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The Effectiveness of Proposed Antitrust Programs for Developing Countries†

A.E. Rodriguez and Mark D. Williams††

Abstract

We examine whether traditional antitrust policies are appropriate for developing economies. Economists have typically claimed that antitrust enforcement does little good in small economies with free trade since imports should temper anticompetitive behavior. However, some recent trade liberalization programs have not had the full effect that their proponents had advertised. Specifically, imports have not adequately tempered domestic market power in a number of countries that have liberalized trade. Many commentators, arguing primarily that nontradeables are immune to trade effects, advocate the establishment of antitrust agencies to correct this problem. However, we believe that this failure of liberalization suggests the inappropriateness of antitrust policies. We argue that the continuance of market power is due to interest group rent-seeking rather than price-fixing or other private cartelizations. In fact, policymakers in developing economies are institutionally susceptible to rent-seeking. Interest groups find soliciting preferential treatment from the state more attractive than cartelization. Thus, trade liberalization gives rise to significant state-sponsored non-tariff barriers, against which antitrust is powerless. We suggest that, at its most effective, an antitrust agency can have a powerful competition advocacy program insulated from political pressure.

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I. Introduction

Liberal trade policy has long been defended by the proposition that imports discipline domestic producers' market power to raise prices.¹ In broad geographic markets, international competition forces domestic firms to be competitive. However, trade economists puzzle over the seemingly insignificant effects of trade liberalization.² For example, Moises Naim, Venezuelan Minister of Development and architect of the 1989 radical liberalization and privatization program noted in a recent retrospective:

It is usually assumed that the lowering of tariff barriers and the liberalization of imports will tend to curb the pricing excesses of the highly concentrated local firms; this was clearly not the case in the initial stage of the Venezuelan experience.³

And, from two advocates of antitrust,

The evidence from the United States, the European Community, and Japan indicates that it is simply not the case that open borders or large numbers of competitors or easy entry or ensconced competitive values have prevented the formation of cartels.⁴

The perceived persistence of anticompetitive pricing has resulted in a number of developing countries adopting antitrust legislation and enforcement agencies,⁵ and has bolstered arguments for increased antitrust enforcement.⁶ Both the World Bank and developing country

¹ See RICHARD E. CAVES, INTERNATIONAL TRADE AND INDUSTRIAL ORGANIZATION: PROBLEMS, SOLVED AND UNSOLVED (Harvard Institute of Economic Research Discussion Paper No. 1131, 1985) ("[T]he larger is imports' share of domestic sales, the smaller is the effect of the concentration of domestic producers on the profits earned by those producers."); Louis Esposito & Frances Ferguson Esposito, *Foreign Competition and Domestic Industry Profitability*, 53 REV. ECON. & STAT. 343 (1971); Alexis Jacquemin et al., *Concentration and Profitability in a Small Open Economy*, 29 J. INDUS. ECON. 131, 142 (1980) ("In terms of policy, our results . . . suggest that one of the most felicitous public policies to maintain domestic competition is to condemn any form of protectionism."); Howard P. Marvel, *Foreign Trade and Domestic Competition*, 18 ECON. INQUIRY 103 (1980); Thomas A. Pugel, *Foreign Trade and U.S. Market Performance*, 29 J. INDUS. ECON. 119 (1980).

² See Albert Fishlow, *The Latin American State*, J. ECON. PERSP. 61, 65 (1990) ("Multiple cross-section studies demonstrating a favorable impact of exports on aggregate performance are not fully satisfying."); Steven Globerman, *Trade Liberalization and Competitive Behavior: A Note Assessing the Evidence and the Public Policy Implications*, 9 J. POL'Y ANALYSIS & MGMT. 80 (1990) ("A stream of literature has recently emerged that raises questions about the magnitude and even the direction of the impact of trade liberalization on competition."); Edward E. Leamer, *Cross-Section Estimation of the Effects of Trade Barriers*, in EMPIRICAL METHODS FOR INTERNATIONAL TRADE 51 (Robert C. Feenstra ed., 1988).

