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# Do Antitrust Laws Protect Consumers?

Tech Central Station, August 2, 2005

by David R. Henderson

Many people think that antitrust laws are in place to protect consumers. But as Microsoft's current troubles in Europe show, that isn't necessarily so. The European Commission is using antitrust to carve out a market share for RealNetworks Inc., Microsoft's main rival in media-player software. And the EC is going to extreme lengths to do so, requiring Microsoft to sell a stripped-down version of its Windows software that doesn't contain Windows Media Player.

Microsoft has complied, but it wanted to name its new Windows version, "Windows XP Reduced Media Edition" ("Microsoft, EU Agree on Slimmer Version of Windows System," Wall Street Journal, March 29, 2005.) The EC refused, saying that the name would discourage sales and mislead customers. It didn't say how exactly putting the label "reduced media" on something that had fewer media features would mislead consumers. It was obvious, though, how it would discourage sales. Why buy a Ford without a radio when you can get a Ford with a radio at the same price?

(Disclosure: in 2002, I consulted for Microsoft. Second disclosure: I have a brain. This second disclosed fact, more than the first, accounts for my ability to see that the EC, whatever else it is doing, is not protecting consumers.)

If you think such nonsense can't happen here, think again. Leading the way were U.S. antitrust laws, beginning with the Sherman Act of 1890, which forbade any contract or conspiracy that restrained trade and any monopoly, attempt to monopolize, or conspiracy to monopolize. Now three philosophers, two economists, an historian and a lawyer, all of whom subscribe to Ayn Rand's philosophy of Objectivism, have written a book, *The Abolition of Antitrust* (Transaction Publishers), which argues that the antitrust laws should be abolished. The authors make a strong case.

Although many economists criticize specific abuses of antitrust laws, rare indeed are economists who think they shouldn't exist and who will challenge them on philosophical grounds. All the essays in the book, by the economists and the other four authors, do so. What is their case?

The best statement of the philosophical case against antitrust is in philosopher Harry Binswanger's essay, "Antitrust: 'Free Competition' at Gunpoint." Binswanger draws a fundamental distinction between economic power and political power. Economic power, he notes, is simply the power to produce and trade, whereas political power is the power of the government and necessarily rests on the use of force or threat of force. Someone can earn a large market share, even, in rare cases, a 100% market share, without ever coercing anyone. That person creates power simply through his productivity and does not forcibly take anything away from anybody; therefore, he should not be persecuted. That, in a nutshell, is Binswanger's philosophical case against antitrust. His whole exposition, though, is well worth reading.

Interestingly, even free-market great Milton Friedman confused economic and political power when discussing monopoly and antitrust. In his 1962 classic, *Capitalism and Freedom*, Friedman wrote, "Monopoly implies the absence of alternatives and thereby inhibits effective freedom of exchange." No it doesn't, unless the monopolist uses coercive power to prevent people from exchanging with others. A monopolist who gets his market power the new-fashioned way, by earning it, offers people an alternative they otherwise wouldn't have.

So how did the antitrust laws come about? Two essays, by historian Eric Daniels and by lawyer Thomas A. Bowden, give the history of the legal thinking on monopoly. In the early 19th Century, "monopoly" was understood to apply to cases where a government had given an exclusive power to a government agency or private firm, a power that prohibited others from competing. But when the corporate form of organization spread in the late 19th Century and firms earned large market shares by garnering economies of scale and cutting prices, smaller competitors and their intellectual allies used coercive language to describe the peaceful activities of such firms- and the language stuck. Economist Richard M. Salsman traces how economists in the early 20th Century came to accept the strangely labeled "perfect competition," under which no one has any power to influence price, no one makes profits, no one innovates and no one advertises. With this view of perfection, argues Salsman, it was a small step for economists and antitrust enforcers to accuse of monopoly any company that had the power to set prices, that made profits, that innovated, or that advertised.

The book is at its most effective when the authors distinguish clearly between force and voluntary action and when they tell horror stories about antitrust. Exhibit A of the latter is the DuPont cellophane story. The book's editor, philosopher Gary Hull, tells of clear-eyed DuPont chemists perfecting cellophane in the 1920s and creative marketers marketing it in the 1930s, revolutionizing the sale of bread, cake and other items. By 1940, a national poll found that Americans' most cherished words were, in order, "mother," "memory," and "cellophane."

Then came antitrust. The government charged that DuPont had "monopolized" the cellophane market. Most antitrust texts point out that the government lost the case. But Hull points out something that I had never read in 35 years of reading about antitrust: DuPont helped assure its "victory" by canceling its expansion plans and actually building a cellophane plant for a competitor, Olin Industries.

The book has some weaknesses. Historian Daniels asserts that a government that enforces patent rights is actually protecting against the initiation of force. While I agree with Daniels that patents are a good idea, violators of patent laws do not initiate force. And economist Salsman, in an otherwise excellent essay, is too critical of early 20th Century economist Joseph Schumpeter. Schumpeter, who argued that the prospect of a temporary monopoly is a strong incentive to innovate, should be a hero.

*David R. Henderson, a research fellow with the Hoover Institution and an economics professor at the Naval Postgraduate School in Monterey, Calif., is author of *The Joy of Freedom: An Economist's Odyssey* and co-author of the forthcoming book, *Making Great Decisions in Business and Life*.*