

Are efficient antitrust rules always optimal?

BY BRETT H. McDONNELL* and DANIEL A. FARBER**

Professors Gifford and Kudrle make a number of interesting and useful points. Their comparison of antitrust policy in the U.S. and the EU through the lens of four strands of policy—producer protection, rivalry, consumer surplus maximization, and wealth maximization—is of particular note. We will not take issue with their characterization of law and policy in the U.S. or the EU. We also will not argue with their preferred ultimate goal of improving the aggregate welfare of a society's entire population.¹

We do, however, question their implicit assumption that in all countries the best way to pursue aggregate welfare is through antitrust policy that focuses on wealth maximization (or perhaps consumer surplus maximization), and that contemporary U.S. antitrust policy more or less points the way forward. We suspect that some of the political obstacles in the EU to moving toward an American-style antitrust policy that they describe are not simply welfare-reducing

* Associate Professor of Law, University of Minnesota.

** McKnight Presidential Professor of Public Law, University of Minnesota; Sho Sato Professor of Law, University of California at Berkeley.

¹ See Daniel J. Gifford & Robert T. Kudrle, *EU Competition Law and Policy: How Much Latitude for Convergence With the U.S.?*, sections I and II in this issue of *The Antitrust Bulletin*. See also Philippa Watson, *Portfolio Effects in EC Merger Law*, in this issue of *The Antitrust Bulletin*.

collective action problems. Rather, they point to factors that may cause optimal antitrust policy to differ in the two societies. There are a variety of reasons why current EU antitrust policy might be best for increasing aggregate welfare in the EU, given current economic and political conditions there.

EU antitrust policy might be best for increasing aggregate welfare in the EU, while a rather different U.S. antitrust policy might be best for increasing aggregate welfare in the U.S. How could that be? It could happen because antitrust policy has effects that go beyond the product market allocative efficiency effects that traditional antitrust analysis largely focuses on. In this comment we consider four relevant effects of antitrust policy: on political institutions, on corporate governance, on the distribution of income, and on risk-bearing. All of these effects are plausibly quite large. All of these effects look rather different in the EU than in the U.S. After tracing out these various effects, it may turn out that the best antitrust policy for the U.S. is not the best antitrust policy for the EU.²

We now turn to examining the effects of antitrust policy on the four areas just listed. After that, in the conclusion we briefly consider how these effects may affect the prospects for convergence between U.S. and EU antitrust policy.

I. Antitrust rules and institutional governance

Antitrust rules have consequences that go well beyond their effect on producer and consumer surplus created in the product markets on which those rules focus. Different antitrust regimes may have quite different consequences for institutional governance arrangements in the economy and society. In particular, antitrust rules may affect the structure of political institutions and corporate governance institutions. When evaluating different antitrust regimes, we should take into account their effect on these institutions, which may be quite large, possibly even larger than the direct effect on product markets. Moreover, the effects may differ in the U.S. and the EU.

² This point can be stated as an application of the theory of the second best. We return to that characterization in the conclusion.

A. *Political institutions*

Gifford and Kudrle assume that a competition policy focused on wealth maximization will best increase total social welfare. Even if that is right when focusing only on effects in the product market,³ it may prove wrong when we consider more indirect effects. Adding in the effects on political institutions may give some reason to prefer antitrust policy based on what Gifford and Kudrle call rivalry or producer protection,⁴ or even a more simplistic “big is bad” policy.

Consider a simple, basic version of public choice interest group theory.⁵ Various interest groups make demands on the state for policies that advance their interests. Forming an effective interest group is costly. One major problem for interest groups is the free-rider incentive that potential group members face.⁶ Groups that have a small number of potential members, each of whom has a relatively strong stake in problems that the group addresses, will be more likely to overcome the free-rider problem and lobby effectively. Such lobbying, though, is costly to society, both in direct costs incurred in the act of lobbying itself, and more importantly, indirectly via the social costs imposed by the resulting policies, which frequently benefit the interest group, but at a greater cost to the rest of society than what the group gains.

Now, consider two types of structure for an industry. The first consists of many small producers, while the second consists of a much smaller number of larger producers. According to the standard interest group theory, other things being equal producers in the latter group will be better able to organize as an interest group and lobby effectively. Now, think about the choice between a policy of wealth

³ It may not be right if the measure of social welfare includes distributional concerns not captured by wealth maximization. *See* section II(A) *infra*.

⁴ *See* Gifford & Kudrle, *supra* note 1, section I.

⁵ For an overview of public choice theory, *see* DANIEL A. FARBER & PHILIP P. FRICKEY, *LAW AND PUBLIC CHOICE: A CRITICAL INTRODUCTION* (1991).

⁶ *See* MANCUR OLSON, *THE LOGIC OF COLLECTIVE ACTION* (1965).

maximization (in the product market) versus a rivalry policy in a case where the second, more concentrated market structure leads to significant production cost savings. A wealth maximization policy may well dictate allowing such a concentrated structure to occur. A rivalry policy may counsel against allowing such a structure. The rivalry policy will thereby lead to a loss of social surplus generated in the product market. However, suppose that the more concentrated industrial structure leads to more, and more effective, political organizing by the businesses, which results in costly policies favoring the industry at an exorbitant cost to society. If the costs to society from that lobbying outweigh the productive gains from the increased concentration, then the rivalry policy will actually lead to a higher level of social welfare than a wealth maximization policy that only looks to welfare effects in the product market.

Of course, it is not always the case that a small number of larger companies will find it easier to organize politically than a large number of smaller companies. Large groups of small businesses do sometimes manage to unite effectively. Indeed, one popular public choice explanation of the antitrust laws is that they are the result of small businesses organizing to protect themselves against larger, more efficient competitors.⁷ However, interest-group theory does strongly suggest that a smaller number of larger businesses will have a strong advantage in organizing, and that theory has been at least arguably borne out empirically in some, though not all, studies.⁸ How much more effective smaller, more concentrated groups are is of course a tough empirical question, as is how much deadweight loss their effective lobbying imposes on society. We do not assert here that this effect necessarily dominates product market efficiency effects. We more modestly claim that the political effect is a plausible and potentially quite important effect that deserves consideration and study.

⁷ See Thomas J. DiLorenzo, *The Origins of Antitrust: An Interest-Group Perspective*, 5 INT'L REV. L. & ECON. 73 (1985); George Stigler, *The Origin of the Sherman Act*, 14 J. LEGAL STUD. 1 (1985).

⁸ For a discussion of attempts to measure the relationship between industry concentration and political representation, see David M. Host, *Political Representation Among Dominant Firms: Revisiting the "Olsonian Hypothesis,"* paper available at www.ssrn.com.

