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The “Conspiracy” of Consumer Welfare Theory

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In April, Matt Stoller argued that a 1980 memo from George Stigler and Richard Posner to Martin Anderson, an economist serving on then-President-elect Reagan’s transition team, was the start of a conspiracy to derail antitrust enforcement.

Herb Hovenkamp responded to Stoller, arguing that the memo was not the “smoking gun” that Stoller thought. Hovenkamp argued the transition was not so dramatic and that “the memorandum and Reagan era antitrust policy is…a continuation of policies that originated in the Nixon administration.”

Erik Peinert pushes back against Hovenkamp’s view. Peinert points to the Horizontal Merger Guidelines revisions as proof that “Reagan officials knew their revised [1982] guidelines were out of step with the original intent of the Clayton Act, Congressional understanding of its purpose, judicial precedent, and popular sentiment.”

Paul Tucker claims the memo is “more akin to a piece of political punditry than a careful policy note weighing the pros and cons of transforming antitrust policy, or asking what might plausibly go wrong.” He laments that those writing the memo did not perhaps seek to disperse political power.

We believe the memo is but a piece of a larger puzzle ignored by the authors above. The economic crisis of the 1970s spurred corporations and high-income individuals to increased levels of activism, giving vast sums of money to promote conservative think tanks, conservative economists, and conservatives in law. This resurgence of corporate power sought to remove the barriers to high income and profits.

We detail here the historical events and subsequent political push that gave rise to the rise of consumer welfare theory, a very recent newcomer to 80-plus years of antitrust enforcement. Consumer welfare theory’s immersion into antitrust enforcement was not a paradigm shift: It was a massive political wave. The Stigler-Posner memo was a part of this concerted and unified push to transform antitrust policy in particular and the American economy in general.

The Economic Crisis of the 1970s

The US experienced a period of structural crisis in the 1970s. Corporate rates of return, or the rate of profit, declined significantly after 1968 and remained low in the 1970s. On one measure of the rate of profit, the period 1952-1971 averaged 20.2 percent. For the period 1974 to 1983, the same rate of profit averaged 15 percent. It recovered in the period 1998-2007 to 17 percent, but never achieved the rates of return in the period after World War II (often referred to as the "golden age of capitalism"). The low profits did not only impact corporations. Those wealthy enough to invest in the stock market also experienced no growth during the 1970s, because in the long run, stock prices tend to track the trend in profits. Rising inflation resulted in low and declining real interest rates, many turning negative in the late 1970s, near zero in 1971, and negative in 1975. An accumulation of factors contributed to the crisis of the 1970s. Beginning in the late 1960s, the US faced increased competition from Japan and Germany, both of which had recovered from World War II and successfully challenged the US in several major industries.

The impact of the structural crisis in the 1970s was devastating to high incomes. While high incomes were eroded by the policies of the New Deal Consensus that emerged in the 1930s and extended until the middle 1970s, high taxes, regulation of the financial sector, unionization, and other policies had resulted in what Claudia Goldin referred to as the "great compression," a period of historic wage compression spanning from the 1940s to the 1970s. However, by the 1970s high incomes were increasingly difficult to maintain. The share of income of the top 1 percent of income earners fell to its lowest historical point of just below 9 percent during the 1970s. The share of wealth of the top 1 percent also declined dramatically between 1968 and 1978.

While New Deal policies were not favorable to the rich, they resulted in spectacular economic performance. There is agreement among many economic historians that "the years 1929-1941 were, in aggregate, the most technologically progressive of any comparable period in the U.S. economic history." According to Robert Gordon, "The Great Leap Forward of the American Level of labor productivity that occurred in the middle decades of the twentieth century is one of the greatest achievements of all of economic history." The growth rate of the economy was also historically high. From 1947 to 1973, the average rate of GDP growth was 3.88 percent, and investment growth was also high at 8.95 percent.

The Backlash

The economic situation facing corporations, finance, and the wealthy sparked a major political backlash. The backlash took many forms but included what John Saloma referred to as the conservative labyrinth of well-funded conservative think tanks, corporate groups, and other organizations that grew in size and influence in the 1970s.

Emblematic of this revolt was a 1971 memo sent to the US Chamber of Commerce titled “Attack on American Free Enterprise System” by future Supreme Court Justice Lewis Powell. Powell called for businesses to organize, plan, and understand the importance of political power to their economic interests. According to economic historian Peter Temin, Charles Koch “was galvanized by the Powell Memo and formed the Cato Institute,” an organization focused on the proliferation of free market ideas among academics and politicians. According to *New York Times* columnist Binyamin Applebaum, “[t]he beer magnate Joseph Coors said he was inspired by Powell’s memo to create the Heritage Foundation.” Political scientists Jacob Hacker and Paul Pierson described the ensuing counterattack of business as “a domestic version of Shock and Awe.”

