

FEDERAL TRADE COMMISSION
HEARINGS ON THE STATE OF ANTITRUST

Testimony of Thomas W. Hazlett¹

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For a policy that is now, by federal statute, well over 100 years old, antitrust is surprisingly unsettled. It is not publicly controversial; there is no great groundswell to, say, amend the Sherman Act. It would awake many thousands of journalists were a presidential debate to feature an inquiry as to the candidate's view of the Herfindahl Index as an appropriate measure of market power, even as it might make many in this room swell with pride.

The controversy exists at the analytical level. When Robert Crandall and Cliff Winston review an impressive history of leading U.S. antitrust cases,² they find no evidence that the legal regime improves economic efficiency. Jonathan Baker, embarking on a parallel mission, arrives at a distinct conclusion.³ There is no consensus among economic experts on even this most basic of questions.

One consensus has been reached, however, and it is that the antitrust agencies have under-invested in analytical assessment of regulatory results. Dennis Carlton notes the "dearth" of "quantitative measures and studies,"⁴ while hearing a "frequent call for retrospective studies."⁵ His plea for empirical analysis to better inform institutions is sound. The antitrust agencies should more systematically create and incorporate "battle assessment" reports.

The practice should evaluate a range of regulatory actions some years ex post. Researchers should estimate Δp and Δq , incorporating quality changes and shifting (exogenous) economic conditions, in markets subject to antitrust regulation. Empirical evaluation should take special care to isolate the changes the associated

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² Robert W. Crandall and Clifford Winston. *Does Antitrust Policy Improve Consumer Welfare? Assessing the Evidence*, JOURNAL OF ECONOMIC PERSPECTIVES (Fall 2003), pp. 3-26.

³ Jonathan, B. Baker, *The Case for Antitrust Enforcement*, 17 JOURNAL OF ECONOMIC PERSPECTIVES (Fall 2003), pp. 27-50.

⁴ Dennis W. Carlton, *The Need to Measure the Effect of Merger Policy and How to Do It*, U.S. Department of Justice Antitrust Division, Economic Analysis Group Discussion Paper 07-15 (Dec. 2007), p. 1.

⁵ Ibid.

with regulatory intervention in merger cases, or lack thereof. The sample investigated should include mergers, mergers blocked, and mergers blocked by the agency and then permitted by the courts.

Such research is sorely lacking; there is little hard evidence produced by the antitrust enforcement agencies that their policies on net promote consumer welfare, nor on the myriad incremental trade-offs – how resources should be allocated across enforcement agency functions – imposed by real-world constraints.

Prof. Carlton alerts us to the fact that empirical results as to any particular merger must be interpreted with care. The optimal level of antitrust enforcement does not imply that no output-reducing merger ever be permitted, nor does it suggest that every output-enhancing merger be accommodated. Rather, it implies that, in aggregate, the benefits of antitrust exceed its costs. Hence, as Carlton notes, the finding that the DOJ/FTC enforcers failed to advance efficiency in a particular merger ruling tells us little about the distribution of antitrust outcomes. He suggests particular procedural reforms that improve analytical transparency and so trace agency analyses against the actual market outcomes that result.

This would constitute a large step forward. But the burdens imposed on antitrust agencies are large, and not likely to be well-supplied by regulators without innovative reforms, not yet devised, that cleverly incentivize the desired data production. Moreover, the vast majority of antitrust costs and benefits are distributed *across* markets. The price and performance of operating system software presumably yields some direct impacts from *U.S. v. Microsoft* (filed by the DOJ in May 1998). But fall-out affecting other ventures in similar or entirely distinct markets – say, in Internet search, or MP3 players – figures to be of larger magnitude. Of course, the primary purpose of law is to generally constrain behavior. This makes the total costs and benefits of a policy elusive.

Three brief points can be made in this brief treatment. The first is that the ex post empirical enterprise is, with all its limitations, utterly essential to the task at hand. If antitrust is to improve Consumer Welfare, it must seek to evaluate the actual results of its work. The presence of Type I and Type II errors should be incorporated into such analyses. The political equilibrium in which antitrust enforcement is nested is likely to be little interested in this pursuit, which explains why it is been so little undertaken. The gains are public, and accrue mainly to future consumers. What private gains can be extracted are likely in the form of rents to practitioners of law and economics,⁶ who should recognize a win-win when they see it, leading the way to better antitrust analysis.

⁶ While the returns are uncertain, the author has rendered some investments relevant to this call. For instance, a current research project, with Prof. Joshua Wright, investigates the post-merger outcome of Oracle-PeopleSoft.

A second front in this effort should be opened, which includes greater focus on non-price, non-quantity data in the analytical framework. In merger cases, in particular, antitrust agencies should incorporate evidence beyond “critical loss” analyses that require, indeed focus on, estimates of pre-merger and post-merger demand elasticities. Often the relevant data for such quantitative exercises are in limited supply; indeed, the post-merger estimates generally require forecasts of counter-factuals. In the best of circumstances, such tools help illuminate market parameters and render evidence regarding competitive effects, but the world is filled with second bests. In reality, other methods are often well suited to supply probative evidence. This is particularly true in high-tech markets dominated not by price competition but by dynamic innovation.⁷

Rich veins of data revealing the welfare effects of changes in market structure can be tapped in financial markets, e.g. Event studies have provided important evidence on mergers⁸ and on the effects of given antitrust investigations.⁹ That there are interpretive issues present in such research is true, but merely suggests that such evidence must be evaluated similarly to other economic evidence. Parallel to the analysis of share price movements, profits and firm capital values are important sources of information. When market power is considered, an implication is that excess returns are available. In the recent XM-Sirius merger, the competitive analysis was assisted by the fact that the aggregate enterprise value of the merging firms was (even with the assumption of a merger premium) considerably below total capital costs. The lack of supra-competitive profits associated with the merger was further buttressed by another set of facts: the rival industry, terrestrial broadcasting, was strongly opposed to the merger.¹⁰ Incorporating such data into the analysis adds robustness.

Finally, Prof. Carlton’s correct appeal for a marked increase in better organized ex post merger research concludes by saying, “Strong opinions are not substitutes for quantitative analysis.”¹¹ This point is clearly *incorrect*. It is commonly observed that strong opinions substitute for quantitative analysis.

The stronger version of this critique is that, even in a more perfect world, such will remain the case. The task for science is not to end “strong opinions,” but to encourage them to be better, more informed opinions. By selecting more merger cases to study in hindsight, a better framework for that analysis, to select relatively

⁷ William J. Baumol, *THE FREE MARKET INNOVATION MACHINE* (2002), p. 35.

⁸ Eckbo 1983 XXX

⁹ George Bittlingmayer and Thomas W. Hazlett, *Has Antitrust Enforcement Against Microsoft Created Value in the Computer Industry?* *JOURNAL OF FINANCIAL ECONOMICS* (March 2000).

¹⁰ Thomas W. Hazlett, *Some Dynamic Considerations in Merger Analysis: In General and With Respect to XM-Sirius*, *JOURNAL OF COMPETITION LAW & ECONOMICS* (2008); doi: 10.1093/joclec/nhn024.

¹¹ Carlton (2007), p. 16.

important cases (as do Crandall-Winston and Baker), and to interject a broader range of information revealing market dynamics, the triumph of better “strong opinions” might be enabled.