A second political cost of industrial concentration is that oligopolists and monopolists may be able to use their market position to pressure politicians into granting them favors. For instance, a municipally-run airport that has one major airline that dominates traffic at that airport may find itself in a tough bargaining position when the airline asks for policies favoring it. If the airline can credibly commit to move much of its traffic elsewhere (say, because it has hubs at several other airports as well), while no other airline would be likely to replace that amount of traffic, the airport may feel forced to give in to the airline's demands.

Antitrust analysts have noted the potential political effects of industrial structure before. However, they have tended to treat this as a political argument about antitrust, as distinct from, and even opposed to, the economic considerations that now dominate the field.⁹ In a sense this is correct, insofar as the argument focuses on political institutions rather than the economic markets that are the standard focus of economics. And yet, in another sense our argument is a perfectly straightforward economic one. In this day and age we are quite used to applying economic logic to nonmarket phenomena; indeed, application to political institutions has become a field of its own. Moreover, both general equilibrium theory and welfare economics quite standardly insist on tracing out the effects of a policy throughout the many areas in which it may have notable effects. Thus, the argument about the effect of antitrust policy on political life should not seem at all unusual to anyone familiar with modern economics.

Indeed, this argument brings out a tension that we have long noticed in Chicago-style law and economics. On the one hand, Chicago antitrust has tended to advocate a relatively laissez-faire approach to antitrust, allowing relatively concentrated industries and

⁹ See, e.g., HERBERT HOVENKAMP, *FEDERAL ANTITRUST POLICY: THE LAW OF COMPETITION AND ITS PRACTICE* 50–51 (2d ed. 1999); Robert H. Lande, *Wealth Transfers as the Original and Primary Concern of Antitrust: The Efficiency Interpretation Challenged*, 50 *HASTINGS L.J.* 871, 902–07 (1999); David F. Shores, *Antitrust Decisions and Legislative Intent*, 66 *Mo. L. REV.* 725, 745–56 (2001).

large businesses to develop.¹⁰ On the other hand, Chicago public choice theory analyzes the increased likelihood of political lobbying under such a structure, and the social costs of that lobbying.¹¹ These two points cry out to be brought together in a unified analysis.

Actually, one of the most influential books in economics' invasion of the antitrust field, Richard Posner's *Antitrust Law*, does briefly consider the argument we make here. Posner took the point seriously, but counterargues that while concentrated industries may indeed be better able to manipulate the political process, they may also have less need to do so than less concentrated industries, since they may be more able to achieve the benefits of monopoly through private means.¹² Perhaps, but given the alleged usual strength of market forces to dissipate monopoly in the long run, it would seem that even concentrated industries would want to seek government help in protecting their position. Moreover, they might also use their lobbying power to seek other forms of government subsidy unrelated to maintaining their monopoly power.

Posner also argued that the political argument does not differ sharply from the economic argument against monopoly, and that the policy implications are not much different either.¹³ If concentrated industries only used their political power to buttress their monopoly position, that might be right—then in those cases where concentration increases productive efficiency in the product market, it might indeed be that such businesses would not need to exercise their political power to protect their economic position. Thus, to return to the airport example, if a hub system presents natural advantages, then perhaps we need not worry too much about airlines using their influence over the

¹⁰ See RICHARD A. POSNER, *ANTITRUST LAW: AN ECONOMIC PERSPECTIVE* (1976); ROBERT H. BORK, *THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF* (1978).

¹¹ See Gary Becker, *A Theory of Competition Among Pressure Groups for Political Influence*, 98 Q.J. ECON. 371 (1983); GEORGE STIGLER, *THE CITIZEN AND THE STATE: ESSAYS ON REGULATION* (1975).

¹² See POSNER, *supra* note 10, at 18.

¹³ See *id.* at 19.

airport authority to limit competition in that airport. However, if companies also use their political power to seek other forms of subsidies unrelated to maintaining their monopoly, then even a benign concentration from the product market perspective may have undesirable consequences in the political realm. In the airport example, the dominant airline may be able to use its local influence to get state subsidies to expand the airport even where public benefits do not justify such subsidies. In such instances, policy focused only on efficiency in the product market may differ from policy that takes into account the political effects of economic concentration.

Considering the effect of economic concentration on political institutions is also consistent with a strand of the legislative history of American antitrust law. There has been a long debate over what the legislative history of that law tells us about the law's purpose.¹⁴ Many of those who choose to focus on product market efficiency have been sympathetic to Robert Bork's argument that advancing consumer welfare and efficiency was the law's purpose.¹⁵ However, others have considered the same history and seen instead a variety of other goals as well: redistributing income from producers to consumers,¹⁶ protecting small business for their cultural and ethical value, and an inherent populist distrust of bigness, as well as concern about the effect of big business and concentrated industries on democratic institutions.¹⁷

We cannot here enter into that debate over legislative history. However, we note that we do find the concern with preserving democratic institutions a highly plausible goal of the antitrust laws. The antitrust laws developed in the context of the Progressive political

¹⁴ See HOVENKAMP, *supra* note 9, at 47–51; David McGowan, *Innovation, Uncertainty, and Stability in Antitrust Law*, 16 BERKELEY TECH. L.J. 729, 741–65 (2001).

¹⁵ See Robert H. Bork, *Legislative Intent and the Policy of the Sherman Act*, 9 J.L. & ECON. 7 (1966).

¹⁶ See Lande, *supra* note 9.

¹⁷ See HOVENKAMP, *supra* note 9, at 47–51; McGowan, *supra* note 14, at 741–65.

movement at the turn of the century—for instance, the two great Progressive presidents, Theodore Roosevelt and Woodrow Wilson, were noted trustbusters. One major concern of that movement was the effect that the new large national businesses were having on American politics. It would be highly surprising if the antitrust laws, which were meant to help limit the economic power of those businesses, were not understood as helping to limit their political power as well.

Finally, how is this point relevant to Gifford and Kudrle's comparison of U.S. and EU antitrust policy? One possible, though highly debatable, implication is that the Europeans actually have a more desirable policy. If in the U.S. as well as Europe the political effects of economic concentration are typically strong enough to swamp the product market effects, then a policy of rivalry or producer protection may promote economy-wide efficiency better than a policy of maximizing consumer or total surplus in the product market.