³ Moises Naim, *The Launching of Radical Policy Changes, The Venezuelan Experience: 1989-1991*, in VENEZUELA: DEMOCRACY AND POLITICAL AND ECONOMIC CHANGE 56, 107-08 (Joseph S. Tulchin ed., 1992).

⁴ Janusz A. Ordover & Russell W. Pittman, *The Role of Antitrust in Eastern Europe*, REG. Summer 1992, at 5.

⁵ All Eastern European countries, several of the former Soviet Republics, and a number of African and Latin American countries have recently inaugurated or increased antitrust scrutiny. See *infra* note 6.

⁶ See Jonathan D. Glater, *Busting Trusts, South of the Border: Latin Countries Take Antitrust Lessons from U.S. to Open Markets*, WASH. POST, Aug. 21, 1993, at B1.

Antitrust practitioners and scholars have advocated inclusion of antitrust policy as a recommended component of World Bank development policy or as an integral measure of lib-

policymakers, in a dove-tailing of interests, have embraced the ineffectiveness of trade liberalization as a rationale for increased antitrust scrutiny.⁷ Janet Steiger, the Chairman of the United States Federal Trade Commission, has recently described antitrust as "largely an American-made product" and one of her country's most successful exports.⁸ Similarly, the Assistant Attorney General for Antitrust during George Bush's tenure, James Rill, accommodated the expected increase in demand for antitrust assistance by establishing "a new Competition Policy Section in the Antitrust Division, whose main function will be to provide economic support for international activity."⁹ Indeed, the Bush administration specifically advocated antitrust for developing countries: "A basic antitrust law aimed at preventing cartel behavior by firms producing the same product and mergers that create monopoly is essential."¹⁰

Not surprisingly, the export of antitrust policy has drawn scathing

eralization programs. See Roger Boner, *The Basics of Antitrust II: Emerging Market Economies* (The World Bank forthcoming); Robert Bradburd & David R. Ross, *Regulation and Deregulation in Industrialized Countries: Some Lessons for LDCs*, (The World Bank 1990); Malcolm Coate et al., *Antitrust in Latin America: Regulating Government and Business*, 24 U. MIAMI INTER-AM. L. REV. 37 (1992); William E. Kovacic, *Competition Policy, Economic Development, and the Transition to Free Markets in the Third World: The Case of Zimbabwe*, 61 ANTITRUST L.J. (1992); William E. Kovacic & Roger S. Thorpe, *Antitrust Law for a Transition Economy*, LEGAL TIMES, Aug. 2, 1993, at 16; James Langenfeld & Marsha W. Blitzer, *Is Competition Policy the Last Thing Central and Eastern Europe Need?*, 6 AM. U.J. INT'L L. & POL'Y 347 (1991); Russell Pittman, *Merger Law in Central and Eastern Europe*, 7 AM. U.J. INT'L L. & POL'Y 649 (1992) ("Merger enforcement will be an important complement to the more obvious components of anti-monopoly enforcement (demonopolization, import liberalization, and dominant-firm regulation) in the transformation of the economies of Central and Eastern Europe."); Russell Pittman, *ANTIMONOPOLY LAWS IN A DEVELOPING MARKET ECONOMY*, draft, Department of Justice (undated), published in Czech language in NÁRODNÍ HOSPODÁRSTVÍ 32 (1991); James F. Rill, *Competition Policy and Economic Efficiency: Providing the Framework*, in COMPETITION AND ECONOMIC DEVELOPMENT 59, 59 (1991) (recommending to developing countries an "antitrust framework along the lines of those that have evolved in the United States and other OECD member countries as being the best way of securing and preserving competitive markets"); Robert D. Willig, *Anti-Monopoly Policies and Institutions*, in THE EMERGENCE OF MARKET ECONOMIES IN EASTERN EUROPE (Basil Blackwell ed., 1992) ("While the fundamental importance and difficulties of these steps cannot be overstated, it would, nevertheless, be a serious error to omit anti-monopoly policy from the list of free-market essentials or to leave it for last as an afterthought."); James F. Rill, *The Implementations of Competition Laws in Central and Eastern Europe: Lessons from the U.S. Experience*, Remarks Before the International Conference on Competition Law and Policy (Oct. 3, 1991) (on file with authors). Apart from Kovacic and Coate et al., most commentators have directed their analysis specifically towards Eastern Europe. However, similar ongoing FTC and DOJ aid initiatives in Latin America and Africa suggest that recommendations to these countries will be similar to those for Eastern Europe. Moreover, the recent (May 3-4, 1993) World Bank Conference on Competition Policy directed at Latin America underscores this focus on antitrust.

