices facilitating the exercise of monopoly power and simultaneously creating efficiencies.[43]

While the withdrawal of the Section 2 Report was not surprising, the rationale for more aggressive enforcement was intriguing, to say the least. The nation was in a "distressed economy," Ms. Varney said,[44] similar to that experienced during prior "economic crises."[45] It was therefore appropriate to draw on the nation's "prior experience in responding" to such crises.[46] She claimed the current crisis was reminiscent of the Great Depression, which had followed a period of relaxed antitrust enforcement and resulting cartelization of numerous industries during the 1920s.[47] Once

38. *See* SECTION 2 REPORT, *supra* note 33, at 45–46 (rejecting the consumer welfare effects test).

39. *See generally* Varney, *supra* note 2. Ms. Varney stepped down from her position as Assistant Attorney General in July 2011 to join Cravath, Swaine & Moore LLP. *See* Press Release, Cravath, Swaine & Moore LLP, Christine A. Varney Joins Cravath (Sept. 6, 2011), http://www.cravath.com/Christine-A-Varney-Joins-Cravath-09-06-2011/. Because the Obama Administration has indicated no intention to alter its section 2 enforcement strategy, this Essay will attribute the policy and rationale that Ms. Varney articulated in her speech to the Obama Administration generally.

40. *See* Varney, *supra* note 2, at 7.

41. *Id*.

42. *See id.* ("Accordingly, I believe the Section 2 Report loses sight of an ultimate goal of antitrust laws—the protection of consumer welfare.").

43. *See* Meese, *supra* note 26, at 670–73 (describing different definitions of "consumer welfare").

44. Varney, *supra* note 2, at 19.

45. *Id.* at 2.

46. *Id.*

47. *Id.* ("Th[e] lack of interest in antitrust enforcement [that followed World War I] continued through the 1920s.").

the Depression began, she said, the national government had erred by suspending antitrust enforcement and enforcing so-called "codes of fair competition," which were adopted and imposed under the NIRA.[48] Such codes imposed cartel pricing and output restrictions, which raised prices and reduced consumer welfare and purchasing power.[49] In short, she said, "the welfare of firms took priority over the welfare of consumers."[50]

Ms. Varney opined that the nation's experience with lax antitrust enforcement and the Great Depression "raises the question of whether current economic challenges reflect a 'failure of antitrust'"—that is, "could United States antitrust authorities have done more" before the most recent downturn?[51] Ms. Varney answered her own rhetorical question in the affirmative, claiming that the Bush DOJ had, "with the exception of cartel enforcement," given "firms . . . room to run with the idea that markets 'self-police'" and the view that "authorities should wait for markets to 'self-correct.'"[52] The public, she said, had been "waiting for this 'self-correction,'" as well as "spurred innovation" and "enhanced consumer welfare," but instead saw "numerous markets distorted" and watched "firms fail and take American consumers with them."[53] Along with "ineffective government regulation, [and] ill-considered deregulatory measures," Ms. Varney claimed "inadequate antitrust oversight contributed to the current conditions."[54] These "extreme conditions," she said, "require a recalibration of economic and legal analysis and theories," and a "sound competition policy as part of our nation's economic strategy."[55] This strategy would include repudiation of the disproportionality standard, which was slanted too much in the direction of firms and "possible efficiencies."[56] The obvious implication was that more intrusive enforcement of section 2 could have helped prevent the economic downturn in the first place and that such aggressive enforcement, along with a larger national strategy, would help foster recovery from the Depression-like "extreme" crisis that the nation now faced.[57]

B. The Content and Effects of a More Intrusive Section 2 Standard

In her speech explaining the withdrawal of the Section 2 Report, Ms. Varney did not explain which enforcement standard would replace that endorsed by the Bush Administration.[58] Instead, she claimed that the DOJ

48. *Id.* at 2–3.
49. *Id.* at 3.
50. *Id.*
51. *Id.* at 4.
52. *Id.*
53. *Id.*
54. *Id.* at 4–5.
55. *Id.* at 5.
56. *Id.* at 7.
57. *Id.* at 5; *see* Crane, *supra* note 21, at 16–17 ("Varney has gone so far as to suggest that the economic crisis is partly attributable to lax antitrust enforcement.").
58. Varney, *supra* note 2, at 9 ("[T]he Department is not proposing any one specific test to govern all section 2 matters at this time.").

would simply enforce the principles announced in two important Supreme Court decisions and three appellate court decisions, including the D.C. Circuit's 2001 *United States v. Microsoft Corp.*[59] decision.[60] This assertion raised more questions than it answered, however. After all, the Bush Administration's disproportionality test was itself *more* intrusive than the approach that the Supreme Court has repeatedly articulated.

For instance, in *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*,[61] the Court quoted and applied the test for exclusionary conduct articulated by Harvard scholars Donald Turner and Phillip Areeda in their monumental treatise, *Antitrust Law*.[62] According to the *Aspen Skiing* Court (and Areeda and Turner), the category of conduct banned by section 2 "comprehends *at the most* behavior that *not only* (1) tends to impair the opportunities of rivals, *but also* (2) either does not further competition on the merits or does so in an unnecessarily restrictive way."[63] Put affirmatively, conduct that excludes rivals but is either "competition on the merits" or "furthers" competition on the merits in the least restrictive way does not violate section 2.[64] While exclusion of rivals and, presumably, injury to consumers might be *necessary* to a finding of liability, it is by no means sufficient.[65] Simply put, the test announced by the *Aspen Skiing* Court does not turn on the impact of challenged conduct on the welfare of consumers in the relevant market. Application of this standard necessarily contemplates that monopolists who achieve and/or maintain their position via "competition on the merits" might injure consumers in the relevant market, perhaps even "disproportionately."[66] The classic example of such "competition on the

59. 253 F.3d 34 (D.C. Cir. 1999) (en banc) (per curiam).

60. *See* Varney, *supra* note 2, at 9 (invoking and discussing Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585 (1985), Lorain Journal Co. v. United States, 342 U.S. 143 (1951), and *Microsoft*). Later in the speech, Ms. Varney also invoked *United States v. Dentsply International, Inc.*, 399 F.3d 181 (3d Cir. 2005), and *Conwood Co. v. U.S. Tobacco Co.*, 290 F.3d 768 (6th Cir. 2002), along with *Microsoft*, as "strong examples of successful challenges to exclusionary conduct . . . [that] the Department will look to . . . in establishing its Section 2 enforcement priorities." *See* Varney, *supra* note 2, at 13.

61. 472 U.S. 585 (1985).

62. *See* PHILLIP AREEDA & DONALD F. TURNER, ANTITRUST LAW (1978).

63. *See Aspen Skiing*, 472 U.S. at 605 n.32 (emphasis added) (quoting AREEDA & TURNER, *supra* note 62, ¶ 626b).

64. *See id.* at 605; *see also* Eastman Kodak Co. v. Image Technical Servs., Inc., 504 U.S. 451, 482–83 (1992) (citing *Aspen Skiing*, 472 U.S. at 605, for the proposition that conduct supported by "valid business reasons" does not violate section 2); Berkey Photo, Inc. v. Eastman Kodak Co., 603 F.2d 263, 273–75 (2d Cir. 1979) (reading pre-*Aspen Skiing* precedent as establishing a safe harbor for conduct justified by valid business reasons); *id*. at 281 ("[A]s we have already indicated, a monopolist is permitted, and indeed encouraged, by § 2 to compete aggressively on the merits . . . ." (citing United States v. United Shoe Mach. Corp., 110 F. Supp. 295, 344 (D. Mass. 1953), *aff'd*, 347 U.S. 521 (1954) (per curiam))); *id.* at 274 ("A firm that has lawfully acquired a monopoly position is not barred from taking advantage of scale economies by constructing, for example, a large and efficient factory. These benefits are a consequence of size and not an exercise of power over the market.").

65. *Cf. Aspen Skiing*, 472 U.S. at 605 (considering impact of conduct on consumers in the relevant market as one factor in overall analysis of whether conduct constituted unlawful exclusion).

66. *See* CARL KAYSEN, *UNITED STATES V. UNITED SHOE MACHINERY CORPORATION*: AN ECONOMIC ANALYSIS OF AN ANTI-TRUST CASE 16–19 (1956) (arguing that monopoly

merits" is the realization of economies of scale and the resulting above-cost pricing that excludes rivals and acquires or protects monopoly. This sort of conduct has been lawful per se for decades.[67] Indeed, in their classic 1975 article on predatory pricing, Professors Areeda and Turner expressly recognized that a monopolist's above-cost pricing could exclude rivals and result in increased consumer prices, but nonetheless argued that such pricing should be lawful per se, in part because the prospect of such high prices could incentivize monopolists to innovate and engage in other "competition on the merits."[68] The Supreme Court has applied the same test to refusals to deal and exclusionary agreements, like tying contracts, holding that such agreements are lawful, despite any exclusionary impact, if they are the least restrictive means of achieving a legitimate business objective—that is, of furthering competition on the merits.[69]

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maintained by means of economies of scale is unobjectionable); CARL KAYSEN & DONALD F. TURNER, ANTITRUST POLICY: AN ECONOMIC AND LEGAL ANALYSIS 78 (1959) ("Market power resting on certain bases we consider 'reasonable,' because we think it either undesirable or impossible to eliminate them. . . . [Market power resulting from economies of scale] could be reduced only at the cost of producing at higher costs in inefficiently small units; this price we do not desire to pay."); *id*. at 133–34 (mergers that create market power and substantial efficiencies should be lawful). None of these sources even suggests that section 2 should condemn a monopoly achieved via economies of scale simply because the monopolist charges higher prices than would be charged in a more competitive market comprised of firms with higher costs.

67. *See* Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 223–24 (1993) (holding that above-cost pricing cannot violate section 2); *Berkey Photo*, 603 F.2d at 274; *see also Aspen Skiing*, 472 U.S. at 596–97 (quoting with approval jury instructions treating realization of economies of scale as lawful per se); *United Shoe*, 110 F. Supp. at 344 (reasoning that United Shoe's conduct might contravene section 2 because its "control does not rest *solely* on its original constitution, its ability, its research, or its economies of scale" (emphasis added)).

68. *See* Phillip Areeda & Donald F. Turner, *Predatory Pricing and Related Practices Under Section 2 of the Sherman Act*, 88 HARV. L. REV. 697, 705–06 (1975); *id*. at 707 (contending that restrictions on monopoly pricing by firms that achieved or maintained monopoly by means of competitive merit would eliminate appropriate rewards for superior skill, foresight, and industry, and improperly stifle innovation). Thus, Professors Areeda and Turner anticipated the Supreme Court's decision in *Verizon Communications, Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398 (2004), which opined that the prospect of legitimately obtained monopoly profits provides appropriate incentives that encourage pro-competitive activity. *Id.* at 407.

69. *See Eastman Kodak*, 504 U.S. at 458, 461–63, 482–83 (finding that Kodak implemented tying agreements and refusals to deal with competitors, and then applying the *Aspen Skiing* test to determine if this conduct violated section 2); *Aspen Skiing*, 472 U.S. at 600–11 (applying this test to a refusal to deal after contractual negotiations over the fruits of joint venture activity broke down); *see also* United States v. Dentsply Int'l, Inc., 399 F.3d 181, 186–87 (3d Cir. 2005) (invoking and applying the *Eastman Kodak* standard). As noted above, Ms. Varney invoked *Dentsply* as an exemplar of the more aggressive enforcement posture the Antitrust Division would take. *See supra* note 60. Yet that decision opined that conduct supported by legitimate business reasons would not violate section 2, even if it excluded rivals and harmed consumers, unless there was a less restrictive means of achieving the same benefits. *See Dentsply*, 399 F.3d at 187; *id.* at 196–97 (repeating that proof of a legitimate business justification would immunize conduct that excluded rivals and produced harm, but finding that the challenged conduct did not produce such benefits). Thus, *Dentsply* simply applied the Areeda-Turner test, which does not turn on the challenged conduct's impact on the welfare of consumers in the relevant market. *See* AREEDA & TURNER, *supra* note 62, ¶ 626b.

The Areeda-Turner test, with its safe harbor for "competition on the merits,"[70] was not novel when the *Aspen Skiing* Court endorsed it. The Harvard school of antitrust had advocated such a test since at least the late 1950s, when Donald Turner and Carl Kaysen endorsed a similar formulation announced in a decision by Judge Charles Wyzanski and affirmed by the Supreme Court.[71] No Supreme Court decision either before or since holds or even suggests that liability under section 2 should turn on the extent of harm to consumers in the relevant market, nor does any such decision hold that courts should weigh the efficiency benefits of challenged conduct against the harms that conduct creates.[72] As I have explained elsewhere, current monopolization law reflects the Harvard school's view that antitrust law, including the Sherman Act, should concern itself with encouraging efficient resource allocation, without regard to the impact of resulting doctrine on the distribution of income.[73] Under this approach, conduct that creates significant efficiencies escapes condemnation even if it also creates market power, because such efficiencies generally exceed the harm resulting from the misallocation of resources produced by market power.[74]

Taken at face value, then, the Obama Administration's promise of more aggressive section 2 enforcement than the Bush Administration would require a standard for liability that is significantly more intrusive than that

70. AREEDA & TURNER, *supra* note 62, ¶ 626b.

71. *See United Shoe*, 110 F. Supp. at 344–45 (announcing safe harbor for "competition based on pure merit"), *aff'd*, 347 U.S. 521 (1954) (per curiam); KAYSEN & TURNER, *supra* note 66, at 22 ("[T]he Sherman Act has been interpreted—and properly, we think—to leave room for legal monopolies, that is, for monopolies acquired solely by competitive merit . . . ."); *see also* LAWRENCE ANTHONY SULLIVAN, HANDBOOK OF THE LAW OF ANTITRUST 95–99 (1977) (concluding that *United Shoe*'s safe harbor for "competition on the merits" properly stated the law under section 2).