Perhaps more interestingly, it might be that the EU policy makes more sense for the EU, while the American policy makes more sense for the U.S. Why might that be? It could be true if Europe faced more serious consequences from enhanced political organizing power in concentrated industries than the U.S. does. In turn, why might that be? One possibility is cultural sensitivity. The domination of European markets and polity by a smallish number of large companies may be objectionable insofar as those companies come mostly from one or a few countries. Other countries may resent the resulting concentration of power.¹⁸

A second possibility is that European-wide political institutions may be more vulnerable to interest group capture than American political institutions. The EU has a relatively stronger executive branch, the European Commission, a relatively weaker legislative branch, and probably a weaker judicial branch than the American

¹⁸ Of course, interstate cultural sensitivity exists in the U.S. too, but nowadays is probably less strong than between nations of the EU. Also, to the extent that the shareholders and employees of companies in the EU become truly transnational, such concerns will presumably fade. The EU is meant to move us toward that situation, but we are not there yet for most corporations.

federal government.¹⁹ There has been much complaint about the resulting lack of transparency of European institutions. That lack of transparency may make the European institutions even more vulnerable to capture by business groups than American institutions. Indeed, at least some observers of European politics seem to believe this is so.²⁰

If it is, then well-organized groups could do more damage in Europe than in the U.S. European political institutions may do less to impede interest groups than American political institutions. If the costs derived from interest group organization are greater in Europe than the U.S., then those costs may be more important in the European calculus of the effects of antitrust policy than they are in the U.S. If so, then efficient competition policy may correctly give more weight to promoting rivalry or protecting producers in the EU than it does in the U.S.

Gifford and Kudrle themselves note that political considerations help explain why the EU has not fully adopted a wealth maximization goal in its antitrust policy.²¹ In part, we are simply elaborating on this point. But we do so with a slightly different normative twist. Gifford and Kudrle seem to find it regrettable that politics prevent the EU from pursuing an optimal policy. We instead suggest that the EU antitrust policy may indeed be optimal within the context of EU institutions. Or at least more weakly, we suggest that the political effects of antitrust policy may weigh more heavily against a purely efficiency-based antitrust policy in the EU than in the U.S.

B. Corporate governance

The effect of antitrust policy on corporate governance institutions is another issue that has received less attention than it deserves. One of the major uses of antitrust policy may be to promote better corporate governance. In this area, too, there may be a significant difference in calculating the relative benefits and costs for different antitrust policies

¹⁹ See J.H.H. WEILER, *THE CONSTITUTION OF EUROPE: "DO THE NEW CLOTHES HAVE AN EMPEROR?" AND OTHER ESSAYS ON EUROPEAN INTEGRATION* 266 (1999).

²⁰ See *id.* at 266–68.

²¹ See Gifford & Kudrle, *supra* note 1, section V (B).

in the U.S. as compared with the EU. The exact nature of that difference, however, is ambiguous. That ambiguity stems from uncertainty both as to the exact relationship between product market competition and corporate governance, and as to the effect of the different antitrust policy goals identified by Gifford and Kudrle on product market competition in the sense relevant to corporate governance.

Large corporations face some serious agency problems. Their directors and top managers are given much authority to make most major corporate decisions, creating a temptation for them to use that authority to benefit themselves rather than shareholders. Systems of corporate governance provide a variety of methods for controlling those agency problems. One is hostile takeovers, and the threat thereof.²² A second method for controlling managers is equity-based compensation.²³ A third important method is managerial labor markets.²⁴

Product market competition is another, independent means of controlling managerial behavior.²⁵ If managers are running a business poorly, resulting in high costs and prices or poor quality output, then in a competitive market they will lose market share quickly. Too

²² If incumbent managers of a company are running it poorly, its market value will tend to fall well below what it would be worth if it were well run. This creates the potential for large profit were someone to take over the company, kick out (or better discipline) the incumbent managers, and run the company better. Successful takeovers thus reduce the agency problem, and the mere threat of a hostile takeover helps induce incumbent managers to do a better job. *See* PAUL MILGROM & JOHN ROBERTS, *ECONOMICS, ORGANIZATION & MANAGEMENT* 508–19 (1992).

²³ If much of managers' compensation is tied to the value of their company's equity, then managers have a strong incentive to increase the value of that equity, thereby better aligning their objective with those of shareholders. *See id.* at 423–45.

²⁴ Managers who do a good job should develop good reputations, and as a result have better chances at getting attractive jobs either higher within their own companies or at other companies. *See* Eugene F. Fama, *Agency Problems and the Theory of the Firm*, 88 J. POL. ECON. 288 (1980).

²⁵ *See* Oliver D. Hart, *The Market Mechanism as an Incentive Scheme*, 14 BELL J. ECON. 366 (1983); Stephen J. Nickell, *Competition and Corporate Performance*, 104 J. POL. ECON. 724 (1996).

drastic a drop in market share eventually leads to bankruptcy, and the loss of jobs for managers. In contrast, a company that has little product market competition will be able to remain profitable for a much longer time even if it is providing low quality goods or services at a high price. Competition between companies can both provide information as to which one is doing a good job, and can also give incentives to managers to do a better job.²⁶ For some time economists have suspected a link between product market competitiveness and the technical efficiency or degree of slackness within companies.²⁷ Harvey Leibenstein described this link in his work on X-efficiency, and suggested that the effect of competition on X-efficiency could be much stronger and more important than the traditional link between competition and allocative efficiency.²⁸ There have been a few attempts to formally analyze the effect of competition on corporate governance.²⁹ There have also been some efforts to measure the effect empirically.³⁰ Neither the theoretical nor the empirical work is lacking in ambiguity, but overall they do suggest that competition may induce companies to organize production more efficiently.

We suspect this is one of the most important methods of disciplining managers. It operates with a lag, and allows room for a fair degree of slack, but ultimately provides a strong incentive to managers to keep their business from being too poorly run. All of the other mechanisms described above have limitations that are at least as great as product market competition. Antitakeover defenses have made hostile takeovers much less effective than they were in the 1980s. Many observers think that high levels of equity-based compensation are more a sign of uncontrolled agents run amuck than a way of controlling those agents. Labor markets have quite imperfect

²⁶ See JOSEPH E. STIGLITZ, *WHITHER SOCIALISM?* 112 (1994).

²⁷ See Nickell, *supra* note 25, for a review.

²⁸ See Harvey Leibenstein, *Allocative Efficiency vs. "X-Efficiency"*, 56 AM. ECON. REV. 392 (1966).

²⁹ See Hart, *supra* note 25; David Scharfstein, *Product-market Competition and Managerial Slack*, 19 RAND J. ECON. 147 (1988).

³⁰ See, e.g., Nickell, *supra* note 25; RICHARD E. CAVES ET AL., *INDUSTRIAL EFFICIENCY IN SIX NATIONS* (1992).

information as to the effectiveness of individual managers, and poor managing may become apparent only with a long lag.