⁷ See CLAUDIO FRISCHTAK ET AL., *COMPETITION POLICIES FOR INDUSTRIALIZING COUNTRIES* (1989); VINOD THOMAS ET AL., *LESSONS IN TRADE POLICY REFORM* (1990).

⁸ *Trustbusters, Inc.*, ECONOMIST, Nov. 9, 1991, at 84.

⁹ James F. Rill, *International Antitrust Policy—A Justice Department Perspective*, Remarks Before the Fordham Corporate Law Institute Program on EC and U.S. Competition Law (Oct. 24, 1991) (on file with authors).

¹⁰ President's Message to Congressional Leaders Transmitting the 1991 Economic Report, 1 PUB. PAPERS 134 (Feb. 12, 1991).

criticism, most reflecting the view that imports will sufficiently temper market power.¹¹ In this Article, we further question the effectiveness of antitrust in developing economies. We recognize that imports may not fully eliminate market power in recently liberalized countries. However, we argue that this does not suggest that antitrust is the appropriate remedy. We argue that non-tariff barriers to trade will replace tariffs that trade liberalization removes because of the political power of rent-seeking special interest groups.¹² Antitrust is ill-prepared to counter market power generated by government protection.¹³

Next we discuss the relationship between endogenous trade theory¹⁴ and why import competition has seemingly been unable to control market power. Part III examines the economics of interest groups

¹¹ See Roger Boner & James Langenfeld, *Liberal Trade and Antitrust in Developing Nations*, REG., Spring 1992, at 5; Paul E. Godek, *One U.S. Export Eastern Europe Does Not Need*, REG., Winter 1992, at 21 (blasting American antitrust advocacy to Eastern European countries that have recently enacted antitrust laws and established enforcement agencies); Ordoover & Pittman, *supra* note 4, at 5; Paul E. Godek, *Protecting Eastern Europe from Antitrust*, REG., Fall 1992, at 4 (responding to Ordoover and Pittman's article). For other criticisms of the export of antitrust, see the Fall 1990 issue of REG. For a general criticism of antitrust, see DOMINICK T. ARMENTANO, *ANTITRUST AND MONOPOLY: ANATOMY OF A POLICY FAILURE* (1992) (rejecting virtually all antitrust enforcement). See also Lester C. Thurow, *Let's Abolish the Antitrust Laws*, N.Y. TIMES, Oct. 19, 1980, at C2. Although these critics attack American antitrust, it is probably safe to assume they feel similarly about other antitrust regimes.

¹² A "rent" is a return in excess of a resource owner's opportunity cost. Rents can arise naturally or as a result of a government action. When rents are created from short term shifts in, for example, tastes or technology, the pursuit of these rents, or "rent-seeking," is no different from "profit-seeking." However, rents can also exist through government action, but this does not mean that they are exempt from competition. The study of rent-seeking examines how people or groups compete for government-created rents.

There are several economic problems associated with artificially-created rents and associated rent-seeking activities. First, the monopolization of these rents results in an allocatively inefficient distribution of resources away from the monopolized sector. Second, all resources spent in the successful and unsuccessful pursuit of artificial rents are lost to society because they yield no additional social product. Similarly, resources used to protect rents from other people and groups generate no social product. These secondary expenditures of resources in the pursuit of artificial rents may constitute a far larger cost than the direct distortion due to market power. See Robert D. Tollison, *Rent Seeking: A Survey*, 35 KYKLOS 575 (1982).