72. *Lorain Journal Co. v. United States*, 342 U.S. 143 (1951), which Ms. Varney also invoked, is actually an example of the "no economic sense" test that the Bush Administration decried as insufficiently interventionist. *See* SECTION 2 REPORT, *supra* note 33, at viii–ix (claiming that the no economic sense test would immunize conduct that produced trivial benefits even if it was significantly harmful to consumers); *id.* at 43. As Ms. Varney noted, *see* Varney, *supra* note 2, at 9 n.12, Robert Bork, a proponent of a safe harbor for conduct that produces non-trivial efficiencies and makes economic sense separate and apart from its exclusionary impact, has invoked *Lorain Journal* as a decision that exemplifies his preferred approach, *see* ROBERT H. BORK, THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF 144 (1978) (defining unlawful predation as involving conduct that increases profits not by increased efficiency, but by driving rivals from the market or otherwise deterring rivals from engaging in competition, and stating that such conduct reduces "consumer welfare" and should be unlawful); *id*. at 107–15 (equating "consumer welfare" with the total welfare of society and rejecting the use of antitrust law to favor purchasers over producers, or vice versa); *see also* Varney, *supra* note 2, at 10–11 (invoking *Lorain Journal* as indicative of the sort of enforcement standard the Antitrust Division would apply).

73. *See* Meese, *supra* note 26, at 692–715. *See generally* Ken Heyer, *Welfare Standards and Merger Analysis: Why Not the Best?*, 2 COMPETITION POL'Y INT'L, Autumn 2006, at 29 (describing the difference between the "total welfare" and "consumer welfare" tests as applied to mergers and advocating adoption of the former).

74. *See* Oliver E. Williamson, *Economies as an Antitrust Defense: The Welfare Tradeoffs*, 58 AM. ECON. REV. 18, 22–23 (1968).

allowed by the very Supreme Court decisions that Ms. Varney invoked as the purported basis for the Antitrust Division's future enforcement agenda. There is nothing inappropriate about an agency adopting an enforcement policy at odds with Supreme Court case law. The Sherman Act—not to mention Article II of the Constitution—leaves the Executive Branch significant discretion to determine its own view of the meaning of the antitrust laws and to adopt corresponding enforcement policies that are either more or less aggressive than those endorsed by Supreme Court decisions.[75] To the extent that such policies are more intrusive than those currently endorsed by the case law, however, agencies must ultimately convince Article III courts, which have the last word on the imposition of damages, fines, or imprisonment, that the proposed standard is in fact a better view of the law.

Still, at some point an agency has to settle on *some* standard. Moreover, an evaluation of the claim that a more aggressive enforcement agenda will help stabilize the economy depends on the content of that agenda. The most obvious such standard—and one consistent with the Obama DOJ's professed concern for the welfare of consumers—is the consumer welfare effects test.[76] Under this approach, agencies and courts would determine whether a challenged practice reduces output, raises prices, and thus injures the welfare of consumers in the market served by the monopolist, without considering whether the challenged conduct produces benefits realized by others or comparing the magnitude of such benefits to the harm suffered by these consumers.[77] That is, courts applying this standard would focus on the welfare of some consumers—purchasers in the relevant market—while ignoring the welfare of other consumers—namely, the monopolist's

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75. *See* William F. Baxter, *Separation of Powers, Prosecutorial Discretion, and the "Common Law" Nature of Antitrust Law*, 60 TEX. L. REV. 661, 680–82 (1982) (defending the Antitrust Division's authority to decline to prosecute conduct that contravenes standards articulated by the courts); Alan J. Meese, *Raising Rivals' Costs: Can the Agencies Do More Good than Harm?*, 12 GEO. MASON L. REV. 241, 250–59 (2003) (documenting various instances in which agencies have taken doctrinal positions at odds with the case law and defending this practice).

76. *See* Salop, *supra* note 25, at 355–56 (advocating such a standard); *accord* Pitofsky, *supra* note 25, at 217; *see also* Meese, *supra* note 26, at 671 (distinguishing the "purchaser welfare" standard adopted by these two scholars from a "total welfare" standard that seeks to maximize the welfare of all consumers in society).

77. *See* Pitofsky, *supra* note 25, at 217 (endorsing comparison of efficiency effects with adverse impacts on consumers in the market served by the monopolist); Salop, *supra* note 25, at 329–33 (same); *see also* AAI TRANSITION REPORT, *supra* note 7, at 67 (endorsing the standard articulated by Professor Salop and contending that the "best default framework is the consumer welfare balancing test articulated by the D.C. Circuit in *Microsoft*"). As I have argued elsewhere, *Microsoft*'s support for the purchaser-focused "consumer-welfare balancing test," advocated by Professor Salop and others, is ambiguous at best. *See* Meese, *supra* note 26, at 732–36 (rebutting arguments that the D.C. Circuit's *Microsoft* decision altered the Supreme Court's definition of conduct unlawful under section 2). After all, the court opined that harm to consumers in the relevant market was merely a *necessary* condition for liability, and that the ultimate question in section 2 cases entails "distinguishing between exclusionary acts, which reduce *social* welfare, and competitive acts, which increase it." *See* United States v. Microsoft Corp., 253 F.3d 34, 58 (D.C. Cir. 2001) (en banc) (per curiam) (emphasis added).

shareholders or other owners who reap the benefits of monopoly pricing and lower costs due to efficiencies.[78] Courts would thus ban any practice that, say, results in prices that are higher than they would be without the practice, even if it increases the welfare of all of society's consumers by producing significant economic benefits that outweigh the economic harm that results when output reduction results in a misallocation of resources.[79] While Ms. Varney did not expressly endorse this "consumer" or "purchaser" welfare approach in her speech explaining the DOJ's new strategy, it is the most plausible section 2 standard that is more intrusive than the disproportionality test that she condemned.[80] The balance of this Essay will attribute this new standard to President Obama's Antitrust Division and assume that courts will embrace it, solely for the sake of examining the impact of such a novel approach on primary conduct and the macroeconomy.

The consumer welfare effects test would obviously ban more conduct than both the current standard employed by the courts, which immunizes all conduct necessary to produce efficiencies regardless of the impact on prices in the relevant market,[81] and the Bush Administration's disproportionality test. All three tests would ban all conduct that excludes rivals and increases prices without producing any benefits. Unlike the current legal standard, the two alternative tests would also ban all conduct that raises prices and visits harms on consumers that significantly outweigh, and thus are disproportionate to, the conduct's efficiency benefits. Only the consumer welfare effects test, however, would go even further and ban conduct that produces consumer harm that is *not* disproportionate to its efficiency benefits. Thus, this test would prohibit conduct resulting in consumer harm that barely exceeds, is equal to, or is less—even far less—than its efficiency benefits.[82] When "harm to consumers" in a particular market is the

78. *See* Meese, *supra* note 26, at 669–73 (explaining how the "consumer welfare effects" standard ignores the welfare of consumers outside the relevant market and characterizing this approach as a "purchaser welfare effects" standard).

79. *See* Meese, *supra* note 26, at 669–71 (explaining how this standard would ban practices regardless of their overall welfare impact); *see also* Williamson, *supra* note 74, at 18, 21–23 & tbl.1 (explaining that "a relatively modest cost reduction is usually sufficient to offset relatively large price increases").

80. An alternative but even more aggressive standard would ban all monopolies, including those that result in lower consumer prices. *See generally* John J. Flynn, *Statement of John J. Flynn, Modification of Sherman Act, Section 2: Proposed Simplification of Standards for Proving Attempted Monopolization Under Section 2*, 48 ANTITRUST L.J. 845 (1979) (advocating a "no conduct" approach to monopolization doctrine, whereby proof of monopoly would itself establish liability under section 2); Eleanor M. Fox, *Monopoly and Competition: Tilting the Law Towards a More Competitive Economy*, 37 WASH. & LEE L. REV. 49 (1980) (same). This standard seems incompatible with the Obama Administration's position.

81. *See* Meese, *supra* note 26, at 670–73 (describing distinction between the total welfare and purchaser welfare approaches).

82. For instance, a practice could confer significant market power, but also result in large cost savings that moderate any price increase and resulting consumer harm. *See generally* Heyer, *supra* note 73, at 36 n.16 (emphasizing that reduction in marginal costs will moderate exercises of market power). In such cases, the consumer welfare effects test would still condemn the practice, even though efficiencies are large relative to consumer harm.

touchstone of antitrust analysis, the welfare of the rest of society is beside the point.[83]

The conduct that the consumer welfare test uniquely bans would create two types of harm.[84] First, price increases on remaining output transfer income from consumers to the monopolist and its shareholders. This is a purely distributional effect that does not impact social welfare. Second, the reduced output that results in higher prices causes a misallocation of resources, as inputs once used to produce the now-missing output are employed elsewhere to create less valuable output. Because this misallocation results from changes in output "at the margin," the resulting economic harm is generally a small fraction of the distributional "harms" resulting from higher prices.[85] Yet, this newly condemned conduct would do more than just create harm. Because the consumer welfare effects test alone bans this kind of conduct, it must produce efficiencies large enough relative to consumer harm to avoid condemnation under the disproportionality test and, of course, current law. By their nature, such efficiencies would entail a reduction in the use of scarce resources, lower costs per unit of output, and a corresponding increase in the real economic welfare of producers and thus society.[86]

Conduct uniquely subject to the consumer welfare effects test will both harm consumers by reducing output and raising prices, but also benefit society by creating efficiencies, thus creating a seemingly ambiguous result. Recognition that the harms resulting from such conduct are largely distributional in nature, however, allows for an evaluation of the overall welfare consequences of such conduct and thus the consumer welfare effects test. Simply put, conduct that survives scrutiny under a disproportionality test but offends a consumer welfare effects test will almost certainly create more economic welfare than it destroys. After all, by definition, the total consumer harm from such conduct at most barely exceeds its efficiency benefits. Moreover, actual economic harm is merely a fraction of total consumer harm, most of which is only distributional. Therefore, the efficiency benefits of such conduct will necessarily exceed its actual economic harm. Banning such conduct—as the consumer welfare effects test would do—would thus reduce overall economic welfare. The result is that the consumer welfare effects test is a recipe for reducing society's economic welfare. Proponents of the test have admitted as much,

83. *See* Robert H. Lande, *The Rise and (Coming) Fall of Efficiency as the Ruler of Antitrust*, 33 ANTITRUST BULL. 429, 447–50 (1988) (contending that the Sherman Act requires courts to ban conduct that increases society's overall welfare whenever such conduct reduces the welfare of consumers in the relevant market).

84. *See generally* Williamson, *supra* note 74, at 21–23 (graphically illustrating the impact of a transaction that produces efficiencies and market power, and distinguishing between allocative and transfer effects).

85. *See* Alan A. Fisher & Robert H. Lande, *Efficiency Considerations in Merger Enforcement*, 71 CALIF. L. REV. 1580, 1633 (1983) (stating that "wealth-transfer effects almost always swamp allocative efficiency effects"); Williamson, *supra* note 74, at 28 (stating that "income [re]distribution which occurs [from an exercise of market power] is usually large relative to the size of the dead-weight loss").

86. *See* Williamson, *supra* note 74, at 21–23 & n.4.

arguing that distributional concerns, and not efficiency, motivated Congress to pass the Sherman Act.[87]

II. ANTITRUST AND THE DEPRESSION

This part reviews the relationship between antitrust regulation and the Great Depression, thereby providing the context necessary to evaluate the Obama Administration's claim that more aggressive section 2 enforcement would have helped stave off, or at least mitigated, the most recent economic downturn. Ms. Varney's account of this history in her speech outlining the DOJ's new enforcement agenda was basically correct, subject to some important qualifications and amplifications. Lax enforcement of the Sherman Act during the late 1920s facilitated cartelization and may have helped bring on the Great Depression in the first place. Moreover, once the Depression started, the NIRA thwarted competition throughout the economy by imposing so-called "codes of fair competition" on hundreds of industries.[88] These codes mandated overt price fixing and practices facilitating horizontal collusion. Such price fixing and related practices would have contravened the Sherman Act but for the NIRA's express provision of antitrust immunity for such practices.[89]

Ms. Varney's narrative was not entirely complete, however. For one thing, the NIRA did more than facilitate the cartelization of industry: it also encouraged the cartelization of labor by requiring firms that participated in codes to engage in collective bargaining with their employees.[90] Thus, all resulting codes included minimum wage provisions that applied to union and non-union employees alike.[91] Moreover, the NIRA's business and labor cartelization measures did more than merely reduce output, increase consumer prices, and "reduce[] consumer purchasing power," as Ms. Varney correctly observed.[92] Such provisions, combined with post-NIRA legislation bolstering collective bargaining rights, also deepened and lengthened the Great Depression.[93] These documented macroeconomic impacts lend some superficial plausibility to her suggestion that less aggressive enforcement during the Bush Administration helped cause and exacerbate the current Great Recession.[94]

A. Pre-Depression Antitrust (Non-)enforcement

In 1911, the Supreme Court announced that sections 1 and 2 of the Sherman Act ban "unusual and wrongful" contracts and other practices, not

87. *See* Kirkwood & Lande, *supra* note 25, at 201, 203; Lande, *supra* note 83, at 448–50; *see also* AAI TRANSITION REPORT, *supra* note 7, at 8 (emphasizing that "the people" have a right to lobby Congress to exempt various sectors from free market competition).
88. *Id.* § 3.
89. *Id.* § 5.
90. *See id.* § 7.
91. *See infra* note 132 and accompanying text.
92. Varney, *supra* note 2, at 3.
93. *See infra* notes 185–203 and accompanying text.
94. Varney, *supra* note 2, at 4–5.

"normal" or "usual" conduct of the sort protected by liberty of contract, even if such "normal" conduct helps acquire or maintain a monopoly.[95] Conduct was "normal" if it produced significant efficiencies unrelated to its exclusionary impact.[96] Applying this test in the 1920s, the Supreme Court condemned horizontal price fixing between significant industry participants,[97] as well as so-called "open price plans" adopted and enforced by trade associations and challenged by the Harding Administration.[98] Such plans required each member of a trade association to file its prices, output, customers, and other competitive variables with a central agent, who would then share the information with other participants. Downward deviation from filed prices was generally prohibited.[99] According to the Court, these plans were unreasonable and contrary to section 1 because they

95. United States v. Am. Tobacco Co., 221 U.S. 106, 181 (1911); *accord* United States v. United Shoe Mach. Co. of N.J., 247 U.S. 32, 66–67 (1918) (rejecting a challenge to efficient conduct that fostered monopoly); Standard Oil Co. of N.J. v. United States, 221 U.S. 1, 59–62 (1911); United States v. Joint Traffic Ass'n, 171 U.S. 505, 566–68 (1898) (reading the Sherman Act so as not to ban "ordinary contracts and combinations," even if such agreements indirectly restrained interstate commerce); *see also* Alan J. Meese, Standard Oil *as* Lochner*'s Trojan Horse*, 85 S. CAL. L. REV. (forthcoming 2012) (describing how liberty of contract considerations influenced adoption and content of the Rule of Reason); Alan J. Meese, Competition Policy and the New Deal: Lessons Learned and a New Way Forward (Aug. 2011) (unpublished manuscript) (on file with author) (examining various sources of competition policy, including the Sherman Act, Commerce Clause, and Due Process Clauses, before, during, and after the Depression).