Product market competition is not only important on its own as a disciplinary mechanism. It also complements the other methods mentioned above. Poor managerial performance can become apparent to outsiders much more quickly in a company that faces strong product market competition than in one that does not. Monopolists may remain profitable and thus appear successful to outsiders even if they are quite poorly run. If outsiders detect poor performance more quickly in companies subject to competition, then, among other things, poor performance will show up more quickly in a lower stock price. That in turn both makes the company more vulnerable to hostile takeover and also directly hurts managers who have much of their compensation tied to the value of company stock. The quicker and greater visibility of poor performance for competitive companies should also show up in how effectively labor markets can evaluate the performance of managers. Thus, product market competition is a vital part of corporate governance, both directly and indirectly. To date there has been little empirical study of possible complementarities between product market competition and other aspects of corporate governance, although one recent study of Polish companies does provide some suggestive evidence in favor of such complementarity.³¹

These points as to the role of product market competition in corporate governance apply more strongly to the U.S. than to the EU, though. The continental European system of corporate governance (the U.K. excepted) looks quite different from the American system. Even most large public corporations in Europe have a large shareholder (individual, family, or institutional, often a bank) that effectively controls the company.³² Such large shareholders may have a much stronger incentive to monitor the performance of company

³¹ See Irena Grosfeld & Thierry Tresselt, *Competition and Corporate Governance: Substitutes or Complements? Evidence from the Warsaw Stock Exchange*, paper available at www.ssrn.com. See section 2.3 of that paper for other work on the topic.

³² See Rafael La Porta et al., *Corporate Ownership Around the World*, 54 J. FIN. 471 (1999).

management than do dispersed American shareholders,³³ arguably improving monitoring in Europe as opposed to the U.S. On the other hand, the other mechanisms mentioned above are typically less strong.³⁴ That tends to weaken European corporate governance vis-à-vis the U.S. It is heavily debated whether one can sensibly say whether either system of corporate governance does a better job, and if so, which one.³⁵

As a result of these various differences, it is uncertain whether product market competition is a more important limit on agency costs in the U.S. or continental Europe. On the one hand, if concentrated shareholding succeeds in solving the managerial agency problem better in Europe than the American market-based mechanisms, then product market competition as a limit on managers would seem less important in Europe than in the U.S.³⁶ On the other hand, if other disciplinary mechanisms limit managers better in the U.S. than in

³³ See Andrei Shleifer & Robert Vishny, *Large Shareholders and Corporate Control*, 94 J. POL. ECON. 461 (1986).

³⁴ The concentration of shareholding, among other factors, makes hostile takeovers much less common. See Julian Franks & Colin Mayer, *Bank Control, Takeovers, and Corporate Governance in Germany*, in COMPARATIVE CORPORATE GOVERNANCE: THE STATE OF THE ART AND EMERGING RESEARCH 641, 642 (Klaus J. Hopt et al. eds., 1999). European managers typically receive much less compensation based on company stock, although there is something of a trend toward the American system of compensation. See Brian Cheffins & Randall Thomas, *The Globalization (Americanization) of Executive Pay: Yes, No or Not Yet?*, working paper. External managerial labor markets are less active in Europe than in the U.S.

³⁵ For an overview of the debate, see Brett H. McDonnell, *Convergence in Corporate Governance—Possible, But Not Desirable*, 47 VILL. L. REV. 341 (2002).

³⁶ Mark Roe suggests that causality may work in the opposite way as well. Greater shareholder concentration may have developed in Europe in reaction to greater product market concentration. The greater slack created by decreased competition creates a need for shareholders to oversee managers more closely, and concentrated shareholding is a way of achieving greater oversight. See Mark J. Roe, *Rents and Their Corporate Consequences*, 53 STAN. L. REV. 1463 (2001).

Europe, then product market competition could be even more important in Europe as a limit on agency costs. That is not necessarily right, though. Even if the agency problem remains as or more serious in Europe than in the U.S., the deemphasis on the other mechanisms (takeovers, equity compensation, labor market) that product market competition complements could make such competition less important to corporate governance in Europe than in the U.S. All in all, it would appear that vigorous product market competition is more central to the American system of corporate governance than to the European system, though this is not free from doubt. That is not to say that product market competition is of no importance in Europe, just that it is probably less important. At this point, we simply posit this as a possibility, though one that strikes us as fairly likely.³⁷

Consider next the consequences of product market competition's effects on corporate governance for the choice of competition policy goals. Here we have another source of uncertainty. The relative value of the four policy goals identified by Gifford and Kudrle (rivalry,

³⁷ We are aware of little systematic empirical estimation of the relative effect of competition on corporate governance in the U.S. and the EU. We note a few bits of evidence. A study of technical efficiency in six countries found that the optimal level of product market concentration (optimal in the sense of leading to the greatest technical efficiency) was higher in Japan and South Korea, which both tend to resemble Europe in corporate governance more than the U.S., than it was in the United States, Australia, Canada, and the U.K., all of whom resemble the U.S. more than continental Europe in corporate governance. See CAVES ET AL., *supra* note 30, at 12. Also, a recent study of German industries finds little evidence of an effect of product market competition on productivity. See Silke Januszewski et al., *Product Market Competition, Corporate Governance, and Firm Performance: An Empirical Analysis of Germany*, working paper (2001).

It is true that even though concentrated shareholding may reduce agency problems in Europe relative to the U.S., such shareholding does open up a new set of problems. Minority shareholders of European companies may well be subject to significant self-dealing by controlling shareholders. This problem may well make the European system of corporate governance more problematic than the American system. However, it does not appear that product market competition is of much help in solving that particular governance problem.

producer protection, consumer surplus maximization, and wealth maximization) for promoting competition in the sense relevant to corporate governance is not clear. The relevant sense of competition here is as follows: competition is strong if firms that slack off are quickly punished as customers move to rival firms. What sort of antitrust policy best promotes such competition? The producer protection goal looks clearly worst from this perspective. Producer protection helps cushion less efficient companies from competition from more efficient rivals. The effect of such a policy on corporate governance is potentially catastrophic. Product market competition aids corporate governance precisely by threatening the welfare of companies and their managers if the companies do not perform as well as their rivals. Cushioning companies from efficient rivals therefore could very badly hurt the entire system of disciplining corporate managers. This corporate governance effect of competition policy may well be of at least the same order of magnitude in importance as the allocative efficiency effects more typically stressed in analysis of antitrust laws.