¹³ Apart from the traditional objections to antitrust policies and the criticism within this paper, many groups, although generally supportive of the implementation of antitrust in theory, remain apprehensive of possible misuse of antitrust law. For example, commenting on competition policies recently inaugurated in Eastern Europe and other newly emergent market economies, the American Bar Association recently noted, "other antitrust prohibitions and emerging patterns of enforcement give cause for concern that the law might be applied too intrusively. The abuse of dominance law could, if applied unwisely, effectively restore price control under the guise of antitrust, thus taking back the freedom and rewards that the market gives." *Introduction and Recommendations of ABA Antitrust Law Section's Special Committee on International Antitrust*, 62 Antitrust & Trade Reg. Rep. (BNA) No. 1551, at 171 (Feb. 6, 1992). Note that the ABA's caveats are consistent with our hypothesis. Specifically, the possible abuse of antitrust law could be interpreted as a non-tariff barrier to trade, and the establishment of antitrust agencies lowers the costs of rent-seeking.

¹⁴ Endogenous trade theories have tariff levels determined within a model, and are derived by combining trade and public choice models. For example, Findlay's model marries a specific factors trade model with a median voter political model. See Ronald Findlay, *The New Political Economy: Its Explanatory Power for LDCs*, 2 ECON. & POL. 193 (1990).

seeking rents through government protection and why incentives for this are higher in developing countries. Part IV highlights the likely results of increasing antitrust enforcement. Part V discusses alternative approaches to reducing market power, and we conclude in Part VI.

II. Protectionism in Response to Import Competition

A cornerstone of neoclassical economics—and of antitrust analysis¹⁵—is the belief that reduction of tariffs and other barriers to trade will promote imports that will discipline domestic supracompetitive pricing.¹⁶ In fact, this prescription was a fundamental part of the policy package of reforms for the developing world known as the “Washington consensus.”¹⁷ Trade reform has also figured prominently in World Bank and IMF proposals.¹⁸

Traditional economics suggests that free trade policies are a cheaper means of preserving competition than antitrust enforcement for small economies.¹⁹ However these theories often have not considered distortions arising from interest groups seeking favors from policymakers. Results from economic theory may change dramatically

¹⁵ See, e.g., Symposium, *Antitrust Law and the Internationalization of Markets*, 64 CHI-KENT L. REV. (1988) (addressing how the internationalization of markets and of competition affects antitrust law and antitrust policy); *Joint Manufacturing Opportunities for Small Business: How High the Barriers?: Hearings on H.R. 423 Before Subcomm. on Antitrust, Impact of Dereg., and Privatization, and Subcomm. on Reg., Bus. Opportunities, and Energy of the House Comm. on Small Bus.*, 101st Cong., 1st Sess. 4 (Feb. 27, 1989) [hereinafter *Hearings*] (Statement of Charles F. Rule: “[Foreign competition] makes it unlikely that cooperative production ventures among U.S. firms would give those firms the ability to exercise market power and harm competitors and consumers.”); U.S. Department of Justice and Federal Trade Commission 1992 Horizontal Merger Guidelines, 57 Fed. Reg. 41,552, 41,555 (1992), reprinted in 62 *Antitrust & Trade Reg. Rep.* (BNA) No. 1559 (Special Supp. Apr. 2, 1992) [hereinafter *Horizontal Merger Guidelines*] (used by the Federal Trade Commission and the Department of Justice to evaluate the likelihood of anticompetitive effects of mergers between competitors, and recognizing the potential procompetitive impact of foreign imports).

¹⁶ A large number of empirical industrial organization studies examined this concept by comparing changes in domestic competitive performance to changes in tariffs. See *supra* note 2. For another study of the relationship between domestic profits and import levels, see Emilio Pagoulatos & Robert Sorensen, *Domestic Market Structure and International Trade: An Empirical Analysis*, 16 Q. REV. ECON. & BUS. 45 (1976). This research has concluded that import competition tends to reduce price-cost margins and thus constrains domestic prices.