96. *See United Shoe*, 247 U.S. at 65 (finding that the defendant adopted the challenged practices for reasons that "move[] and may move the transactions of men"); *id.* at 63–64 (explaining that the practice of leasing machines helped finance entry of small shoe manufacturers and ensured that machines were used in proper relation to other machines); *id*. at 64 (explaining that requirement that lessees also lease accessory machines created "great economic advantage"); *see also* William H. Page, *Legal Realism and the Shaping of Modern Antitrust*, 44 EMORY L.J. 1, 16–17 (1995) (explaining how the *United Shoe* decision rested upon a determination that the challenged provisions were voluntary arrangements that benefitted both parties). As I have suggested before, the test applied in *United Shoe* was akin to the modern "no economic sense" test. *See* Meese, *supra* note 26, at 677 n.70; *see also* Werden, *supra* note 37, at 413.

97. *See* United States v. Trenton Potteries Co., 273 U.S. 392, 394–98 (1927) (banning all price fixing between "members of a combination controlling a substantial part of an industry"); Addyston Pipe & Steel Co. v. United States, 175 U.S. 211, 235–40 (1899) (finding horizontal price restraint between major industry participants "direct" and thus unlawful because it raised prices above the competitive level).

98. *See* United States v. Am. Linseed Oil Co., 262 U.S. 371, 389–90 (1923) (banning open price plans); Am. Column & Lumber Co. v. United States, 257 U.S. 377, 410–12 (1921) (same).

99. *See Am. Linseed Oil*, 262 U.S. at 382–83 (detailing these requirements of the challenged plan); *Am. Column & Lumber*, 257 U.S. at 394–95 (same); *see also Am. Linseed Oil*, 262 U.S. at 389 (participants agreed to follow price schedules "unless more onerous [prices] were obtained"); RUDOLPH J.R. PERITZ, COMPETITION POLICY IN AMERICA: HISTORY, RHETORIC, LAW 76 (rev. ed. 1996) (describing the role of a major consulting firm in managing thirty major trade associations before 1940). Thus, Ms. Varney's statement that there was little interest in antitrust enforcement from the end of World War I until 1937 is not entirely accurate. The DOJ did challenge outright cartels and "open price plans" in the early through mid-1920s. *See* ROBERT F. HIMMELBERG, THE ORIGINS OF THE NATIONAL RECOVERY ADMINISTRATION 7–21 (1993) (discussing aggressive civil and criminal prosecution of cartel and cartel facilitating activity in the early 1920s).

were "a new form of combination . . . resorting to methods which are not normal," whose "necessary tendency is to suppress competition."[100]

The government's aggressive pursuit of such horizontal arrangements did not last long. During the Coolidge Administration, Secretary of Commerce Herbert Hoover and others lobbied Assistant Attorney General William Donovan, head of the Antitrust Division, to refrain from prosecuting open price plans that contravened the Supreme Court's recent decisions.[101] During the same period, the FTC orchestrated dozens of "trade practice conferences," at which industry proposed, and the Commission adopted, so-called "codes of fair competition."[102] Such codes banned as "unfair" various forms of otherwise lawful competition, including below-cost pricing, price discrimination, the granting of favorable credit terms, and promotional activities such as giveaways and lotteries held by gasoline stations—all without any additional showing that the banned practice produced competitive harm.[103] On the eve of the Depression, then, antitrust enforcement had reached its nadir. One of the enforcement agencies declined to challenge plainly anti-competitive conduct, while the other was actively prohibiting pro-competitive activities.

B. The Great Depression and New Deal Cartelization

Herbert Hoover took office in March 1929, presiding over a nation enjoying unprecedented prosperity. Standard and Poor's composite index (S&P Index) of 90 common stocks peaked at 254 in September, and unemployment hovered around 3 percent.[104] By late October, however, the S&P Index had fallen to 162, national output was plummeting, and unemployment was climbing.[105] By 1932, output had fallen 28 percent

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100. *Am. Linseed Oil*, 262 U.S. at 389.

101. *See* HIMMELBERG, *supra* note 99, at 57–59 (reporting that Donovan provided comfort letters to associations that employed open price plans that most likely contravened decisions such as *Am. Linseed Oil*); *id*. at 17–18, 20–21, 39–40, 65–67 (describing Hoover's lobbying of the Attorney General in favor of trade association plans).

102. *See* THOMAS C. BLAISDELL JR., THE FEDERAL TRADE COMMISSION: AN EXPERIMENT IN THE CONTROL OF BUSINESS 92–102 (1932) (describing this process); *see also* 1930 FTC ANN. REP. 37 (reporting fifty-seven conferences held during the fiscal year); 1928 FTC ANN. REP. 5–16 (describing this procedure and various participating industries); *id*. at 5 ("The work of this [trade practice conference] division has increased enormously during the past fiscal year.").

103. *See, e.g.*, FTC TRADE PRACTICE CONFERENCES 81 (July 1, 1929) (adopting a code prohibiting gasoline stations from giving away motor oil or other products on "opening days, special sale days, or other occasions," or holding lotteries or other games of chance); HIMMELBERG, *supra* note 99, at 63 (stating that, as of 1928, such codes "routinely" banned below-cost pricing and price discrimination, without any additional requirement that such activities actually injure consumers).

104. *See* RUDIGER DORNBUSCH, STANLEY FISCHER & RICHARD STARTZ, MACROECONOMICS 414 tbl.18-1 (8th ed. 2001); MILTON FRIEDMAN & ANNA JACOBSON SCHWARTZ, A MONETARY HISTORY OF THE UNITED STATES 1867–1960, at 299–308 (1963).

105. *See* FRIEDMAN & SCHWARTZ, *supra* note 104, at 304–06 ("During the two months from the cyclical peak in August 1929 to the crash, production, wholesale prices, and personal income fell at annual rates of 20 per cent, 7½ per cent, and 5 per cent, respectively.").

from its 1929 peak and the S&P Index hovered around 50.[106] Unemployment stood at 23.6 percent and would climb to almost 25 percent by 1933.[107]

Perhaps ironically, Hoover rejected Coolidge's hands-off approach to antitrust enforcement, refusing to reappoint William Donovan to run the Antitrust Division.[108] Donovan's successor challenged trade association activities that Donovan had approved, and encouraged the FTC to revisit "trade practice codes" that banned below-cost pricing and price discrimination that did not enhance or protect market power.[109] Finally, despite Hoover's sympathy for collusive resource conservation, his Antitrust Division challenged a joint venture between 137 Appalachian coal producers in four states that funneled members' output through an exclusive sales agency.[110]

This reinvigoration of antitrust enforcement did not last long. Hoover lost his 1932 bid for reelection to Franklin Delano Roosevelt, who worked with Congress to develop the NIRA.[111] Passed and signed in the summer of 1933, this centerpiece of the New Deal authorized the President to impose so-called "Codes of Fair Competition," either unilaterally or at the behest of industry representatives.[112] Moreover, the statute expressly provided antitrust immunity for conduct authorized by the codes.[113]

Less than two years after FDR's signature, the National Recovery Administration (NRA), the entity created to implement the NIRA, had approved over 550 codes, purportedly covering businesses employing 80 percent of the private non-farm workforce.[114] The resulting codes coercively interfered with normal free market competition by expressly fixing prices or otherwise encouraging horizontal collusion: 38 set

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106. DORNBUSCH ET AL., *supra* note 104, at 78, 414 tbl.18-1; FRIEDMAN & SCHWARTZ, *supra* note 104, at 304 tbl.29.

107. DORNBUSCH ET AL., *supra* note 104, at 414 tbl.18-1.

108. HIMMELBERG, *supra* note 99, at 88–89.

109. *Id.* at 104–05 (describing the DOJ's litigation against the Sugar Institute and other associations whose activities the Coolidge administration had approved); *id.* at 90–97 (describing DOJ challenges to activities previously approved by the FTC's trade practice conferences).

110. *See generally* Appalachian Coals, Inc. v. United States, 288 U.S. 344 (1933).

111. *See* National Industrial Recovery Act (NIRA) of 1933, ch. 90, 48 Stat. 195 (previously codified at 15 U.S.C. §§ 701–712 (Supp. 1933)), *invalidated by* A.L.A. Schechter Poultry Corp. v. United States, 295 U.S. 495 (1935).

112. *See id.* § 3.

113. *See id.* § 5.

114. *See* HIMMELBERG, *supra* note 99, at 211; Harold L. Cole & Lee E. Ohanian, *New Deal Policies and the Persistence of the Great Depression: A General Equilibrium Analysis*, 112 J. POL. ECON. 779, 784 (2004). I say "purportedly" because some of the industries covered, such as bowling alleys, barber shops, billiard halls, and burlesque houses, were plainly beyond the jurisdiction of Congress to regulate under then-extant case law. *See* CHARLES FREDERICK ROOS, NRA ECONOMIC PLANNING 538 (1937) (listing "Barber Shop Trade" and "Bowling and Billiard Operating Trade" as codes approved as of April 5, 1935); *id*. at 539 (listing "Burlesque Theatrical" in same table); *id*. at 547 (listing "Motor Vehicle Storage and Parking Trade" in same table); *cf*. Hammer v. Dagenhart, 247 U.S. 251, 272 (1918) (holding that Congress cannot regulate employment practices of manufacturer even though the firm intended to sell its output in interstate commerce).

minimum prices;[115] 188 included "[e]mergency price fixing provisions," defining "emergency" as "destructive price cutting" endangering maintenance of a code;[116] and 422 included "open-price" provisions, like those declared unlawful by the Supreme Court, requiring firms to file their prices publicly with the code authority, with most including waiting periods between the filing of new prices and their effective dates.[117] Other codes reduced output by limiting production to certain days of the week or hours of the day, limiting construction of new capacity, preventing firms from shifting from one form of output to another, discouraging the movement of facilities from one locality to another, prohibiting the opening of new plants, and discouraging new routes or extending existing ones.[118]

Code provisions facilitated collusion or tempered rivalry in other ways as well. Eighty mandated resale price maintenance, which in some circumstances can facilitate upstream horizontal price fixing.[119] Another 352 banned sales below a firm's individual costs, regardless of whether such prices injured competition or even a rival.[120] One hundred codes prohibited "destructive price cutting," defined as cuts "impair[ing] code wages and working conditions," regardless of the prices' relationship to costs.[121] Bans on below-cost pricing and "destructive" price cutting put a floor under prices, discouraged cheating on cartelistic arrangements, and replicated provisions adopted under the FTC's "Trade Practice Conferences."[122] Various codes banned or limited package sales and others limited the extension of consumer credit, both of which could facilitate secret discounting.[123] It is no surprise, then, that one historian has concluded that "[i]n the initial phase [of the NIRA], at least, the philosophy

115. *See* LEVERETT S. LYON ET AL., THE NATIONAL RECOVERY ADMINISTRATION: AN ANALYSIS AND APPRAISAL 579 (1935).

116. *Id.* at 605–08 & n.18.

117. *Id.* at 610–11 (recounting that 422 codes included "open-price plans" and that 297 required a delay between filing and changing prices); *see also* ELLIS W. HAWLEY, THE NEW DEAL AND THE PROBLEM OF MONOPOLY 59–60 (1966) (describing the operation of such provisions).

118. LYON ET AL., *supra* note 115, at 624–29 (sixty codes limited operation of plants and/or machinery to a certain number of hours per day or week); *id.* at 632–37 (detailing various other restrictions). Thus, the cement code only allowed new construction when necessary to improve efficiency, modernize, or if capacity was not increased, and motor bus and air transport companies required approval from code authorities before opening new routes. *See id*. at 633–35.

119. *See* HAWLEY, *supra* note 117, at 58–59 (reporting that eighty codes mandated minimum resale price maintenance); *see also* Cont'l T.V., Inc. v. GTE Sylvania Inc., 433 U.S. 36, 51 n.18 (1977) (stating that "industry-wide" minimum resale price maintenance can facilitate upstream horizontal collusion).

120. *See* LYON ET AL., *supra* note 115, at 585–86. Some codes both prohibited below-cost sales and authorized emergency price fixing. *See id.* at 605–08.

121. *Id.* at 603–05.

122. *See supra* notes 102–03 and accompanying text (describing provisions adopted by the FTC's "Trade Practice Conferences").

123. LYON ET AL., *supra* note 115, at 690–93; *cf*. Catalano, Inc. v. Target Sales, Inc., 446 U.S. 643, 650 (1980) (holding that there is a per se ban on wholesalers' agreement not to extend certain credit terms); *see also supra* note 103 and accompanying text (describing the presence of such provisions in some codes of fair competition approved by FTC-sponsored trade practice conferences).

of government-supported cartels was clearly outdistancing the concept of enforcing competition."[124]

So far, this history is consistent with that offered by the Obama Administration. There was, however, one important oversight in Ms. Varney's speech. While the NIRA certainly facilitated cartelization between firms in numerous industries and tempered rivalry in other ways as well, such cartelization was simply a means to a larger end—namely, raising wages and thus the "purchasing power" of labor.[125] Indeed, provisions boosting the prerogatives and income of labor, which Ms. Varney only mentioned once in passing,[126] were seen as working hand-in-hand with those facilitating cartelization. Without cartelization, it was said, destructive and cutthroat competition would result in "chiseling" on prices and thus wages.[127] While higher wages would reduce profits, policymakers surmised that wage earners spent a larger proportion of their income than shareholders, with the result that such a transfer of income would, on balance, increase overall consumption and thus aggregate demand.[128]

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124. *See* HAWLEY, *supra* note 117, at 62.