The rivalry goal presents a puzzle, though. On some interpretations, rivalry can be understood as fostering competitive pressure on companies and their managers. Indeed, one commentator has recently advocated a return to rivalry as a goal precisely as a way to encourage technical efficiency.³⁸ Others understand rivalry somewhat differently. Gifford and Kudrle tend to see rivalry and producer protection as similar.³⁹ However, they do note that some have attempted to revive rivalry as a prod to productivity.⁴⁰ An advocate of rivalry distinguishes between injury to rivalry and injury to rivals.⁴¹ Only the latter equates with producer protection. However,

³⁸ See Harry S. Gerla, *Restoring Rivalry as a Central Concept in Antitrust Law*, 75 NEB. L. REV. 209 (1996).

³⁹ See Gifford & Kudrle, *supra* note 1, section I.

⁴⁰ See *id.* (citing M. Porter, *Competition and Antitrust: Toward a Productivity-Based Approach to Evaluating Mergers and Joint Ventures*, 46 ANTITRUST BULL. 919 (2001)).

⁴¹ See Gerla, *supra* note 38, at 249–51.

the distinction may be hard for courts to maintain in practice. Whether fostering rivalry need degenerate into producer protection becomes an important question if we are right about the strength of the corporate governance effects of antitrust policy.

It appears, though with some uncertainty, that product market competition is less central to the European system of corporate governance than to the American system. Thus, the antitrust policy goal of producer protection (and rivalry too, if it does tend to degenerate into producer protection) is likely to cause less harm for European corporate governance than for American corporate governance. That is not to say that those goals would cause no harm for European corporate governance. Product market competition is still of use in Europe as a way to discipline managers. But the effect is probably weaker than in the U.S.

To summarize our argument: Product market competition has a strong effect on corporate governance, and thus on how efficiently companies are run. That effect is rather different in the EU than in the U.S. because of the different systems of corporate governance. Most likely, product market competition is a less important limit on managerial misbehavior in the EU than in the U.S., although there is some doubt on this point. There is also doubt as to the relative effectiveness of different forms of antitrust policy in promoting competition in the sense relevant to corporate governance, although producer protection clearly looks harmful. We thus cannot say with assurance how these differences may affect the optimal choice of antitrust policy in the EU as opposed to the U.S.

We can make these two points with some confidence, though. First, the effects discussed in this section are potentially important, quite plausibly of at least the same order of magnitude as the direct allocative efficiency effects antitrust analysts usually focus on. Second, the effects of antitrust policy on corporate governance are different in the U.S. and the EU, and the difference may well be significant. Thus, in calculating the overall costs and benefits of different choices of antitrust policy in the U.S. and the EU, the calculations for corporate governance effects will look different. We make the same caveat here as with our other arguments: we have not

demonstrated that all things considered one policy (say wealth maximization) will turn out to be optimal for the U.S. and another policy (say producer protection) will be optimal for the EU. In the end, the same policy could be optimal for both. But the calculations will look different for the U.S. and the EU.⁴²

II. Antitrust policy and welfare economics

The goal of wealth maximization has certainly not lacked for discussion among U.S. antitrust scholars. But, perhaps because economic analysis achieved prominence earlier in antitrust law than elsewhere, the antitrust discussion has seemed inattentive to the broader scholarly debate about economic efficiency and its role in law. In this section, we explore two of the most powerful arguments in favor of basing legal rules exclusively on economic efficiency. We are not interested in critiquing these arguments here. Rather, we will show that these arguments have reduced force in the context of European competition law than in American antitrust. Correspondingly, the argument for considering nonefficiency (“fairness”) factors is stronger in the European context.

A. Efficient legal rules and optimal taxation

The dominant view among U.S. antitrust scholars seems to be that antitrust law should focus on maximizing efficiency, without any concern about whether the resulting gains in society’s wealth are shared with consumers or about the impact on small producers. One reason to question this approach is that consumers and small producers may be poorer than the owners of large firms, so that an efficient antitrust rule might have adverse distributional effects. The question, then, is whether antitrust should be based purely on wealth

⁴² There is one important exception to that statement: the U.K. The British system of corporate governance resembles the American system more than it resembles that of continental Europe. Thus, a producer protection policy is likely to be more harmful in the U.K. than on the continent. We might expect, therefore, that the British are likely to be at odds with the rest of the EU in their preferred antitrust policy.

maximization, with no attention to distribution. A more general question goes beyond the field of antitrust: Should legal regulations incorporate distributional concerns or should they leave those concerns to the tax system? A substantial body of scholarship now exists about this broader question, though it does not yet seem to have had much impact on antitrust scholars. As we will see, there are some strong arguments why legal rules (including antitrust rules) should focus more on efficiency than on distribution. But these arguments apply less fully to the European Union than to the United States.

Recent debates about the relevance of distributional goals have centered on what has been called the double-distortion argument. This argument holds that, as a general matter, the tax system is a more efficient way of engaging in redistribution than the regulatory system. Although the full argument is technical and complex, the basic rationale is straightforward. Suppose we readjust some economically efficient legal rule so that the new rule redistributes income from the rich to the poor. Since we have moved away from the efficient rule, there is necessarily a direct efficiency cost to the change. But the rule change will also cause a second, less obvious, economic distortion. Just as someone considering an additional hour of work might be deterred by an increase in the marginal tax rate, so they might be deterred by knowing that they are making themselves targets for disadvantageous legal rules. Thus, besides the direct efficiency cost of the redistributive rule, it also has the same efficiency cost (by way of distorting the labor supply) as the income tax. Hence, we can always transfer the same amount of funds more efficiently just by raising the tax rate on the rich while using an efficient legal rule.⁴³

This conclusion is not ironclad, as its originators themselves admit.⁴⁴ For instance, if what we are trying to equalize is not income itself, but rather some quantity that correlates with income, legal rules

⁴³ The theory is summarized in Louis Kaplow & Steven Shavell, *Should Legal Rules Favor the Poor? Clarifying the Role of Legal Rules and the Income Tax in Redistributing Income*, 29 J. LEGAL STUD. 821 (2000).

⁴⁴ See *id.* at 827–32.

might add to the efficiency of redistribution.⁴⁵ For present purposes, however, we can put to one side this and other somewhat subtle objections. If the double-distortion argument does hold, then antitrust (like other legal regulations) should ideally concentrate on efficiency and leave redistribution to the tax system. We can fully accomplish this separation of functions, however, only if the tax system is capable of handling society's redistributive program. This may be less true at the European level than in the United States, given the EU's more restricted fiscal instruments.