¹⁷ LATIN AMERICAN ADJUSTMENT: HOW MUCH HAS HAPPENED? 1 (John Williamson ed., 1990).

“Washington” meant primarily the International Monetary Fund, the World Bank, and the U.S. executive branch, although the term was intended to cover also at least the Inter-American Development Bank, those members of Congress who take an interest in Latin America, and the think tanks concerned with economic policy. A summary description of the content of this Washington agenda is macroeconomic prudence, outward orientation, and domestic liberalization.

Id. (laying out the policy changes that Washington had been urging the Latin American countries to make).

¹⁸ See DEMETRIOS PAPAGEORGIOU ET AL., *LIBERALIZING FOREIGN TRADE IN DEVELOPING COUNTRIES: THE LESSONS OF EXPERIENCE* (1990); VINOD THOMAS ET AL., *supra* note 7.

¹⁹ See Godek, *One U.S. Export Eastern Europe Does Not Need*, *supra* note 11; Godek, *Protecting Eastern Europe from Antitrust*, *supra*, note 11; *Hearings*, *supra* note 15.

once this endogenous rent-seeking behavior is allowed. This may explain why the recent trade liberalizations seem so weak in combatting market power.²⁰ Producer interest groups may respond to increased import competition with innovative forms of anticompetitive behavior. Theories of endogenous protectionism predict that private domestic interest groups will respond to potential loss of rents by intensifying their lobbying efforts.²¹ Higher losses of rents cause proportionately greater lobbying activities.

Theorists of endogenous tariffs,²² rent-seeking²³ and other related fields have found a direct correlation between reduced tariffs and the rise of non-tariff barriers.²⁴ This indicates that interest groups may

²⁰ A firm or group of firms acting together have market power if they face downward sloping demand curves and have the power to influence prices. A firm or cartel with market power can profitably charge a price above that determined under competition. As such, when price is above marginal costs, society suffers welfare losses due to the misallocation of resources away from sectors where firms have market power. See DENNIS W. CARLTON & JEFFREY M. PERLOFF, *MODERN INDUSTRIAL ORGANIZATION* 737 (1990).

²¹ Many modern political economy theories of regulation view government activity as the outcome of competition between interest groups for access to the political process and its redistributive power. For a closely related interest group theory of legislation, see Robert Tollison, *Regulation and Interest Groups*, in *REGULATION: ECONOMIC THEORY AND HISTORY* 59 (Jack High ed., 1991). For theories of endogenous-tariff formation, see *infra* note 22. For theories of rent-seeking, see *infra* note 23. These theories share the assumption that government policymaking arises from a noncooperative game rather than a cooperative "public interest" game. Our definition of "interest group" is not the same as in the interest groups theory. Rather, we use the term to refer to any firm, trade association, or similar organization that uses the political process to obtain protective regulation or other non-tariff barriers to deny entry to a potential competitor.

²² See generally JAMES ANDERSON & ROBERT E. BALDWIN, *THE POLITICAL MARKET FOR PROTECTION IN INDUSTRIAL COUNTRIES: EMPIRICAL EVIDENCE* (World Bank Working Paper No. 492, 1981); ROBERT E. BALDWIN, *THE POLITICAL ECONOMY OF U.S. IMPORT POLICY* (1985); REAL P. LAVERGNE, *THE POLITICAL ECONOMY OF U.S. TARIFFS: AN EMPIRICAL ANALYSIS* (1983); STEPHEN P. MAGEE ET AL., *BLACK HOLE TARIFFS AND ENDOGENOUS POLICY THEORY: POLITICAL ECONOMY IN GENERAL EQUILIBRIUM* (1989); William A. Brock & Stephen P. Magee, *The Economics of Special Interest Politics: The Case of the Tariff*, 68 AM. ECON. REV. 246 (1978); Anne O. Krueger, *The Political Economy of the Rent-Seeking Society*, 64 AM. ECON. REV. 291 (1974); Wolfgang Mayer, *Endogenous Tariff Formation*, 74 AM. ECON. REV. 970 (1984); Edward John Ray, *Tariff and Non-tariff Barriers in the United States and Abroad*, 63 REV. ECON. & STAT. 161 (1981); Edward John Ray, *The Determinants of Tariff and Non-tariff Restrictions in the United States*, 89 J. POL. ECON. 105 (1981); Stanislaw Wellisz & Ronald Findlay, *Protection and Rent-Seeking in Developing Countries*, in *NEOCLASSICAL POLITICAL ECONOMY: THE ANALYSIS OF RENT-SEEKING AND DUP ACTIVITIES* 141 (David Colander ed., 1984).