Numerous conservative think tanks were both established and expanded, including the Business Roundtable, the Scaife Foundations, the Lynde and Harry Bradley Foundation, the American Enterprise Institute, and the Institute for Contemporary Studies. As Roger E. Backhouse argued, these foundations were successful because they focused their support on a small group of conservative academics promoting neoliberal academic centers. Examples include the Coase-Sandor Institute for Law and Economics at Chicago, Public Choice at the University of Virginia, and George Mason University. We are not arguing that these economists were captured in their thought by the support they received. These scholars were supported *because* of the policies they already advocated.

Funding of conservative academics was nothing new. From the early 20th century, Chicago School economic programs were supported by the Volker Fund, which funded Hayek and other conservative economic scholars. As Applebaum describes, Stigler himself was offered a $25,000 position at the University of Chicago, with a “large research endowment” provided by Charles Walgreen.

However, now the money came more freely for positions, academic programs, and research support. As Elizabeth Popp Berman in her new book, “Thinking like an Economist: How Efficiency Replaced Equality in U.S. Public Policy” writes, “During the 1960s, big business felt increasingly threatened, by antitrust enforcement in particular, and by anti-business sentiment in general. As a result, organized business, which had not been associated with a particular school of economics, became more interested in Chicago ideas.” She describes how large corporations began to support Chicago economics as a means of defending against progressive policies.

By the late 1970s, the Olin Foundation became the primary patron of law and economics and Chicago School antitrust, as well as Harvard, Yale, Columbia, Stanford, Berkely, Virginia, Duke, Georgetown, and other schools. As described by Steven Teles, the goal of Olin Foundation funding was to promote law and economics as a free market counterweight to the legal theories of the New Deal consensus. As Popp Berman and Teles both describe, money became easier to have. Quoting Manne: “At this point, the [corporate] world knew that Chicago economics was the only thing saving them from an antitrust debacle.”

Antitrust law fell in line, with Justice Powell (of eponymous memo fame) leading the charge in the 1977 decision Continental T.V. Inc. v. GTE Sylvania Inc. Writing for the 6-2 majority, Justice Powell held that non-price vertical restraints warrant only rule of reason analysis. Appelbaum's interpretation is that "Powell was adopting Stigler's view that markets should get the benefit of the doubt." Regardless, holding made vertical exclusive customer and territory restrictions much more difficult to challenge. Antitrust law has further heeled in other areas. For example, the Chicago School's skepticism about cartel stability also contributed to the higher burden that emerged for proof of conspiracy. We note that not every instance of constriction of the per se rule need be related to the Chicago School's influence.

The Chicago School's influence also led to a more permissive approach to mergers. In the 1974 decision United States v. General Dynamics Corp., the Court rejected the DOJ's reliance on market shares. Extending this departure from precedent, lower courts also engineered several defenses to a merger challenge. Circuit courts followed suit, allowing for high-market share mergers to consummate due to ease of entry or substantial efficiencies. The agencies certainly helped. Each version of the Horizontal Merger Guidelines (HMG) published by the DOJ and FTC weakened merger enforcement. The 2010 HMG requires much more than the original structural presumptions mandated by the Court, including proof of an anticompetitive scenario resulting from the proposed merger. Even if that exacting hurdle is met, a showing of entry or significant efficiencies can still defeat the case for the merger challenge.

After conservatives began successfully advocating their neoliberal policies, the high incomes of the top 1 percent that had been held down by the policies of the New Deal consensus were restored. The share of income of the top 1 percent steadily increased after 1980. By 2017, it had reached levels nearly higher than prior to the great depression. The percent of wealth owned by the top 1 percent similarly increased dramatically beginning at the end of the 1970s reaching levels just below those of the 1920s by 2013.

While high incomes to the top 1 percent were restored, overall economic performance deteriorated under the neoliberal free market policies. Comparing, for example, 1947–1973 with 1980–2015, growth of GDP was lower, labor productivity was lower, real wage growth was lower, and unemployment was higher. Some of this decline in performance is a result of less competition. Thomas Philippon shows that the decline in investment rates beginning in the late 1990s is due to a reduction in competition in the economy.

Conclusion

Thus, the Posner-Stigler memo is a piece of a larger and more deliberate effort to advocate neoliberal policies. Hovenkamp is correct that the Posner-Stigler memo is not a smoking gun. However, Stoller is correct that the rise of Chicago antitrust was not merely a contest of ideas. The dominance of Chicago school ideas represented real benefits to big business that felt under duress because of the economic trends in the 1970s.

We provide economic data to assert that there were impacts derived from advocating the consumer welfare standard and accompanying neoliberal agenda policies. We only describe here the data and the before and after picture of higher growth and less inequality prior to the enactment of neoliberal policies.

Antitrust policy has changed many times throughout its history. To believe that the consumer welfare theory is anything more than a political policy with certain economic goals ignores the 80-plus years of antitrust enforcement and economic success that preceded consumer welfare theory.