In general, European countries (at least in Northern Europe) are more concerned about income inequality than the United States.⁴⁶ Moreover, at least some of those countries have high tax rates, which would presumably be capable of handling the wealth effects of an antitrust rule within any single European country. But EU members differ greatly in their levels of wealth, a disparity that will only increase with the projected expansion of the EU to the east. Moreover, powerful firms are not randomly distributed across Europe, nor are their financial backers. Thus, producer surplus is likely to accrue primarily to the most powerful and wealthy EU members, increasing existing wealth disparities at the margins. Assuming that Europeans care about the distribution of wealth across Europe rather than merely within individual countries, efficient rules—rules that focus on total surplus with no attention to the division between producers and consumers—will tend to pump wealth in the “wrong” direction.

The double-distortion argument teaches us that the best response to this effect would be to use the tax system to redistribute the wealth back where it “belongs.” The problem is that the EU does not possess the necessary fiscal instruments. Although the EU's revenue sources and

⁴⁵ For more complete explanations of this point, and of other qualifications to the double-distortion argument, see Chris Sanchirico, *Taxes Versus Legal Rules as Instruments for Equity: A More Equitable View*, 29 J. LEGAL STUD. 797 (2000); Daniel A. Farber, *What (If Anything) Can Economics Teach Us About Equity?*, MICH. L. REV. (forthcoming).

⁴⁶ For documentation of this difference and a theory about its cause, see Alberto Alesina & George-Marios Angeletos, *Fairness and Redistribution: U.S. versus Europe*, http://papers.ssrn.com/abstract_id=346545.

expenditures both demonstrate concern about wealth disparities among member states, its budget is far too small to have a significant impact.

The difference in financial scale between the European Union and the United States government is striking. The EU budget is capped slightly below 1.5% of total European gross national product (GNP).⁴⁷ In contrast, the current U.S. government budget is approximately 20% of gross domestic product (GDP).⁴⁸ In monetary terms, the U.S. government's budget is approximately \$2 trillion.⁴⁹ The comparable figure for the EU is around 100 billion euros, but nearly half of this amount goes for agricultural support.⁵⁰ Of the total budget, only about a third is available for the three funds designed to decrease economic disparities in welfare between member states.⁵¹

Unlike the U.S., the EU also is constrained in its sources of revenue. It is limited to four sources: customs duties, export charges on food, a small share (under one percent) of member state's value-added taxes (VAT), and a charge on member states based on their GNP.⁵² Of these, only the last (the so-called fourth resource) is designed to provide any redistribution between member states, but it amounts to under half of total revenue.⁵³ Thus, under half of the EU's revenues and taxes are designed with an eye to cross-national distributional concerns, and its capacity to address this issue is minuscule in terms of the overall European economy. Unlike the United States, Europe cannot rely purely on fiscal instruments to deal

⁴⁷ See JO SHAW, *LAW OF THE EUROPEAN UNION* 163 (1996).

⁴⁸ See OFFICE OF MANAGEMENT AND BUDGET (OMB), *A BIRD'S EYE VIEW OF THE BUDGET*, available at www.whitehouse/omb/budget/fy20003/cguide.pdf. For present purposes, the difference between GDP and GNP is too small to affect the comparison.

⁴⁹ See *id.*

⁵⁰ See Table A: Financial Perspective EU-15, ewww.europa.eu.int/comm/budget/pdf/financialfruk/perspectfin/tbl20002006eur15-en.pdg.

⁵¹ See *id.* for precise figures.

⁵² See SHAW, *supra* note 47, at 164.

⁵³ See EUROPEAN UNION, 2001 AND 2002 BUDGETS: BREAKDOWN BY TYPE OF REVENUE, available at europa.eu.int/comm/budget/pubfin/data/x-en23.pdf.

with large disparities in wealth across its domain. Thus, there is a stronger argument for modifying regulatory policies (including antitrust) to take account of these distributional issues.

In addition to the problem of adverse distributional effects within the EU, efficient antitrust rules may well move wealth from European consumers to foreign producers. The EU lacks any obvious mechanism for taxing foreign shareholders so as to redistribute their wealth to less affluent European consumers. A corporate income tax on the European activities of foreign corporations might serve this function, but the EU does not have the authority to impose such a tax.

Thus, if distributive concerns extend beyond the borders of member states, the EU may lack the ability to pursue those concerns through the tax system. This undermines the argument that taxation is a better mechanism to pursue redistribution than legal regulation. By itself, this argument does not prove that introducing distributive concerns into EU competition law is warranted. The efficiency effects may still outweigh the distributional benefits. But what we can say with assurance is this: Comparatively speaking, the argument for purely efficiency-based, distribution-blind rules is weaker in the EU than in the United States, where much more powerful fiscal instruments are available. Consequently, of the four goals listed by Gifford and Kudrle, wealth maximization should count for less in the European context and consumer surplus should have greater weight.

B. Efficient legal rules and risk aversion

Even putting aside any concern about the overall distribution of wealth, economic efficiency has long been a controversial legal goal. Particularly in the early days of the law-and-economics movement, scholars devoted considerable attention to the legitimacy of efficiency as a social value. The most vocal defendant of economic efficiency at that time was Richard Posner. On the other side of the debate were arrayed such legal notables as Guido Calabresi, Jules Coleman, and Ronald Dworkin.⁵⁴

⁵⁴ For an excellent overview of the debate, see NEIL DUXBURY, *PATTERNS OF AMERICAN JURISPRUDENCE* 397–406 (1995). For critiques of efficiency as a social value, see Jane B. Baron & Jeffrey L. Dunoff, *Against Market Rationality: Moral Critiques of Economic Analysis in*

Posner's fullest discussion of the subject is found in a 1980 article, written after he had already exchanged initial shots with some of his critics. The crux of the argument is as follows. Because there is no way of determining whether individuals actually consent to legal rules, the best we can do is to look for implied consent. One way of doing this is to ask whether, if transaction costs were zero, the parties would have agreed to the legal rule in advance. This procedure, he says, "resembles a judge's imputing the intent of parties to a contract that fails to provide expressly for some contingency."⁵⁵ Thus, he says, "an institution predicated on wealth maximization may be justifiable by reference to the consent of those affected by it even though the institution authorizes certain takings, such as the taking of life, health, or property of an individual injured in an accident in which neither party is negligent, without requiring compensation *ex post*."⁵⁶

As adapted to the antitrust context, the argument would run as follows. In any given case, efficiency-based antitrust rules may favor some individuals and hurt others. For example, efficient rules may lower prices to the benefit of consumers and businesses that purchase the goods in question. Efficient rules will also hurt some individuals, most often producers who are put out of business by more efficient firms, sometimes consumers who pay higher prices while efficiency gains flow to dominant firms. On balance, however, the net gains outweigh the losses (otherwise, the rule would not be efficient). A rational citizen, lacking any specific knowledge about his or her own economic situation, would agree in advance to efficient rules because such efficient rules would *on average* give him or her the highest economic welfare.