²³ See generally JAMES A. BUCHANAN ET AL., *TOWARD A THEORY OF THE RENT-SEEKING SOCIETY* (1980); R.E. McCormick, *The Strategic Use of Regulation*, in *THE POLITICAL ECONOMY OF REGULATION: PRIVATE INTERESTS IN THE REGULATORY PROCESS* (1984); Charles K. Rowley & Robert D. Tollison, *Rent-Seeking and Trade Protection*, in *PROTECTIONISM AND STRUCTURAL ADJUSTMENT* (Heinz Hauser ed., 1986); Robert D. Tollison, *supra* note 12. For an attempt to group related theories from many fields in economics, see *NEOCLASSICAL POLITICAL ECONOMY: THE ANALYSIS OF RENT-SEEKING AND DUP ACTIVITIES* (David Colander ed., 1984) (surveying the literature and collecting papers by several of the original contributors to the theory).

²⁴ See generally Daniel Treffer, *Trade Liberalization and the Theory of Endogenous Protection: An Econometric Study of U.S. Import Policy*, 101 J. POL. ECON. 138, 139 (1993) (showing that "[w]hen trade protection is modeled endogenously, its restrictive impact on imports is large, ten times the size obtained from treating protection exogenously"). For a critique discussing the difficulty that endogenous trade theorists have in tying theoretical constructs to empirical

find soliciting protective regulation more attractive than either competing or cartelizing.²⁵ Economic benefits sought through political means with anticompetitive intent are considered by most economists to be wasteful because of the accompanying reduction in social welfare.²⁶

As liberalization programs are implemented, domestic interest groups that have traditionally benefited from high tariffs and other government favoritism resort to soliciting non-tariff barriers as a means of continuing their control over home markets. Government action, such as establishing product standards, environmental standards, local purchasing preferences, exemptions from restrictions on specialization and export-sharing agreements, anti-dumping legislation,²⁷ trade-remedy laws,²⁸ and formal and informal vertical restrictions such as exclusive dealing arrangements, often result in the establishment of these non-tariff barriers.²⁹ This can impose a significant cost on the economy.³⁰

A promising hypothesis to explain the low rate of price decline is that non-tariff barriers that perpetuate anticompetitive pricing persist or even arise after trade liberalization. This hypothesis suggests that the orthodox competition policy for small economies of free trade is inappropriate. Moreover, the erection of non-tariff barriers seems, at first, to support the establishment of antitrust regimes.

Traditionally, antitrust advocates justify interventionist policies by alleging a market's inability to deal with particular structural problems.³¹ Of course, other rationales are mentioned in political de-

formulations, see Douglas Nelson, *Endogenous Trade Theory: A Critical Survey*, 32 AM. J. POL. SCI. 796 (1988).

²⁵ Robert E. Baldwin, *Assessing the Fair Trade and Safeguard Laws in Terms of Modern Political Economy Analysis*, WORLD ECON., Mar. 1992, at 185, 193-94.

²⁶ See T.N. Srinivasan, *Neoclassical Political Economy, the State and Economic Development*, 3 ASIAN DEV. REV. 38 (1985).

²⁷ See generally PATRICK A. MESSERLIN, ANTIDUMPING REGULATIONS OR PROCARTEL LAW? THE EC CHEMICAL CASES (World Bank Working Paper No. 397, 1990). "[A]ntidumping regulations are a device that domestic firms—which would not be able to collude if there were no protection—can easily capture for cartelizing domestic markets." *Id.* at Foreword.