125. The NIRA's "Declaration of Policy" even included the goal of "increas[ing] the consumption of industrial and agricultural products by increasing purchasing power." *See* National Industrial Recovery Act (NIRA) of 1933, ch. 90 § 1, 48 Stat. 195.

126. Varney, *supra* note 2, at 3 (noting that the NIRA required code participants to engage in collective bargaining).

127. *See* HAWLEY, *supra* note 117, at 13 (internal quotation marks omitted); *see also* HIMMELBERG, *supra* note 99, at 202–05 (detailing business support for industry self-regulation of prices, wages, employment, and production); *id.* at 204 (explaining that "business leaders . . . were able to persuade [Senator] Wagner that elimination of 'cutthroat competition' and improvement of wages and hours through industry-wide agreements would, together with public works, be an adequate recovery mechanism"); *id.* at 197 ("The labor provisions, on the grounds that they would increase 'purchasing power' and spread work, made it somewhat possible to regard the N.I.R.A. as a recovery measure, as did the antitrust suspension, upon the supposition that unfair and ruthless competition was causing continuing deflation of prices and wages and making revival impossible.").

128. *See* WILLIAM LEUCHTENBURG, FRANKLIN D. ROOSEVELT AND THE NEW DEAL: 1932–1940, at 36 (1963) (reporting that FDR "accepted the underconsumptionist explanation of the cause of the depression" and was influenced by experts who believed "that the crisis centered in a failure of purchasing power but espoused structural reform rather than deficit spending"); HERBERT STEIN, THE FISCAL REVOLUTION IN AMERICA 48–49 (1969) ("Underlying [the NRA's] reforms was the thought that in the twenties too small a share of the national income had gone to workers and farmers—the consuming classes—and too large a share had gone to savers. As a result investment had run for a time at a rate that could not be sustained by the rate of consumption, and had then collapsed, causing the Depression. The NRA and the AAA were to raise and sustain the share of workers and farmers and thereby raise and sustain the share of consumption in the total national income."). Thus, the statute anticipated the concern, expressed by John Maynard Keynes and his followers during the 1930s and 1940s, that increasing affluence would increase the proportion of income saved, reduce the proportion of income devoted to consumption, and thereby prevent aggregate demand from reaching a level necessary to achieve full employment of the nation's resources. *See, e.g.*, ALVIN HANSEN, FULL RECOVERY OR STAGNATION? 13–34 (1938) (invoking a Keynesian framework to make this argument). As explained below, however, Keynes himself believed the NIRA would slow recovery and recommended a quite different remedy for such a shortfall in aggregate demand: increased government spending. *See infra* note 187 and accompanying text.

The NIRA did more than simply facilitate cartelization in the hope that business would pay higher wages. The statute pursued the objective of raising labor's "purchasing power" in a variety of ways. First, the Act banned "yellow-dog" contracts—agreements that forbade employees from joining a union.[129] The statute also required firms participating in codes to engage in collective bargaining with unions.[130] Finally, the statute contemplated that industry and labor would propose codes that included minimum wage and maximum hour provisions, and it empowered the President to impose such provisions by fiat if industry and labor could not come to agreement.[131] In fact, all codes mandated minimum wages and nearly all contained maximum hour provisions.[132]

The public policy favoring labor cartels persisted despite the NIRA's eventual demise. Less than two years after its passage, the Supreme Court unanimously invalidated the NIRA in *A.L.A. Schechter Poultry Corp. v. United States*,[133] thereby ending the codes and antitrust immunity for the NIRA cartels.[134] Nevertheless, Congress immediately moved to enact the National Labor Relations Act[135] (NLRA), which authorized the formation of labor cartels—also known as unions[136]—and compelled private firms to bargain with such entities over wages and other terms of employment.[137] The NLRA's "Findings and Declaration of Policy" included an assertion that firms' exercise of unequal bargaining power had reduced wages paid to labor and thus reduced the "purchasing power" necessary to maintain adequate consumption expenditures.[138] The Supreme Court narrowly sustained the NLRA as applied to manufacturing, previously deemed beyond the reach of Congress.[139]

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129. NIRA § 7(a)(2); *cf.* Coppage v. Kansas, 236 U.S. 1, 26 (1915) (voiding state ban on "yellow dog" contracts); Adair v. United States, 208 U.S. 161, 180 (1908) (voiding congressional ban on such contracts in the railroad industry).

130. NIRA § 7(a)(1).

131. *See id.* § 7(b) (authorizing industry participants to adopt "standards as to the maximum hours of labor, minimum rates of pay, and such other conditions of employment"); *id*. § 7(c) (empowering the President to establish minimum rates of pay, maximum hours, and other conditions of employment).

132. *See* LYON ET AL., *supra* note 115, at 367 n.a (reporting that all but the fur trading code included maximum hour provisions); Cole & Ohanian, *supra* note 114, at 784 (all codes included minimum wage provisions).

133. 295 U.S. 495 (1935).

134. *See id.* at 550–51.

135. Ch. 372, 49 Stat. 449 (1935) (codified at 29 U.S.C. §§ 151–169 (2006)).

136. *See* GEORGE J. STIGLER, THE THEORY OF PRICE 279 (4th ed. 1987) ("The labor union is for the labor market the equivalent of the cartel in the product market.").

137. *See* NLRA §§ 7–8 (codified at 29 U.S.C. §§ 157–158).

138. *See id.* § 1 (codified at 29 U.S.C. § 151) ("The inequality of bargaining power between employees who do not possess full freedom of association or actual liberty of contract, and employers who are organized in the corporate or other forms of ownership association substantially burdens and affects the flow of commerce, and tends to aggravate recurrent business depressions, by depressing wage rates and the *purchasing power of wage earners* in industry and by preventing the stabilization of competitive wage rates and working conditions within and between industries." (emphasis added)).

139. *See* NLRB v. Jones & Laughlin Steel Corp., 301 U.S. 1, 25–26, 49 (1937) (sustaining by a 5–4 vote application of the NLRA to the nation's fourth largest steel manufacturer); NLRB v. Friedman-Harry Marks Clothing Co., 301 U.S. 58, 75 (1937)

Within a few years of the NLRA's passage, union membership had exceeded a quarter of the workforce and the number of "strike days" in the nation had doubled from fourteen million to twenty-eight million.[140] At the same time, the Roosevelt Administration maintained a hands-off approach to antitrust enforcement, declining to challenge cartelization in industries that had agreed to generous collective bargaining agreements with their unions, at least until Thurman Arnold took the helm of the Antitrust Division in 1938.[141] When supplemented to include the cartelization of labor via NIRA Codes and then the NLRA, the Obama Administration's descriptive account of the national government's anticompetitive response to the Great Depression appears complete.

III. MACROECONOMIC LESSONS FROM THE NEW DEAL'S REJECTION OF COMPETITION

The history recounted in Part II is certainly necessary to an understanding of the link between New Deal cartelization and the macroeconomy, but such history, no matter how detailed, is not sufficient. One also needs a theoretical framework to assist in evaluating the impact of cartelization—a microeconomic phenomenon—on the overall macroeconomy. This part provides such a framework, employs it to predict the impact of massive cartelization on wages and prices, and reviews the empirical evidence of that effect. The results provide a platform for evaluating the impact of President Obama's more aggressive section 2 enforcement policy on the larger economy.

A. Aggregate Demand, Aggregate Supply, and GDP

A key indicator of a nation's macroeconomic performance is GDP, defined as the annual "dollar value of economic activity" throughout the

(sustaining by a 5–4 vote application of the NLRA to a single clothing factory in Richmond); *cf.* Hammer v. Dagenhart, 247 U.S. 251, 272 (1918) ("[T]he mere fact that [goods manufactured with child labor] were intended for interstate commerce transportation does not make their production subject to federal control . . . ."); United States v. E.C. Knight Co., 156 U.S. 1, 12 (1895) ("Commerce succeeds to manufacture and is not a part of it.").

140. Cole & Ohanian, *supra* note 114, at 785 (reporting a doubling of strike days and an increase of union membership to 29 percent of the workforce by 1940); Michael Wachter, *The Rise and Decline of Unions*, 30 REGULATION, Summer 2007, at 23, 27 (reporting that union membership reached 26 percent of the workforce by 1940).

141. Cole & Ohanian, *supra* note 114, at 786. Enforcement was not entirely moribund, however. *See* United States v. Socony-Vacuum Oil Co., 310 U.S. 150, 165–66, 223–28 (1940) (sustaining numerous convictions based on indictments for anticompetitive conduct authorized by a pre-*Schechter* Code of Fair Competition); Daniel A. Crane, *The Story of* United States v. Socony-Vacuum*: Hot Oil and Antitrust in the Two New Deals*, *in* ANTITRUST STORIES 91, 103 (Eleanor M. Fox & Daniel A. Crane eds., 2007) (recounting late 1936 indictment of several firms and individuals in *Socony-Vacuum*); *see also* SPENCER WEBER WALLER, THURMON ARNOLD: A BIOGRAPHY 78–110 (2005) (describing Arnold's aggressive tenure at the Antitrust Division); John D. Harkrider, *Lessons from the Great Depression*, 23 ANTITRUST, Spring 2009, at 6, 8–9 (discussing post-NIRA antitrust enforcement by the Roosevelt Administration, including a substantial increase in enforcement actions during Arnold's tenure).

nation.[142] A recession is "a period of general economic decline," manifesting itself as a fall in the real (inflation-adjusted) value of GDP lasting two quarters or more.[143] The most recent recession began in the second half of 2008, when real GDP fell at just under a 4 percent annual rate in the third quarter and at a nearly 9 percent rate in the fourth quarter.[144] The recession continued into the first half of 2009, with GDP falling at rates greater than 6.5 percent in the first quarter and less than 1 percent in the second quarter.[145] A recovery of sorts began in the third quarter of 2009, with GDP rising, though sometimes quite modestly, in each of the last eight quarters.[146]

Any evaluation of the link between antitrust enforcement and the onset, depth, and persistence of the most recent downturn must begin with an understanding of the determinants of GDP. Basically, macroeconomists treat GDP as a function of two modeling constructs: aggregate demand and aggregate supply.[147] Like any demand schedule, the aggregate demand schedule denotes the quantity of output that consumers will demand—albeit "in the aggregate"—at any given price, with "price" denoting the economy's overall or general price level.[148] This similarity between the "aggregate" demand familiar to macroeconomists and the "ordinary" demand studied by microeconomists masks an important distinction between the two constructs, however. The ordinary demand curve from microeconomics takes a "partial equilibrium" approach, modeling the impact of price on the quantity consumers demand *in a particular industry* and assuming that price and output in other industries is held constant.[149] In this construct, a price reduction causes individuals to purchase more of

142. *See* N. GREGORY MANKIW, MACROECONOMICS 18 (7th ed. 2010) (describing GDP as a "single number representing the dollar value of economic activity in a given period of time").

143. *See* ANDREW B. ABEL & BEN BERNANKE, MACROECONOMICS 277, 278 n.2 (2005). This Essay employs the term "GDP" and "real GDP" interchangeably to refer to the inflation-adjusted value of annual economic activity.

144. *See Gross Domestic Product (GDP): Percent Change from Preceding Period*, BUREAU ECON. ANALYSIS, http://www.bea.gov/national/xls/gdpchg.xls (last updated Jan. 27, 2012).

145. *See id*.

146. *See id*. For instance, in the first quarter of 2011, GDP rose 0.4 percent. *See* News Release, Bureau of Econ. Analysis, Gross Domestic Product: Second Quarter 2011 (Advance Estimate) (July 29, 2011), http://www.bea.gov/newsreleases/national/gdp/2011/gdp2q11_adv.htm.

147. *See generally* DORNBUSCH ET AL., *supra* note 104, ch. 5.

148. *See* MANKIW, *supra* note 142, at 269 (defining "aggregate demand" as "the relationship between the quantity of output demanded and the aggregate price level").

149. *See, e.g.*, KELVIN LANCASTER, INTRODUCTION TO MODERN MICROECONOMICS 10 (1969) (explaining how microeconomists generally employ such "*partial analysis*" when examining the impact of price on demand and supply in a particular market); *see also* W. KIP VISCUSI, JOHN M. VERNON & JOSEPH E. HARRINGTON, JR., ECONOMICS OF REGULATION AND ANTITRUST 76 (3d ed. 2000) (explaining how partial equilibrium tools focus on impacts in a particular market to avoid second best problems presented by general equilibrium analysis when some markets are characterized by monopoly, externalities, and other departures from perfect competition).

the product in question and less of other products. Thus, there is no impact on overall consumption.

By contrast, the *aggregate* demand curve models the relationship between price and demand for all goods in the entire economy simultaneously, as part of a larger general equilibrium analysis.[150] Within this construct, a "price reduction" refers to a reduction in the *average* price of goods and services produced by the entire economy.[151] Moreover, instead of inducing substitution of demand of some products for others, an aggregate price reduction increases the demand for all goods and services simultaneously.[152] In particular, for any given supply of money, a price reduction increases the real value of money balances held by individuals. This increase can, holding all other factors constant, influence aggregate demand in two different ways.[153] First, the increase leaves individuals holding more money in real terms—that is, money that does not bear interest—than necessary to conduct their day-to-day transactions.[154] As a result, individuals will rebalance their asset portfolios by using excess money to purchase interest-bearing assets, bidding up the price of such assets and lowering interest rates.[155] This reduction in interest rates will, in turn, increase personal and business investment, thereby increasing overall demand for goods and services.[156] Second, separate and apart from any change in interest rates, an increase in real balances will enhance individuals' wealth and thereby stimulate aggregate consumption, in the same way that any other wealth increase will boost consumption.[157] Economists refer to this distinct impact on consumption (somewhat confusingly) as the "real balance effect" or the "Pigou effect."[158]

150. *See* ABEL & BERNANKE, *supra* note 143, ch. 9 (treating the aggregate demand model as general equilibrium in nature); MANKIW, *supra* note 142, at 74 (explaining that the basic model of the macroeconomy is general equilibrium in nature, because it incorporates various interactions determining the overall supply and demand for goods and services); *see also* DORNBUSCH ET AL., *supra* note 104, at 86 tbl.5-1 ("[T]he economics underlying the aggregate supply-aggregate demand diagram is unrelated to the microeconomic version. (It's too bad that our macroeconomic version wasn't given a different name.)").