One key part of this argument is that individuals want to maximize average gain and do not care independently about the risk

Legal Theory, 17 CARDOZO L. REV. 431 (1996); Anthony T. Kronman, *Wealth Maximization as a Normative Principle*, 9 J. LEGAL STUD. 227 (1980).

⁵⁵ Richard A. Posner, *The Ethical and Political Basis of the Efficiency Norm in Common Law Adjudication*, 8 HOFSTRA L. REV. 487, 492-93 (1980).

⁵⁶ *Id.*

of losing, so long as it is balanced by at least an equal prospect of gain. Economic efficiency guarantees that on average citizens will experience a gain, but does not speak to the accompanying level of risk. Some individuals may well end up in a worse position in any specific case than they would otherwise, although on average the rule results in improved welfare for the population as a whole. But if individuals are risk averse, they may be unwilling to take the risk of losing even if on average they can expect to be better off under the efficient rule. More precisely, risk-averse individuals might not agree *ex ante* to an efficient antitrust policy because the average net gain is not enough to compensate them for the increase in risk-bearing.

It is easy to see how risk aversion might be implicated by antitrust law. Imagine an economy containing a million people. Now assume that an efficient antitrust policy will reduce consumer prices, thereby saving the average consumer \$10 per year (or a total \$10 million). The efficient policy will, however, put a hundred small firms out of business every year, at a loss of \$70,000 per owner (a total of \$7 million). The net gain averages out at \$3 per person. Posner's argument, then, is that if you did not know in advance whether you would be a winner or a loser, you would accept this gamble, since you can expect on average to gain \$3 from the efficient law. But you might not agree to this gamble from the *ex ante* position of someone who does not know how the rule will affect him or her. If you are risk averse, you might very well be willing to pay \$10 per year extra as a consumer, in order to avoid the risk of 1 in 10,000 chance of suffering a \$70,000 loss as a producer. More generally, the social gains from an efficient antitrust law mostly take the form of small, broadly distributed price decreases, while the social costs fall heavily on small groups of impacted firms and workers. If individuals are risk averse, they might be willing to pass up some of the diffuse individual benefits of unrestrained competition in return for greater economic security.

Risk aversion is not always a factor, however. In some situations, individuals may have eliminated risk through diversifying their investment portfolios, or insurance may be available without any significant distortion in incentives. Or perhaps the amount at stake is too small for risk aversion to play a significant role. In any event,

Posner's argument for the legitimacy of efficiency will not work unless risk aversion can be eliminated as a significant factor.

For several reasons, risk aversion may be more important in assessing European competition policy than American antitrust law. First, in a more rigid economy, the real economic losses from firm closures and unemployment may be greater. Second, loss-spreading mechanisms may be weaker. And third, Europeans may be more risk averse. We consider these points in turn.

The first point relates to the consequences of economic rigidity. Europeans have long stressed economic stability more than Americans do, with higher levels of job security for those who do have jobs (though higher unemployment for others).⁵⁷ The difference has been connected with the greater flexibility of the U.S. labor market.⁵⁸ As Gifford and Kudrle themselves point out, "[i]n sharp contrast with the U.S., most major political forces in each of the constituent states . . . place stability of production and employment ahead of efficiency and growth."⁵⁹ Thus, the general policy balance seems different in Europe.

⁵⁷ Unemployment in Europe has averaged 150% of the United States. See Jim Chen, *Rejoinder: "Globalization and Its Losers": Epiphytic Economics and the Politics of Place*, 10 MINN. J. GLOBAL TRADE 1, 30–31 (2001). Moreover, spells of unemployment are also much longer in Europe. See *id.* at 31. Similar statistics are presented in Joel Handler, *Questions About Social Europe by an American Observer*, 18 WIS. INT'L L.J. 437, 437–38 (2000) (European levels of unemployment are "far higher" than the U.S., and Europe suffers "increasing long-term of permanent unemployment."); *id.* at 451–52 (providing detailed statistics). These differences in labor policy and markets may themselves be in part the consequences of less competitive product markets. See Roe, *supra* note 36, at 1490–91.

⁵⁸ See Philip Harvey, *An Analysis of the Principal Strategies That Have Influenced the Development of American Employment and Social Welfare During the Twentieth Century*, 21 BERKELEY J. EMPLOYMENT & LABOR L. 677, 716 (2000).

⁵⁹ Gifford & Kudrle, *supra* note 1, section V(B). See also Handler, *supra* note 57, at 449 (political consensus on "secure jobs, backed by state guarantees of full employment").

For example, almost all European countries have statutes that limit employee discharges.⁶⁰ The standards vary: the French require the employer to have a justification that is “genuine and serious”; the Germans require reasons connected with the person or his conduct or “urgent social needs”; even the comparatively laissez-faire British require a good faith belief in the existence of a sufficient reason for discharge.⁶¹ In contrast, the general rule in the United States is that the employer needs no justification at all to discharge an employee, so long as the motive for the discharge does not rest on some forbidden basis such as race.

Policy differences of this kind lead to adjustments in economic behavior. Because employees can expect a longer-term relationship with a firm, their incentives and conduct during the employment relationship are also different. The existence of more secure employment relationships makes it rational for employees to invest more in “firm-specific capital”—skills and knowledge useful in a particular firm but not readily transferrable. As Jim Chen explains, the “longer human beings work in one setting and with a single set of tools or skills, the more ‘specific’ they become to that niche.”⁶² So, we would predict that European workers have a higher investment in firm-specific skills and knowledge.

In turn, this behavior increases the losses accompanying firm closures or unemployment. This firm-specific capital becomes worthless if the employee loses his job, but no insurance policy can cover such a loss. Moreover, because of higher European

⁶⁰ See Stephen Befort, *Labor Law and Employment Law at the Millennium: A Historical Review and Critical Assessment*, 43 B.C. L. REV. 351, 405 (2002).

⁶¹ *Id.* at 405 (“The United States stands virtually alone among industrialized nations in failing to provide general statutory protection against unjust dismissals.”). Exceptions to the at-will rule are discussed in *id.* at 378–83.