²⁸ See Thomas Coughlin, *U.S. Trade Remedy Laws: Do They Facilitate or Hinder Free Trade?*, 73 REV. FED. RESERVE BANK OF ST. LOUIS 3 (1991) ("[T]he concept of fair trade and trade remedy laws are often used by special interest groups to pursue their own agenda at the expense of the national interest.").

²⁹ For a discussion of how these policies can act as non-tariff barriers, see ANDERSON & BALDWIN, *supra* note 22; BALDWIN, *THE POLITICAL ECONOMY OF U.S. IMPORT POLICY*, *supra* note 22.

³⁰ These barriers raise prices for imports and their protected domestic substitutes. Moreover, they result in allocative inefficiency. In an economy at full employment, increased imports in an industry force resources to be employed in other sectors where they can be used more productively. By producing goods and services in which it has a comparative advantage and importing the rest, a nation can increase its income available to consume and invest. Since increased protection distorts the relative prices away from costs, it leads to an inefficient allocation of resources.

³¹ The focus of American antitrust enforcement has historically been on market structure, especially concentration levels. Although one still finds proponents of the structural

bate and the details of any program often reflect the strengths of countervailing political forces, not reasoned argument exclusively.³² Several competing hypotheses explain an increase in demand for antitrust. First, increased antitrust activity could be due to the conventional public interest assumptions that a workably competitive marketplace will achieve a more efficient allocation of resources, greater efficiency in production, and increased innovation.³³ This assumes the state is benign and maximizes welfare. This "naive" premise has come under intense criticism especially from the "New Political Economy School", which views government officials as seeking private goals, giving rise to endogenously-determined policies.³⁴

Second, it is possible that government officials incorrectly infer what antitrust can accomplish. Apart from anecdotal vignettes we found no clear evidence that the objectives of antitrust have been misinterpreted.³⁵ It is, however, more likely that diverse interest groups view government antitrust policies as privately beneficial.³⁶

Third, the adoption of antitrust is one of a number of mechanisms whereby developing countries can signal investors that investment in their countries is attractive. For example, in a recent statement, a Department of Justice official, referring to recently passed antitrust legislation in Eastern Europe, noted, "They recognize the importance of

approach, the new "law and economics" learning has shifted this focus to overall market efficiency and the short term interests of consumers. For the most part, American antitrust has challenged activities that restrict competition and lead to higher consumer prices. See generally ROBERT H. BORK, *THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF* (1978); RICHARD A. POSNER, *ANTITRUST LAW: AN ECONOMIC PERSPECTIVE* (1976); Frank H. Easterbrook, *The Limits of Antitrust*, 63 TEX. L. REV. 1 (1984).

³² See generally STEPHEN BREYER, *REGULATION AND ITS REFORM* (1982).

³³ See, e.g., PHILLIP AREEDA, *ANTITRUST ANALYSIS* 6-34 (1974).

³⁴ Unlike the more traditional economic analysis, the New Political Economy does not assume that the government is composed of Platonic guardians and acts benevolently, seeking the public interest. In the New Political Economy, rational agents, using available information in forming future expectations maximize their private gains. For example, bureaucrats fight for turf or to distribute publicly-created rents. This methodology predicts the implementation of policy by examining the costs and benefits that accrue to all agents. Thus the ultimate shape and impact of any policy prescription is dependent upon both the interests and political strengths of all interested agents. By contrast, economics had traditionally viewed governmental policy as an exogenous *deus-ex-machina*. Analysts often accepted the superficial rationale for various policies and just examined the implications of each government policy. See, e.g., *POLITICS AND POLICY-MAKING IN DEVELOPING COUNTRIES* (Gerald M. Meir ed., 1991).

³⁵ But see Joan Nelson, *The Political Economy of Stabilization: Commitment, Capacity, and Public Response*, in *TOWARD A POLITICAL ECONOMY OF DEVELOPMENT* 80, 91-92 (Robert H. Bates ed., 1988) ("In some cases, ministers and political leaders simply have very limited economic backgrounds and understanding. This can be true in any country, but it is more likely in countries with short history of independence and comparatively few highly educated people.").