151. *See* DORNBUSCH ET AL., *supra* note 104, at 86 tbl.5-1 (identifying "price" relevant for macroeconomic aggregate demand analysis as "the cost of a basket of all the goods we buy measured in money terms"); MANKIW, *supra* note 142, at 269 (stating that aggregate demand models the relationship between total demand and "aggregate price level").

152. *See* DORNBUSCH ET AL., *supra* note 104, at 90.

153. *See* MANKIW, *supra* note 142, at 329.

154. *See* DORNBUSCH ET AL., *supra* note 104, at 244.

155. *Id.* at 244–45.

156. *Id.*; *see also* Christina D. Romer, *What Ended the Great Depression?*, 52 J. ECON. HIST. 757, 759 (1992) (contending that the inflow of gold during the 1930s increased the real money supply, reduced interest rates, and spurred business investment and individual purchases of durable goods).

157. *See* DON PATINKIN, MONEY, INTEREST, AND PRICES: AN INTEGRATION OF MONETARY AND VALUE THEORY 17–21 (MIT Press 2d ed. abr. 1989) (1965); Don Patinkin, *Price Flexibility and Full Employment*, 38 AM. ECON. REV. 543, 556 (1948). *See generally* A.C. Pigou, *The Classical Stationary State*, 53 ECON. J. 343 (1943) (elaborating on the claim that the fall in prices will increase real balances and stimulate aggregate demand, and defending it against Keynesian criticism).

158. *See* PATINKIN, *supra* note 157, at 19 n.13 ("The 'real balance effect' is identical with . . . the 'Pigou effect.'"); Patinkin, *supra* note 157, at 556 (equating the "Pigou effect"

While there is little doubt that aggregate demand curves slope down and to the right, the location and slope of the curve is not set in stone. As with ordinary demand curves, any given aggregate demand curve holds constant all the factors other than price that can influence demand.[159] A change in one or more of these variables will result in a shift in the curve.[160] A reduction in the money supply or a tax increase, for instance, will shift the curve to the left, while an increase in the money supply or a tax cut will shift the curve to the right.[161]

Aggregate demand is meaningless unless the economy has the wherewithal to respond with supply. The aggregate supply schedule denotes the output of goods and services that a nation's business establishments would produce at each given price level.[162] Those familiar with an ordinary supply curve might expect the aggregate supply curve to slope up and to the right. Sometimes it does, but macroeconomists often begin with the assumption that the aggregate supply curve is vertical, at least in the long run.[163] Ordinary supply curves model the price and output relationship for a particular industry, which can always bid productive resources away from the rest of the economy.[164] The *aggregate* supply curve, by contrast, models the response of the entire economy to an increase in the general price level.[165] The vertical slope of this curve reflects the fact that society's given stock of resources—labor, capital, and technical knowhow—can only produce so much, regardless of the price level.[166] When aggregate demand at a given price level exceeds the economy's capacity to produce, inflation will occur, choking off excess demand and

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with "real balance effect"); *see also* DORNBUSCH ET AL., *supra* note 104, at 244 & n.2 (distinguishing the "real balance effect," whereby higher balances directly increase demand for commodities, from impact of higher balances on interest rates and thus business and personal investment); MANKIW, *supra* note 142, at 313–15, 329 (distinguishing the reduction in interest rates as a result of real balance increases under the "*IS–LM* model" and the "Pigou effect" on commodity demand). Reference to this distinct effect as the "real balance" effect can be confusing because both of the effects on interest rates and consumption depend upon an increase in the real value of money balances and thus, in that sense, are both "real balance" effects.

159. *Cf.* WILLIAM J. BAUMOL & ALAN S. BLINDER, ECONOMICS: PRINCIPLES AND POLICY 70–71 (8th ed. 2000) (explaining this aspect of ordinary demand curves).

160. *See* MANKIW, *supra* note 142, at 322–23 (explaining how a change in any variable other than the price level that impacts demand will cause a shift in the aggregate demand curve).

161. *Id.* at 271 & fig.9-6 (showing how changes in the money supply affect aggregate demand); *id*. at 296 (discussing how tax cuts increase aggregate demand).

162. *See* DORNBUSCH ET AL., *supra* note 104, at 87 ("The aggregate supply curve describes, for each given price level, the quantity of output firms are willing to supply.").

163. *See* MANKIW, *supra* note 142, 272–73 & fig.9-7 (representing the "long run aggregate supply curve" as vertical).

164. *See* DORNBUSCH ET AL., *supra* note 104, at 87 (highlighting this aspect of normal supply curves and distinguishing such curves from the aggregate supply curve).

165. *See id.*

166. *See id.* ("The classical [vertical] supply curve is based on the assumption that the labor market is in equilibrium with full employment of the labor force."); MANKIW, *supra* note 142, at 272–73.

limiting actual and potential output.[167] Moreover, the location of the vertical region of the curve represents an economy's "potential" or "full employment" output.[168] A change in variables that improve the nation's productivity, such as advancing technology, will shift the location of that vertical "curve" to the right, thereby increasing the nation's potential output at any given level of aggregate demand.[169]

The intersection of the aggregate demand and aggregate supply curves determines the economy's output and thus GDP, at least when the economy is in equilibrium.[170] Like individual markets, however, the macroeconomy sometimes departs from equilibrium, often because of an exogenous shock to the economic system.[171] For instance, a tax increase or other reduction in wealth might reduce consumption, thereby shifting the aggregate demand curve down and to the left.[172] Or an uncertain regulatory or tax climate might reduce the propensity of businesses to invest in new plants and equipment and produce the same result.[173] If the aggregate price level remains the same, such shifts will result in lower output and thus lower GDP.[174] Moreover, some resources, including human resources, will become unemployed, as individuals and businesses are willing to supply more goods and services at prevailing prices than consumers are willing to purchase.

But will such unemployment persist? The answer would seem to be "no." After all, absent price regulation, surpluses drive prices down as owners of surplus goods and services lower the prices they charge to rid themselves of excess supplies.[175] If wages and prices are allowed to fall, aggregate demand will rise and the economy will, assuming a vertical aggregate supply curve, reach a new, full employment equilibrium, albeit at a lower price level.[176] Such a self-adjusting response to a shift in demand depends critically upon the flexibility of prices and resulting price reductions.[177] If, after a downward shift in aggregate demand, prices remain fixed—or worse yet, rise—no self-correction will occur, and the

167. DORNBUSCH ET AL., *supra* note 104, at 87 ("[I]f high demand is economywide and all the factors of production are already at work, there isn't any way to increase overall production, and all that happens is that all prices increase . . . .").

168. *Id.*

169. *See* MANKIW, *supra* note 142, at 192, 218, 244.

170. *Id.* at 271–76.

171. *Id.* at 278.

172. *Id.* at 327 (discussing the hypothesis that the 1929 stock market crash reduced household wealth and thus dampened consumer spending and aggregate demand); *id.* at 328 (explaining how tax increases during the early 1930s reduced consumption and thus aggregate demand).

173. *See, e.g.*, *id.* at 480–81 (discussing the theory that consumers are reluctant to increase consumption if they anticipate future tax increases).

174. *Id.* at 274–75.

175. BAUMOL & BLINDER, *supra* note 159, at 77–80 (explaining this process of reaching a new equilibrium in ordinary markets).

176. MANKIW, *supra* note 142, at 276.

177. *See* Patinkin, *supra* note 157, at 557 (explaining that resistance to price reductions will prevent such an automatic adjustment).

economy will remain "stuck" at a disequilibrium of less than full employment.[178]

Moreover, even completely flexible prices will not guarantee a return to full employment. The scenario just described assumes that the aggregate supply curve in fact remains vertical—that is, that lower prices will have no impact on the total output that firms are willing to supply. This assumption may prove untrue in the real world because of the impact of falling prices on real wages and thus the cost of labor, a major input in most production. As John Maynard Keynes argued, workers resist reductions in their nominal "money-wage," even when prices are falling all around them.[179] If aggregate prices fall more precipitously than nominal wages, real wages—and thus the relative cost of labor—will rise.[180] This rise in real wages will increase production costs, reduce the amount of output that firms are willing to supply at any given price, and result in a sloped supply curve, preventing a return to full employment despite complete price flexibility.[181] Eventually, persistent unemployment may induce a fall in nominal and thus real wages, returning the supply curve to its vertical state. In the shorter run, however, only fiscal policy, monetary policy, or a countervailing shock can restore the economy to full employment.[182]

B. Macroeconomic Effects of New Deal Cartelization

As explained earlier, lax enforcement of the antitrust laws likely encouraged horizontal collusion before the Great Depression. Such collusion could have reduced aggregate demand during the late 1920s in one of two ways. First, higher prices could have increased the aggregate price level and thereby reduced aggregate demand.[183] Second, higher prices could have transferred income from consumers, who spend a large

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178. MANKIW, *supra* note 142, at 274–75; F. M. SCHERER, INDUSTRIAL MARKET STRUCTURE AND ECONOMIC PERFORMANCE 363 (2d ed. 1980) (explaining how inflexible monopoly pricing can prevent price reductions despite drop in aggregate demand and thus prevent increase in real balances that would bolster demand); *cf.* Romer, *supra* note 156, at 781–83 (finding that the exogenous increase in the money supply, and not self-correction, prompted economic recovery during the 1930s).

179. *See* JOHN MAYNARD KEYNES, THE GENERAL THEORY OF EMPLOYMENT, INTEREST AND MONEY 7–13 (1936).

180. *See id.*; *see also* DORNBUSCH ET AL., *supra* note 104, at 111–16 (explaining how "sticky" wages can prevent self-correction from an economic downturn).

181. *See* WENDY CARLIN & DAVID SOSKICE, MACROECONOMICS AND THE WAGE BARGAIN: A MODERN APPROACH TO EMPLOYMENT, INFLATION, AND THE EXCHANGE RATE 49 (1990) ("A central component . . . of Keynes's model . . . is the failure of money wages to fall. This market imperfection led, in the context of a fall in autonomous demand, to the real wage rising and the consequent fall in employment and output . . . ."); *see also* MANKIW, *supra* note 142, at 169 (explaining how the failure of wages to fall can affect the aggregate supply curve and prevent recovery to full employment).

182. *See* BAUMOL & BLINDER, *supra* note 159, at 714–16 (explaining how inflexible wages can prevent the economy's "self-correction," thereby necessitating a policy response); MANKIW, *supra* note 142, at 331–32 (explaining how more activist monetary policy could have counteracted the Depression).

183. *See supra* notes 150–58 and accompanying text (explaining how aggregate demand depends on the price level).

fraction of their income, to cartelists and their shareholders, who spend a smaller fraction of their income. This latter effect would reduce overall consumption expenditures and thus cause a shift in the aggregate demand curve down and to the left.[184]

After the onset of the Depression, the NIRA imposed cartels and cartel-facilitating practices throughout the economy.[185] The NIRA also required collective efforts to raise wages and the post-*Schechter Poultry* NLRA followed suit. Basic microeconomics would predict that such schemes would raise wages and prices and that was the object of such schemes—to raise wages and thus the "purchasing power" of labor so as to counteract a pre-Depression drop in such purchasing power and thereby foster economic recovery.[186]

Employing the tools of aggregate demand and aggregate supply developed above, we can generate predictions about the likely effects of the various forms of New Deal cartelization. Indeed, John Maynard Keynes predicted, in an open letter to President Roosevelt shortly after the NIRA was passed, that the NIRA's wage and price fixing would slow recovery from the Depression, and he was not alone.[187] As a theoretical matter, Keynes and others were on solid ground. Wage and price floors can interfere with the ordinary process of macroeconomic adjustment and self-

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184. *See* SCHERER, *supra* note 178, at 362 ("Monopolistic pricing may be a *cause* of recession if it reinforces tendencies toward the stagnation of demand—e.g., by transferring too much income into the hands of individuals or groups with high marginal propensities to save.").

185. *See supra* notes 111–24 and accompanying text.

186. *See supra* notes 125–28 and accompanying text.

187. *See* Letter from John Maynard Keynes to President Franklin D. Roosevelt (Dec. 30, 1933), *in From Keynes to Roosevelt: Our Recovery Plan Assayed*, N.Y. TIMES, Dec. 31, 1933, at XX2 ("[T]oo much emphasis on the remedial value of a higher price-level as an object in itself may lead to serious misapprehension of the part prices can play in the technique of recovery. The stimulation of output by increasing aggregate purchasing power [i.e., aggregate demand] is the right way to get prices up; and not the other way around."); *id*. ("[M]y first reflection—[is] that NRA, which is essentially reform and probably impedes recovery, has been put across too hastily, in the false guise of being part of the technique of recovery."). Keynes was not the only contemporary economist who recognized that the NIRA's wage and price fixing provisions would stultify economic recovery. *See* ECONOMIC RECONSTRUCTION: REPORT OF THE COLUMBIA UNIVERSITY COMMISSION 17 (1934) ("It is the rise of prices reflective of increased demand and increased purchasing power which alone can be associated with the process of recovery. The concomitant illusion that a *deliberate* limitation of output, because it raises prices, helps toward recovery is a still more dangerous fallacy."); *id*. at 17–18 ("[A]n all-round application of [NIRA price fixing] would make for general impoverishment and would solve the problem of 'poverty in the midst of plenty' by removing the plenty."); Henry Simons, *A Positive Program for Laissez Faire: Some Proposals for a Liberal Economic Policy* (Harry D. Gideonse ed., Public Policy Pamphlet No. 15, 1934), *reprinted in* ECONOMIC POLICY FOR A FREE SOCIETY 40, 53 (1948) (contending that wage and price inflexibility was "[a] major factor in the cycle phenomenon"); *id*. ("Decisively important in the total situation is the exceeding inflexibility of wages—the explanation of which would require attention to many factors, of which effective labor organization is but one."); *id*. at 75 (condemning the NIRA's wage and price fixing provisions); *see also* Alan J. Meese, *Will, Judgment, and Economic Liberty: Mr. Justice Souter and the Mistranslation of the Due Process Clause*, 41 WM. & MARY L. REV. 3, 46–49 (1999) (contending that the NIRA and other legislation that increased wages likely slowed economic recovery).

correction described above, whereby falling prices increase the real value of the money supply, stimulate aggregate demand, and return output to the full employment level given a vertical supply curve.[188] Thus, if the NIRA codes and other New Deal cartelization policies had merely stabilized prices (or wages), they would have prevented the process of ordinary macroeconomic adjustment from occurring. If such cartelization *raised* wages and prices as intended, this impact would have exacerbated the downturn by further reducing aggregate demand and flattening the aggregate supply curve, thus deepening the Depression.[189]

Modern economists have also speculated that the NIRA lengthened and deepened the Depression, in part because alternative explanations for the severity of the Depression have proven elusive.[190] Thus, empirical work in the past two decades has sought to explain why the 1929 downturn proved deeper and more durable than downturns before or since.[191] Economists have concluded that the NIRA and NLRA combined to deepen and lengthen the Great Depression, vindicating the theoretical prediction of Keynes and his contemporaries. Indeed, President Obama's first Chair of the Council of Economic Advisors, Christina Romer, concluded long before her tenure in Washington that the NIRA, particularly its wage provisions, helped produce modest wage and price *inflation* from 1933 through 1937, even though the Depression's large reductions in output and employment should have resulted in wage and price *deflation* in a well-functioning free economy.[192] This finding confirms the Obama Administration's speculation that New

188. *See* SCHERER, *supra* note 178, at 363 (contending that inflexible monopoly pricing can prevent price reductions despite a drop in aggregate demand and thus prevent an increase in real balances that would increase demand); Christina D. Romer, *The Nation in Depression*, 7 J. ECON. PERSP., Spring 1993, at 19, 25 ("In the conventional textbook model a fall in wages and prices raises real balances, lowers interest rates, and thus stimulates investment. The rise in investment serves to counteract at least some of the fall in demand."); *supra* notes 175–78 and accompanying text. *See generally* Pigou, *supra* note 157, at 343 (elaborating on the claim that a fall in wages and prices will increase real balances and stimulate aggregate demand, and defending it against Keynesian criticism).