⁶² Jim Chen, *Globalization and Its Losers*, 9 MINN. J. GLOBAL TRADE 1157, 1165 (2000). See also McDonnell, *supra* note 35, at 358 (instability due to threat of takeover would reduce investment in human capital).

unemployment, the laid-off European worker is likely to face a longer spell of unemployment, another loss that cannot readily be covered by insurance.⁶³

Similarly, because of the general European stress on economic stability and because of local regulations protecting small producers in the past, producers have also been encouraged to make larger investments in existing firms, both in financial and human capital. The switch to an efficient antitrust policy may increase the number of small-firm failures, resulting in the loss of this capital to the owners. These losses may be all the greater because lower competition in product markets encourages owners and workers to make greater investments in firms. European law seems quite sensitive to this potential loss. Gifford and Kudrle observe that European antitrust policy “protects established distribution firms from unwelcome shocks.”⁶⁴ Risk aversion may help explain this protective attitude toward existing firms. Investments by the owners of small firms are difficult to diversify; the owner’s resources are tied up in his own firm rather than being diversified through a large shareholder portfolio. Additionally, because European corporate finance relies more heavily on bank loans than the U.S. system, and correspondingly less on publicly traded securities, portfolio diversification is generally more difficult for investors. Lenders, too, may be inadequately diversified because their loans are restricted to particular geographic areas or to firms with which they have long-term ties.⁶⁵

The upshot is that the risk of a business failure or job loss may be not only larger, but also less easily diversified in Europe than in the United States. This means that risk aversion is more relevant to assessing the validity of economic efficiency as the exclusive goal of competition law. Because Europeans have more to lose when small producers are forced out of the market, and less ability to insure

⁶³ This risk can be reduced by generous unemployment benefits, but these are unlikely to cover the full loss.

⁶⁴ Gifford & Kudrle, *supra* note 1, section V(B).

⁶⁵ For further discussion of these corporate governance issues, see section I(B) *supra*.

against their losses, they may be willing to give up a certain degree of economic efficiency in order to obtain protection against such risks.

Finally, the greater stress on stability in European social policy may be an indication that on average Europeans are simply more risk averse than Americans. Immigration is a high risk activity, so those Europeans who moved to America may have been more risk-accepting than those who stayed behind, shifting the two cultures in opposite directions. In addition, in the past century, Europeans have had tragic experience with the worst cases of instability, in the form of two World Wars on their own soil, political upheaval, and the economic traumas of depression and hyperinflation in parts of the continent. It would not be surprising if these experiences left a mark on European cultural values.

Again, we do not argue that risk aversion justifies the EU's current competition policies. Our claim is comparative. We merely contend that risk aversion would probably justify less emphasis on increasing total surplus in EU competition law as compared with the United States. In particular, risk aversion might lead a rational European regulator to place some weight on producer protection as an antitrust goal.

III. Conclusion

We have identified four ways in which antitrust policy may affect aggregate welfare beyond its effect on allocative efficiency in the product market. An adequate analysis of antitrust policy must thus trace out the effects of that policy on political institutions, corporate governance, distribution, and risk bearing. Differences in political structures, capital markets, and labor markets may mean those effects differ in the U.S. and the EU.

This can be restated as an application of the theory of the second best.⁶⁶ An antitrust policy aiming to maximize wealth created in the

⁶⁶ See Richard S. Markovits, *Second-Best Theory and Law & Economics: An Introduction*, 73 CHI.-KENT L. REV. 3 (1998); Richard S. Markovits, *Second-Best Theory and the Standard Analysis of Monopoly Rent Seeking: A Generalizable Critique, a "Sociological" Account, and Some Illustrative Stories*, 78 IOWA L. REV. 327 (1993).

product market might be the policy one would follow in a world where all other parts of the economy functioned without problems. However, neither the U.S. nor the EU comes close to being such a world. In the real world, many other sorts of imperfections exist in many other areas. Moreover, the nature of those imperfections differs in the U.S. and the EU. Calculation of the best policy for the U.S. and for the EU must take those differing imperfections into account.

One common response to such second-best arguments is that such effects are theoretically possible, but empirically small. Sometimes that is right. This is not one of those times. Each of the effects we have identified is very probably of at least the same order of magnitude as the sort of deadweight losses typically analyzed in antitrust economic analysis.⁶⁷ Analysts might like to avoid the difficulties of second-best analysis, but in this case there is no reason to believe that a partial analysis looking only at product market efficiency effects will lead us to the policy that is best overall.⁶⁸ We again stress a caveat: it could happen that after going through such a full analysis, the optimal antitrust policy in the U.S. and the EU turns out to be the same, or quite similar. We are not yet in a position to tell whether or not the optimal policies really do differ. However, we have seen a variety of reasons why they could well differ.

A consequence of all this is that comparing the welfare effects of antitrust policy becomes much more complex. We cannot look simply at the allocative effects in the product markets; we must consider the economy-wide effects. Moreover, antitrust policy cannot be evaluated in isolation. It must be considered along with the effects of a myriad of other policies in other areas with which it works to create economy-

⁶⁷ Indeed, the relative low size of those deadweight losses has been recognized since Harberger. See Arnold Harberger, *Monopoly and Resource Allocation*, 44 AM. ECON. REV. 77 (1954).

⁶⁸ Analysts should see this as an opportunity. The allocative efficiency effects of various antitrust rules have been analyzed in gory detail over the last few decades. Diminishing marginal returns have probably set in for such inquiries. The effects we consider here have received much less attention. The returns to investigations of those effects are likely to be relatively greater.

wide welfare effects. Which society leads to higher aggregate welfare, the U.S. or the EU? That is not an easy question to answer.

Finally, what are the consequences for the prospects of convergence in antitrust policy? If in the end the analysis suggests that different antitrust policies are optimal for the U.S. and the EU, the prospects for convergence would appear relatively bleak. So long as neither society chooses to change a host of interrelated markets and institutions, then convergence would seem unlikely, as each society would then be hurt if it changed its antitrust policy to resemble that of the other society.

Of course, it is possible that one society will choose to change many of its markets and institutions in a way that moves it closer to the other society. There are some signs that European capital markets, labor markets, and political institutions may be moving in the direction of their U.S. counterparts. Should that happen, we would expect EU antitrust policy to converge to U.S. policy as well. But, there are many obstacles to such change. Europeans may decide that, all things considered, such change is not worth it. Since changing antitrust policy may make sense only if many other policies and institutions change simultaneously, it may just be too costly to make all those changes. Thus, U.S. and EU antitrust policy may be elements that have adapted to larger systems, and American and European society may be locked-in to their different systems.⁶⁹ Historical contingencies may have led to these societal differences, but both societies may find it hard to escape their histories. Even if they do desire to change, the complexity and difficulty of changing so many different institutions may lead to a long, slow process of adaptation. Thus, our analysis reinforces the conclusion of Gifford and Kudrle that we should not expect a convergence of U.S. and EU antitrust policy anytime soon.

⁶⁹ See McDonnell, *supra* note 35, at 356.