189. *See supra* notes 179–82 and accompanying text.

190. *See* FRIEDMAN & SCHWARTZ, *supra* note 104, at 498–99 (contending that the NIRA and NLRA raised wages and prices between 1933 and 1937 and likely slowed the rise in national output during this period); Harold L. Cole & Lee E. Ohanian, *The Great Depression in the United States from a Neoclassical Perspective*, 23 Q. REV. (Fed. Reserve Bank of Minneapolis, Minneapolis, Minn.), Winter 1999, at 2 (reviewing various other possible explanations for the length and depth of the Depression and concluding that no such explanation is convincing); *id.* at 21 (speculating that "[b]y permitting monopoly and raising wages, the NIRA would be expected to have depressed employment, output, and investment in the sectors the act covered, including manufacturing").

191. *See generally* Cole & Ohanian, *supra* note 114; Romer, *supra* note 156; Christina D. Romer, *Why Did Prices Rise in the 1930s?*, 59 J. ECON. HIST. 167 (1999) [hereinafter Romer, *Why Did Prices Rise?*].

192. *See* Romer, *Why Did Prices Rise?*, *supra* note 191, at 187–93 (testing and confirming the hypothesis that the NIRA's wage and price provisions helped bring about wage and price inflation despite significant output reductions in the early 1930s); *id.* at 196 ("As a result [of the NIRA and rapid growth in 1933], the huge negative deviations of output from trend early in the recovery put no countervailing downward pressure on prices.").

Deal cartelization reduced the welfare and "purchasing power" of consumers in cartelized markets.[193]

Professor Romer's research also reached the additional conclusion that NIRA-induced wage and price inflation interfered with the ordinary process of macroeconomic self-correction, whereby falling prices increase real income, stimulate aggregate demand, and return output to the full employment level.[194] As she put it:

> The more important effect of the NIRA was to diminish the responsiveness of price changes to the [negative] deviation of output from trend. By preventing the large negative deviations of [GDP] from trend in the mid-1930s from exerting deflationary pressure, it prevented the economy's self-correction mechanism from working. Thus, the NIRA can be best thought of as a force holding back recovery, rather than as one actively depressing output.[195]

This conclusion supplemented Professor Romer's previous findings that inflexible wages and prices had resulted in an upward-sloping supply curve during the early 1930s, thereby accentuating the impact of demand shocks.[196] Thus, she attributes the ultimate economic recovery to stimulative monetary policy and a resulting shift in the aggregate demand curve, and not to any process of self-correction.[197]

More recently, other economists have reached similar conclusions about both the behavior of wages and prices after enactment of the NIRA, as well as the dampening impact that such increases had on recovery. These scholars conclude that wages and prices in industries covered by the NIRA rose significantly between 1933 and 1939, while wages and prices in other industries remained flat.[198] While recognizing that the NIRA ended in mid-1935, these scholars conclude that the NLRA provided stronger collective bargaining rights for employees than the NIRA and that antitrust enforcement rates were even lower from 1935 through 1939 than during the 1920s, as the Roosevelt Administration declined to prosecute heavy industries that reached collective bargaining agreements with unions protected by the NLRA.[199] The resulting cartelization of labor and industry reduced output and raised wages and prices in the cartelized industries above the levels found in more competitive sectors.[200] This cartelistic output reduction reduced employment, causing unemployed labor to flow to its second best use in more competitive markets, and further depressed

193. *See supra* notes 47–50 and accompanying text.
194. *See* Romer, *supra* note 188, at 19, 25.
195. Romer, *Why Did Prices Rise?*, *supra* note 191, at 197.
196. *See* Romer, *supra* note 188, at 25 ("Between 1929 and 1933, a series of shocks caused aggregate demand to decline repeatedly in the United States. These declines in aggregate demand moved the economy down along an upward-sloping aggregate supply curve. The net result was both progressively worsening unemployment and deflation.").
197. *See* Romer, *supra* note 156, at 757.
198. *See* Cole & Ohanian, *supra* note 114, at 787–93.
199. *Id.* at 785–86.
200. *Id.* at 787–94.

wages in those sectors.[201] This wage difference caused unemployed workers to decline work in the competitive sector and to search for more remunerative work in the cartelized sector, extending the length of their unemployment and depressing national output.[202] Put another way, many workers refused to enter the labor force at competitive wages, thereby creating a positively sloped aggregate supply curve and dampening output.[203] By supplanting competition in labor and other markets, the NIRA, NLRA, and related laxity in antitrust enforcement artificially raised wages and prices, reduced the welfare and purchasing power of consumers in affected markets, and prevented free markets from reaching equilibrium. Thus, these policies dampened aggregate demand, constricted aggregate supply, and slowed the economy's recovery to full employment. There can be little doubt that New Deal cartelization deepened and lengthened the Great Depression.

C. Lessons (Perhaps) for Current Enforcement Policy?

In her speech describing the Obama Administration's more aggressive enforcement policy, Ms. Varney did not specify how "inadequate antitrust oversight" contributed to the Great Recession that formed the backdrop of her announcement.[204] Nor did she explain how more vigorous enforcement would have prevented or ameliorated the recent downturn. Still, the lessons of the NIRA and other forms of New Deal cartelization for antitrust policy would seem unmistakable: competition, not monopoly or cartelization, will foster the sort of price reductions necessary to ameliorate and ultimately correct recessions.[205] By extension, it seems that lax antitrust enforcement and resulting anticompetitive pricing can reduce aggregate demand and spark an economic downturn in one of two ways. First, high prices can reduce the real value of money balances, thereby raising interest rates and reducing investment.[206] Second, monopoly prices can transfer income from

201. *Id.* at 805–07.

202. *Id.*

203. *See supra* notes 179–82 and accompanying text (explaining how workers' resistance to wage reductions can impact the aggregate supply curve).

204. *See* Varney, *supra* note 2, at 4–5.

205. *See* ARTHUR M. OKUN, PRICES AND QUANTITIES: A MACROECONOMIC ANALYSIS 342 (1981) (explaining how more stringent antitrust laws and weakened collective bargaining could enhance price and wage flexibility and thus help prevent shocks to aggregate demand from reducing output); SCHERER, *supra* note 178, at 363 (articulating the theoretical possibility that inflexible monopoly pricing could prevent price reductions despite a drop in aggregate demand, and thus prevent an increase in real balances that would increase demand); *see also* MANKIW, *supra* note 142, at 266–67 & tbl.9-2 (discussing how various factors, including the cost of price adjustments, can deter reductions that would otherwise restore aggregate demand); N. Gregory Mankiw, *Small Menu Costs and Large Business Cycles: A Macroeconomic Model of Monopoly*, 100 Q. J. ECON. 529, 536–37 (1985) (contending that the possession of monopoly power can exacerbate price stickiness and thus dampen aggregate demand during a downturn); Romer, *Why Did Prices Rise?*, *supra* note 191, at 187–93 (finding that the NIRA resulted in wage and price increases during the early to mid-1930s, despite high unemployment).

206. *See supra* notes 154–56 and accompanying text (explaining this effect of increased prices).

high spending consumers to more frugal producers, reducing consumption and further reducing demand.[207] Thus, it seems obvious that before or during a depression or recession, antitrust policy should seek to ban monopolists' practices that exclude or hamper rivals, reduce competition, and raise consumer prices, even if the challenged practice might create more economic value than it destroys and thus enrich producers more than it harms consumers.[208] Any resulting static reduction in economic welfare would be a small price to pay for overall macroeconomic stabilization.

In fact, University of Chicago economist Henry Simons argued as much in the mid-1930s. Then a lonely proponent of *laissez faire*, Simons advocated vigorous government action to break up concentrations of economic power, including labor unions, to enhance wage and price flexibility and combat economic downturns.[209] In particular, he favored vigorous enforcement of existing antitrust laws, combined with a new federal statute chartering all corporations operating in interstate commerce and preempting contrary state chartering provisions.[210] Under this scheme, the FTC would set maximum limits on the amount of property that any single corporation could own, setting ownership ceilings low enough to ensure that markets remained competitive.[211] Moreover, unlike modern case law under section 2 that recognizes a safe harbor for monopoly achieved or maintained by means of efficiency,[212] Simons would have sacrificed efficiency when necessary to maintain competitive markets and resulting price flexibility. He expressly advocated capping the maximum size of firms below that necessary to achieve economies of scale when doing so was "ever necessary to the maintenance of the freedom of enterprise."[213] Simons's specific plan and overall agenda would seem to bolster the Obama Administration's assertion that inadequate antitrust enforcement from 2001 through 2008 helped induce and exacerbate the recession and that more aggressive enforcement via a consumer welfare effects standard would hasten macroeconomic recovery.

207. *See supra* notes 157–58, 184 and accompanying text (outlining such an "underconsumptionist" view of the origins of the Great Depression); *see also* SCHERER, *supra* note 178, at 362 ("Monopolistic pricing may be a *cause* of recession if it reinforces tendencies toward the stagnation of demand—e.g., by transferring too much income into the hands of individuals or groups with high marginal propensities to save.").

208. *See supra* notes 81–87 and accompanying text (explaining how practices uniquely condemned by the consumer welfare effects test invariably enhance economic welfare more than they reduce it).

209. *See* Simons, *supra* note 187, at 56–61.

210. *Id.* at 58–60.

211. *Id.*

212. *See supra* notes 61–74 and accompanying text (explaining that section 2 law has recognized a safe harbor for efficient conduct that created or maintained a monopoly for decades).

213. Simons, *supra* note 187, at 60 (insisting that the size of firms should be "even more narrowly limited" than that required to realize economies of scale).

IV. Modeling the Impact of a "Consumer Welfare" Standard on National Output

This section evaluates the claim that more aggressive section 2 enforcement, pursuant to a consumer welfare effects test, would have helped stave off the Great Recession or at least hastened recovery. As recounted earlier, lax enforcement could have contributed to our current economic woes in one of two ways.[214] First, lax enforcement and resulting high prices could have reduced aggregate demand and helped cause the current downturn by reducing the real value of money balances and also by transferring income from spendthrift consumers to more frugal producers.[215] Second, like the NIRA and other New Deal pro-cartelization measures, lax enforcement could have deepened and/or lengthened the 2008–09 downturn, whatever its initial cause, by exacerbating price inflexibility and preventing the sort of price reductions necessary to restart demand.[216] This, of course, is how the NIRA (with an assist from the NLRA on the wage front) apparently helped thwart the economy's self-correction from the 1929 downturn that resulted in 25 percent unemployment.[217] These two phenomena need not be mutually exclusive. Lax enforcement could conceivably help induce a downturn and then prevent or slow recovery. Nevertheless, any claim that more aggressive section 2 enforcement would prevent recession or hasten recovery does not withstand scrutiny. If anything, more intrusive enforcement would be counterproductive.

A. The (Very) Modest Impact of Modern Section 2 Enforcement

Any claim that more aggressive section 2 enforcement could help stabilize the economy ignores the modest economic impact of such a policy change. Recall in this connection that the NIRA authorized otherwise unlawful horizontal arrangements in more than 500 industries, accounting for roughly 80 percent of private sector non-farm employment.[218] While the Supreme Court dispatched the codes in *Schechter Poultry*, the NLRA authorized the cartelization of labor, and at least 26 percent of American workers had joined unions by 1940.[219]

No one argues that the Bush Administration took its cue from the New Deal and encouraged cartelization of industry or labor in violation of section 1 of the Sherman Act. On the contrary, even its detractors concede

214. *See supra* notes 206–07 and accompanying text.

215. *See supra* notes 157–58, 184 and accompanying text (collecting authorities articulating this "underconsumptionist" account of the Depression).

216. *See supra* notes 175–78 and accompanying text (collecting authorities explaining how monopoly pricing can prevent price reductions and resulting self-correction).

217. *See supra* notes 185–203 and accompanying text.

218. *See supra* notes 114–41 and accompanying text.

219. *See* Cole & Ohanian, *supra* note 114, at 785 (reporting that union membership rose from 13 percent of employment in 1935 to 29 percent in 1939); Wachter, *supra* note 141, at 27 (reporting that 26 percent of the private workforce was unionized in 1940).

that the Bush DOJ vigorously pursued and prosecuted cartels.[220] Any effort to connect lax antitrust enforcement with the economic downturn must focus exclusively on section 2 and demonstrate that more aggressive antitrust regulation of monopolies would have thwarted or ameliorated the Great Recession.

Yet there is no reason to believe that private monopoly achieved or maintained in violation of a consumer welfare effects standard is sufficiently widespread that more aggressive enforcement can affect the macroeconomy. Every indication is to the contrary. Indeed, some monopolies obtain and maintain their dominance via conduct that survives that more exacting standard.[221] Neither the Obama Administration nor other proponents of more aggressive enforcement have asserted that monopolies are ipso facto unlawful.[222] Even the Clinton Administration, which the Obama Administration praised for its aggressive pursuit of monopolists, argued that Microsoft had initially obtained its monopoly by means of conduct beyond the reach of section 2.[223]

The records of those administrations that consciously took a more aggressive section 2 enforcement posture are perhaps the "best evidence" of the impact of such an approach. Consider President Clinton's Antitrust Division, which promised a more aggressive approach than its predecessors.[224] During Mr. Clinton's eight years as President, the Antitrust Division brought at most a dozen monopolization cases.[225] The case challenging the conduct with by far the largest potential impact on the macroeconomy was the 1998 suit against Microsoft, whose total revenues, including those from international operations, accounted for less than 0.2 percent of U.S. GDP that year.[226] Even if these enforcement actions each

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220. *See* AAI TRANSITION REPORT, *supra* note 7, at 21 ("AAI believes that the [Clinton and Bush Antitrust] Division deserves outstanding marks for its cartel enforcement activities, particularly for the surge of enforcement that has occurred since 1995."); Robert Pitofsky, *Some Predictions About Future Antitrust Enforcement*, 16 GEO. MASON L. REV. 895, 896 (2009) ("Also, as far as the [Bush] Antitrust Division is concerned, any reservations I have about the level of enforcement do not extend to cartel enforcement, where I believe the DOJ has been as good or better than almost any administration in my recollection."); *cf. supra* notes 101–03 and accompanying text (recounting lax anti-cartel enforcement during the Coolidge administration).

221. *See* AAI TRANSITION REPORT, *supra* note 7, at 66.

222. *Cf. supra* note 80 and accompanying text (describing an even more intrusive standard of no fault liability for monopolists).

223. *See* Brief for Appellant United States of America at 4, United States v. Microsoft, 56 F.3d 1448 (D.C. Cir. 1995) (No. 95-5037), 1995 WL 17907891 at *4 (detailing the government's conclusion that Microsoft had obtained its monopoly lawfully); AAI TRANSITION REPORT, *supra* note 7, at 58–59 (praising the Clinton Administration for bringing "at least seven monopolization cases").

224. *See* Stephen Labaton, *Rousing Antitrust Law from Its 12-Year Nap*, N.Y. TIMES, July 23, 1993, at F8 (predicting more aggressive antitrust enforcement by President Clinton's Antitrust Division).

225. *See supra* note 27 and accompanying text.

226. In 1998, Microsoft's revenue was $14.5 billion. *See Microsoft 1998 Annual Report: Financial Highlights*, MICROSOFT, http://www.microsoft.com/investor/reports/ar98/fins.htm (last updated May 27, 2010). The U.S. GDP that year was $8.8 trillion in then-current dollars. *See* Press Release, Bureau of Econ. Analysis, Annual Input-Output Accounts of the

resulted in reduced prices in the markets in question, it is hard to believe that such reductions had any more than a negligible impact on the overall price level that determines aggregate demand.

The mere fact that the Clinton Administration was more aggressive than the Bush Administration, however, does not establish that President Clinton's Antitrust Division pursued a bona fide consumer welfare effects test. "More aggressive" does not mean "sufficiently aggressive." The only administration we can confidently say pursued the sort of aggressive policy that the Obama Antitrust Division has outlined is President Obama's. Yet in the nearly three years after the withdrawal of the Section 2 Report, the current administration has charged exactly one firm with a section 2 violation.[227] That firm—a hospital in Wichita Falls, Texas, population 104,000—had 2009 revenues of $265 million, compared to a national GDP nearly 50,000 times larger.[228] The Great Recession did not begin in Wichita Falls, and unlawful monopolization of that town's hospital market did not weaken the current recovery.

In fact, any impact of the Obama Administration's invigorated section 2 enforcement pales in comparison to the impact of its encouragement of outright cartels—labor cartels—under the guise of collective bargaining.[229] As explained earlier, economic historians have concluded that union wage fixing helped slow recovery from the 1930s Depression.[230] Currently, unions represent about 7 percent of the nation's private sector workers.[231] To be sure, this is a decline from the late 1940s, when organized labor

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U.S. Economy, 1998 (Dec. 13, 2001), *available at* http://www.bea.gov/newsreleases/industry/io/2001/pdf/io1201.pdf.

In 1996, the Clinton Antitrust Division also sued General Electric (GE). *See* United States v. Gen. Electric Co., No. 96-CV-121, 1999 WL 819637, at *1 (D. Mont. Jan. 11, 1999) (noting complaint filed Aug. 1, 1996). The suit challenged GE's alleged monopolization of the market for "servicing of medical imaging equipment." *Id.* at *5. According to GE's Annual Report to Shareholders, "Technical Products and Services," of which Medical Equipment and Service was a subset, provided less than 6 percent of the company's $100 billion in revenue in 1998. *See GE 2000 Annual Report: Financial Section*, GE, at 44 (Feb. 2, 2001), http://www.ge.com/annual00/financial/images/GEannual00_financials.pdf (showing $5.323 billion in revenue for that segment). Thus, the government's case against GE impacted far less than 0.1 percent of GDP.

227. *See* Press Release, U.S. Dep't of Justice, *supra* note 15; Thomas Catan, *Obama DOJ Files Long-Promised Monopolization Case*, WALL ST. J. L. BLOG (Feb. 28, 2011, 2:13 PM), http://blogs.wsj.com/law/2011/02/28/at-last-obama-doj-files-long-promised-monopolization-case/.

228. *See* Press Release, U.S. Dep't of Justice, *supra* note 15 (reporting the defendant's annual revenues); *Current-Dollar and "Real" GDP*, BUREAU ECON. ANALYSIS, http://www.bea.gov/national/xls/gdplev.xls (last updated Jan. 27, 2012) (reporting current-dollar GDP of $13.9 trillion in 2009).

229. *See generally* Harold P. Coxson & Christopher R. Coxson, *The National Labor Relations Board in the Obama Administration: What Changes to Expect*, U.S. CHAMBER COMMERCE (Sept. 2009), http://www.uschamber.com/sites/default/files/reports/090915_nlrb_report.pdf (detailing the Obama NLRB's various pending initiatives to strengthen the position of unions at the expense of management).

230. *See supra* notes 192–203 and accompanying text.

231. *See* News Release, Bureau of Labor Statistics, Union Members—2010 (Jan. 21, 2011), *available at* http://www.bls.gov/news.release/pdf/union2.pdf (reporting that 6.9 percent of private sector employees belong to unions).

represented over 30 percent of the nation's private sector workforce.[232] Nevertheless, the collective impact of union wage-fixing still apparently dwarfs the collective impact of the monopolistic conduct the Division has challenged in the past two decades.[233] It is therefore hard to describe more aggressive section 2 enforcement as part of a coherent "national economic strategy" designed to facilitate economic recovery, as the Obama Administration claimed.[234]

More importantly, the impact of section 2 enforcement is likely insignificant compared to the ordinary tools of macroeconomic stabilization—monetary and fiscal policy. Just over a year before the Antitrust Division saved Wichita Falls from a hospital monopoly, Congress passed and the President signed a bill approving $787 billion in tax cuts and spending increases designed to combat the recession.[235] This came just one year after President Bush approved a $168 billion scheme of tax rebates.[236] During the same period, the Federal Reserve purchased more than $1.7 trillion worth of Treasury Bonds and mortgage-backed securities, the first of two rounds of "quantitative easing" designed to increase the nation's money supply and reduce interest rates.[237] These textbook responses to the Great Recession presumably dwarf the impact of more aggressive section 2 enforcement.[238]

B. How a Consumer Welfare Effects Test Could Backfire and Dampen GDP

In any event, there is a more fundamental reason to doubt that adoption of the novel and more intrusive consumer welfare effects test will enhance aggregate demand and assist economic recovery. Simply put, the conduct

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232. *See* Wachter, *supra* note 141, at 27 (reporting that union membership reached 34 percent of the workforce by 1945).

233. Employee compensation accounts for about 64 percent of national income and, thus, GDP. *See* 2011 ECON. REP. PRESIDENT 222 tbl.B-28, *available at* http://www.whitehouse.gov/sites/default/files/microsites/2011_erp_full.pdf; *cf. supra* notes 226–28 and accompanying text (identifying only thirteen section 2 enforcement actions under the Clinton, Bush, and Obama Administrations, none of which impacted more than 0.2 percent of the nation's GDP).

234. *Cf.* Varney, *supra* note 2, at 5 (contending that more vigorous section 2 enforcement could be part of the "nation's economic strategy" to respond to the economy's "extreme conditions").

235. *See* David M. Herszenhorn, *Party Lines Barely Shift as Package Is Approved*, N.Y. TIMES, Feb. 14, 2009, at A15.

236. *See* John Sullivan, *Tax Rebates in $168 Billion Stimulus Plan Begin Arriving in Bank Accounts*, N.Y. TIMES, Apr. 29, 2008, at A10.

237. *See* Sudeep Reddy, *The Fed Decision: How It Works; When It Doesn't*, WALL ST. J., Nov. 4, 2010, at A15; *Quantitative Easing Explained*, LIBER8: ECON. INFO. NEWSL. (Fed. Reserve Bank of St. Louis, St. Louis, Mo.), Apr. 2011, *available at* http://liber8.stlouisfed.org/newsletter/2011/201104.pdf (describing the first two rounds of "quantitative easing").

238. *See supra* notes 182, 197 and accompanying text (collecting sources advocating fiscal and monetary responses to economic downturn); *see also* Alan Devlin, *Antitrust in an Era of Market Failure*, 33 HARV. J.L. & PUB. POL'Y 557, 588 (2010) (contending that antitrust doctrine is suited for addressing market-level failures, but is not an appropriate tool for macroeconomic stabilization).

subject to such a test is far different from the New Deal era cartels that deepened and lengthened the Depression. Even if the monopolistic conduct uniquely subject to this more intrusive test has a substantial impact on aggregate prices and aggregate demand, it is not clear what form such impact will take. For reasons outlined below, some such conduct may even *reduce* aggregate prices. In the long run, application of the consumer welfare effects test could prevent positive shifts in the aggregate supply curve and dampen growth in the nation's potential GDP.

Because any standard of section 2 liability other than per se legality will ban *some* price-raising conduct, an evaluation of a more aggressive standard's macroeconomic impact must focus on the subset of conduct that it uniquely captures: conduct causing harm to market consumers that barely exceeds, equals, or is less than its efficiency benefits.[239] Close analysis reveals that prohibiting this conduct likely will not enhance aggregate demand and may even reduce it. To be sure, monopolistic conduct that survives the Bush Administration's disproportionality test can, along with similar conduct by other monopolists, raise aggregate prices and thereby lower aggregate demand by reducing the real value of money balances and "transferring" income from consumers to monopolists and their shareholders. Application of the more intrusive consumer welfare effects test will ban such conduct simply because it results in prices that are higher than would otherwise prevail. Under such a standard, the monopolists' respective markets would be characterized by less exclusion, more competition, and lower prices.[240] Other things being equal, application of this new, more intrusive test would appear to reduce prices and enhance aggregate demand.

Other things are emphatically not equal, however, thereby distinguishing such aggressive enforcement from the anti-cartel enforcement that could have spurred recovery from the Depression. Unlike cartels or naked exclusion, which a disproportionality test would also condemn, the conduct that the consumer welfare effects test uniquely bans would produce efficiencies that outweigh the allocative harm produced by such conduct.[241] Condemning such conduct would reduce producer welfare more than the resulting increase in consumer welfare, thereby resulting in a net destruction of economic welfare.[242]

Recognition that a consumer welfare effects test will invariably reduce the economic welfare of participants in the relevant market undermines any claim that the more intrusive test will increase consumption by transferring income from producers to consumers. Application of the more intrusive test will increase consumers' income and thus their consumption expenditures, but such an increase will come at the expense of a greater—sometimes much greater—reduction in producers' income. After all, aside

239. *See supra* notes 81–83 and accompanying text (describing conduct banned by competition on the merits, disproportionality, and consumer welfare effects tests).

240. *See* Varney, *supra* note 2, at 7–8.

241. *See supra* notes 84–86 and accompanying text.

242. *See supra* note 87 and accompanying text.

from the impact of greater output at the margins, any increase in consumer income will come at the expense of an equal reduction in the income of producers, who must now charge lower prices.[243] Moreover, such producers will also suffer an additional loss in the form of higher costs that result from condemnation of efficiency-generating conduct.[244] Taken together, these two reductions in producer income will exceed any increase in consumer income resulting from increased output and lower prices.[245] Even if producers do, in fact, consume a smaller portion of their income than consumers, the resulting decrease in their consumption may still more than offset the increased consumption by consumers. At the very least, proponents of the novel consumer welfare effects test would find it difficult, if not impossible, to demonstrate that the increased expenditures by individual consumers would exceed the magnitude of the reduction in producer expenditures.

Of course, the realization that a consumer welfare effects test reduces the overall economic welfare of participants in the relevant market does not rebut the separate claim that this new standard would increase aggregate demand by reducing the aggregate price level—a construct that does not incorporate producers' welfare.[246] The increase in producer welfare, however, does not exhaust the economic impact of the efficiencies that characterize this category of conduct. Such efficiencies will have impacts in other markets as well. By reducing the monopolist's costs of producing and/or distributing each unit of (admittedly reduced) output, the challenged conduct would free up the real resources previously employed to produce the monopolist's more costly output for use in other markets.[247]

Antitrust analysis generally ignores the impact of conduct upon output and prices in other markets because such analysis rests on the so-called partial equilibrium trade-off model, which assumes for convenience that a challenged practice or transaction has no effects beyond the market in question.[248] By focusing on a single market to the exclusion of others, economists and others can generate tractable conclusions about the impact of studied practices on economic welfare, free of the complications that

243. *See supra* notes 150–58, 162–69 and accompanying text.

244. *See supra* notes 86–87 and accompanying text.

245. *See supra* notes 86–87 and accompanying text (explaining that efficiency benefits of conduct uniquely subject to a consumer welfare effects test will significantly exceed "deadweight loss" in consumer surplus resulting from resulting market power).

246. *See supra* notes 76–80, 150–58 and accompanying text.

247. *See* BORK, *supra* note 72, at 108 ("Cost reductions [from a merger to monopoly that creates efficiencies] mean that the saved resources are freed to produce elsewhere in the economy."); SCHERER, *supra* note 178, at 22 (explaining that the cost reduction resulting from a monopolist's realization of economies of scale frees up productive resources and thus increases output in other markets); *see also* Heyer, *supra* note 73, at 39–40 (explaining how merger that reduces production costs frees up resources for use elsewhere in the economy).

248. *See* Williamson, *supra* note 74, at 22–23 (graphically illustrating application of the partial equilibrium model to a merger to monopoly); *see also* BORK, *supra* note 72, at 107–15 (reproducing Williamson's graph and asserting that it can be used to illustrate all antitrust problems); VISCUSI ET AL., *supra* note 149, at 126–27 (reproducing the same graph and agreeing with Bork that the graph can be used to illustrate antitrust problems).

would arise when conducting a general equilibrium analysis that attempts to incorporate impacts in other markets.[249] This, however, may well be one more instance in which application of the partial equilibrium model produces misleading results.[250] The aggregate demand and supply model is general equilibrium in nature, and any complete analysis of the impact of a novel enforcement standard on GDP must presumably shed the blinders of the partial equilibrium framework and attempt to ascertain the overall impact of that standard, not just the impact in the allegedly monopolized market.[251]

This more discerning analysis paints a quite different picture of the impact of a novel consumer welfare effects standard on the aggregate price level, aggregate demand, and GDP. The consumer welfare effects test will admittedly maximize output (and thus reduce prices) in the particular markets where such challenged practices take place.[252] To this extent, it will increase aggregate demand.[253] At the same time, such challenged conduct produces significant efficiencies. In the partial equilibrium model, these efficiencies manifest themselves as lower production costs for the monopolist and enhanced profits for the monopolist's shareholders.[254] Thus, debate about the appropriate welfare standard in antitrust often focuses on whether this and other improvements in producers' welfare should factor into the welfare calculus,[255] but this debate diverts attention from the impact of efficiencies that this model does not capture. Whether or not the benefits of cost reductions are "passed on" to consumers in the relevant market, such efficiencies will free up productive resources that will flow to other sectors in the economy—a fact rarely noted in the antitrust

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249. *See* BORK, *supra* note 72, at 113–15 (explaining why antitrust analysis should generally take a partial equilibrium approach); KAYSEN & TURNER, *supra* note 66, at 12 & n.11 (embracing so-called "Pigouvian assumption" that "we can apply the concept of efficiency to individual industries and firms," "even though economy-wide efficiency is impossible to achieve"); *see also* VISCUSI ET AL., *supra* note 149, at 76 (explaining how partial equilibrium tools focus on impacts in a particular market to avoid second best problems presented by general equilibrium analysis when some markets are characterized by monopoly, externalities, and other departures from perfect competition); Arnold C. Harberger, *Three Basic Postulates for Applied Welfare Economics: An Interpretive Essay*, 9 J. ECON. LITERATURE 785, 789–91 (1971) (conceding that welfare analyses performed by economists are usually partial equilibrium in nature, but also arguing that general equilibrium welfare analyses of such problems are possible).

250. *See generally* Alan J. Meese, *Reframing Antitrust in Light of Scientific Revolution: Accounting for Transaction Costs in Rule of Reason Analysis*, 62 HASTINGS L.J. 457 (2011) (explaining how the application of the partial equilibrium paradigm can produce misleading results in the Rule of Reason context).

251. *See supra* notes 148–52 and accompanying text.

252. *See supra* notes 84–86 and accompanying text.

253. *See supra* note 152 and accompanying text.

254. *See supra* notes 84–86 and accompanying text.

255. *See generally* Heyer, *supra* note 73 (describing the contending positions in this debate and arguing for adoption of the "total welfare" approach that maximizes the welfare of all consumers, and not merely those who happen to purchase the monopolist's product).

literature.[256] Because this resource flow will not enhance market power in other markets, output in those markets will almost invariably increase.[257]

The partial equilibrium trade-off apparatus allows us to ascertain the value of this countervailing output increase in other markets. Like all other firms, monopolists must bid in input markets to purchase productive resources, competing against firms who could employ the same resources to produce different goods and services. The resulting price for inputs—the monopolist's costs—presumably reflects what competing bidders would have paid for such resources, that is, the value of the output that such resources could have produced in other markets.[258] Thus, a challenged practice that reduces the monopolist's costs will also free up resources that presumably increase the value of output in other markets by an amount equal to the magnitude of the monopolist's cost reduction.[259]

Such output increases presumably reduce prices in other markets, thereby tending to increase the value of real money balances held by consumers in those markets and bolstering aggregate demand.[260] Indeed, in some cases, conduct that violates a consumer welfare effects standard might actually reduce the aggregate price level, by freeing up so many resources that output increases in other markets collectively lower prices that exceed the price increase in the monopolized market.[261] This distinguishes such conduct from the sort of New Deal cartels that produced no offsetting efficiencies and helped thwart economic recovery and suggests that the impact of the novel and more intrusive consumer welfare effects test on aggregate demand would be attenuated at best.[262]

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256. *See supra* note 247 and accompanying text.

257. The only exception will be for those presumably rare cases in which cost reductions in other markets manifest themselves entirely as reductions in fixed costs. In such cases, the welfare of producers in those markets will improve without any corresponding output increase or price reduction in that market. *Cf.* Heyer, *supra* note 73, at 36 ("[U]nlike changes in marginal cost, changes in fixed cost generally do not alter the firm's profit-maximizing price, or the level of output at which the firm maximizes its profits, unless they affect the firm's very viability."). Such a reduction in fixed costs, however, may free up resources that flow to other markets and reduce marginal costs there. Moreover, costs that are fixed in the short run may well become marginal in the longer run.

258. *See* FRANK KNIGHT, RISK, UNCERTAINTY AND PROFIT 92 (1921); STIGLER, *supra* note 136, at 112 ("[T]he cost of any productive service in producing *A* is the maximum amount it could produce elsewhere. The foregone alternative is the cost.").

259. *See* SCHERER, *supra* note 178, at 22 (explaining that the cost reduction resulting from a monopolist's realization of economies of scale frees up resources to produce output in other markets).

260. *Cf. supra* notes 84–86 and accompanying text.

261. In such cases, application of the consumer welfare effects standard would actually reduce consumer welfare as a whole, even if one excluded producers from the definition of "consumer" and included only those individuals who purchase products from producers. Put another way, application of a total welfare standard may in fact improve the welfare of such narrowly defined consumers more than application of a standard that purportedly seeks to maximize only their welfare.

262. Monopolized output reduction also frees up resources that can be employed to increase production in other markets, but such reductions "by definition" allocate resources to uses that produce less value than they would produce in the monopolized market, with no offsetting improvement in productive efficiencies. *See* SCHERER, *supra* note 178, at 18–19 ("[F]ailure to maximize the value of the output bundle and failure to maximize the sum of

In fact, the efficiencies produced by such conduct may also impact aggregate supply and the economy's potential output. A practice that reduces the costs of producing any given level of output in the monopolized market and frees up resources for use in other markets unambiguously increases the economy's potential output—the quantity of goods and services the economy can produce with any given endowment of resources.[263] To be sure, exercise of monopoly power in one market will prevent the macroeconomy from reaching its full potential in the short run, but over the medium and long run, competitors will eventually enter the market and erode the monopoly. Such entry will increase that market's output and move national output closer to its potential. In any case where the particular market is too difficult for competitors to enter and have an impact within two years, the DOJ and FTC already step in to challenge the monopolists' conduct.[264] Applying a consumer welfare effects test to ban such conduct entirely will prevent the realization of such aggregate supply benefits in the first place.

Even if future entry may not erode monopoly power in all markets, thus preventing the national output from reaching its full potential, national output may still be higher than it would be under a consumer welfare effects standard if the value of higher output in other markets outweighs the value of output lost in the monopolized market. Indeed, it seems likely that the value of output increases in other markets will predominate for the same reasons that conduct that the consumer welfare effects test uniquely condemns will almost always increase total welfare.[265] Such conduct will generally only reduce output "at the margins," leaving the vast majority of pre-monopoly output unscathed and limiting the value of output lost.[266] Moreover, the price that consumers would have paid for the forgone output would overstate the resulting reduction in national output because the resources once used to produce the monopolist's eliminated output would flow to inferior—and thus less valuable—uses in other markets.[267] Finally, the sort of beneficial practices banned by the consumer welfare effects test will presumably reduce the production costs of all of the monopolist's remaining output, which would enhance the magnitude of overall cost

consumers' plus producers' surpluses are conceptually identical manifestations of monopolistic resource misallocation."). It would be fortuitous, to say the least, if such output reductions and resulting misallocation of resources reduced the aggregate price level.

263. *See supra* notes 162–69 and accompanying text (explaining the concept of potential output and its relationship to aggregate supply).

264. *See* U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, HORIZONTAL MERGER GUIDELINES §§ 3.0, 3.2 (rev. ed. 1997), *available at* http://www.justice.gov/atr/public/guidelines/hmg.pdf (adopting such a two-year time horizon for evaluating the prospect of entry in the merger context).

265. *See supra* notes 86–87 and accompanying text.

266. Any conduct that creates greater than marginal output reductions will likely create very large consumer harm, and therefore would also fail the disproportionality test.

267. *See generally* SCHERER, *supra* note 178, at 14–19. That is, the actual harm will equal the difference between the price consumers would have paid for the foregone output and the cost of producing it.

reductions and the size of resulting output increases in other markets.[268] These various considerations suggest that this kind of conduct will almost always increase the economy's potential output, even if the condemned monopoly persists for the long run and reduces output in its own market below the competitive level. Therefore, even if adoption of the consumer welfare standard could (very modestly) enhance aggregate demand in the short run by reducing the prevalence of market power, any such benefits may well come at the high price of dampened growth in potential output and a smaller GDP in the long run.

Given the various possible impacts of conduct that survives the disproportionality test, antitrust courts should not attempt to determine the overall effect of a particular practice on the aggregate price level and potential output. Those who invoke macroeconomic considerations in support of a more intrusive standard of liability bear some burden of proving that the standard will do more good than harm. The conclusions of this Essay suggest that discharging such a burden would be difficult if not impossible. Indeed, given the ambiguous impact of such conduct, it seems likely that fiscal and monetary policy will prove to be far more effective tools of short-term macroeconomic stabilization than more intrusive section 2 enforcement.

More than four decades ago, Nobel Laureate Oliver Williamson rejected more intrusive antitrust enforcement standards in favor of a total welfare approach, in part because that approach would enhance potential output and long-run economic growth.[269] He espoused the following view:

> Economic theorizing, research, and policy discussion have tended to be excessively concerned with "macro-economic" . . . to the neglect of "micro-economic" problems of efficient resource allocation, whose solutions are likely over the long run to be more important to the achievement of a highly productive and rapidly growing economy. In a fully employed economy, the main concern of economic theory is with these "micro-economic" problems of allocation of scarce resources among competing uses.[270]

The lesson, according to Williamson, is simple. Antitrust is not a tool of macroeconomic stabilization. Instead, the Sherman Act should stick to what it does best—namely, banning any practice that results in a net reallocation of resources, while leaving unscathed conduct that, despite increasing consumer prices, creates significant efficiencies, frees up resources for use in other markets, and increases potential output. Courts implementing section 2 have embraced this preference for efficiency-

268. *Cf.* Fisher & Lande, *supra* note 85, at 1626 ("[C]ost savings, however, extend to all products actually manufactured. Since output still produced typically far exceeds the amount reduced by increased monopoly power, relatively small increases in efficiency can—and usually will—dominate much larger increases in monopoly power . . . ."); *supra* notes 258–59 and accompanying text.

269. *See* Oliver E. Williamson, *Allocative Efficiency and the Limits of Antitrust*, 59 AMER. ECON. REV. (PAPERS & PROC.) 105, 105–06 (1969).

270. *See id.* at 112 (alterations in original) (quoting Harry G. Johnson, *The Economic Approach to Social Questions*, PUB. INT., Summer 1968, at 68, 69).

creating practices for most of the statute's 120-year history, apparently with good reason.[271]

CONCLUSION

For decades, courts applying section 2 have recognized a safe harbor for monopolists' conduct that creates significant efficiencies, even when such conduct reduces the welfare of consumers in the relevant market. Both the disproportionality and consumer welfare effects tests would result in more intrusive regulation of monopolists' practices than the standard applied in the case law. This Essay has evaluated the claim that the Bush Administration's disproportionality standard was analogous to the NIRA and other New Deal cartelization schemes, and thus helped cause and exacerbate the most recent economic downturn. This Essay also examined the Obama Administration's claim that application of the even more intrusive consumer welfare effects test would have helped prevent, or at least attenuated, the downturn.

As shown, section 2 enforcement can have only a very modest impact on the macroeconomy. The Obama Administration itself has only challenged one monopolist—and a local one at that. Furthermore, conduct that survives scrutiny under a disproportionality test, but fails the consumer welfare effects test, bears only passing economic resemblance to the New Deal cartels. While such conduct, like cartel pricing, reduces output in the relevant market, raises prices, and thus harms purchasers of the monopolist's product, it only survives scrutiny under the disproportionality test because it creates significant efficiencies. These efficiencies will almost certainly exceed the magnitude of the deadweight economic loss resulting from monopolistic output reduction. Not only do these efficiencies increase producers' income—and thus consumption—but they also free up resources that flow to other markets, increasing output and reducing prices in those markets. The realization of such efficiencies will also impact the long-run aggregate supply curve by enhancing society's potential output. Thus, it seems improbable that banning conduct uniquely subject to a consumer welfare effects standard will foster macroeconomic stability and maximize GDP over the long term. Instead, antitrust law and policy should focus on identifying and condemning those practices that on balance result in a misallocation of resources and a reduction in total economic surplus. Any more intrusive regulation will likely mean less potential output and less GDP.

271. *See supra* notes 61–74 and accompanying text.