³⁶ This certainly appears to be the case in the United States. See William S. Comanor, *Antitrust in a Political Environment*, 27 *ANTITRUST BULL.* 733, 734-735 (1982) (observing that two sets of interests provide critical support for the American antitrust laws: the first source of ideological support is the American political tradition distrustful of corporate or business power; a second critical group relates antitrust policies to corporate legitimacy).

maintaining a competitive marketplace to attract trade and foreign investment, and to promote the vigor of their domestic economies."³⁷ However, researchers have found exactly the opposite—that antitrust activity fosters investor uncertainty.³⁸

Fourth, assuming that non-tariff barriers are fairly close substitutes for tariff barriers, an interest group that controls government policy might allow tariff liberalization. This allows the government to claim victory to international lenders. In turn, to placate internal opposition, the government would swiftly establish antitrust as a non-tariff barrier.

Fifth, the referral of a troublesome matter, such as the rise of gasoline prices after tariff removals, to an "independent" antitrust authority, enables the executive to effectively defuse potentially troublesome demands for action by affected groups. These are only a subset of the possible explanations for the demand for establishment of antitrust policies, but none appear to us to explain the current interest in establishing antitrust policies in developing countries.

Both proposed and recently adopted antitrust policy recommendations for developing countries have, for the most part, been remarkably restrained.³⁹ These programs reflect the American antitrust experience of the past decade—an economic approach with a minimalist view as to the proper scope of these laws as business regulation.⁴⁰ The minimalist "Chicago School" view of antitrust "seems to favor little other than prosecuting plain vanilla cartels and mergers to

³⁷ Charles S. Stark, *International Antitrust: Looking Ahead*, Address Before the Antitrust and International Sections of the American Bar Association 2 (Aug. 9, 1993) (transcript on file with authors).

³⁸ See, e.g., George Bittlingmayer, *Stock Returns, Real Activity, and the Trust Question*, 47 J. FIN. 1701, 1702 (1992) (finding that in the United States, during the first half of the century, "antitrust case filings and other enforcement events are linked with lower stock prices").

³⁹ See *Ley Federal de Competencia Económica*, D.O. (Dec. 24, 1992), a Mexican law which serves as an especially clear example. By contrast, the recently-enacted Venezuelan law is much more restrictive. However, the Venezuelan antitrust agency has been writing ingeniously minimalist "Rules" ("Reglamentos") to implement the law. In practice, Venezuelan and Mexican antitrust policies are similar. See *Ley para Promover y Proteger el Ejercicio de la Libre Competencia*, GAZETA OFICIAL, Jan. 15, 1992; *Reglamento de la Ley para Promover y Proteger el Ejercicio de la Libre Competencia: Sobre el Regimen de Excepciones*, GAZETA OFICIAL, Jan. 21, 1993.

⁴⁰ See Robert Pitovsky, *Antitrust in the Next 100 Years*, 75 CAL. L. REV. 817, 818 (1987) ("The only matters that regularly attract the attention of the enforcement authorities are cartels, horizontal mergers tending to create a monopoly, and various forms of predation. . . . [E]nforcement agencies have introduced various exceptions and qualifications into prior law and today tend to resolve most doubts in favor of nonintervention.").

Unfortunately, Professor Pitovsky fails to discuss the increasing influence of "Chicago School" analysis in the federal courts and how this affects an agency's decisions. Agencies will less vigorously pursue cases when they believe that the chances of winning in court are lower. With the greater influence of the Chicago School, U.S. antitrust agencies may have pursued only the strongest cases. For an understanding of the main tenets of the Chicago School, see BORK, *supra* note 31; Frank H. Easterbrook, *Workable Antitrust Policy*, 84 MICH. L. REV. 1696 (1986); Richard A. Posner, *The Chicago School of Antitrust Analysis*, 127 U. PA. L. REV. 925 (1979).

monopoly."⁴¹ However, despite continued recognition of the detrimental and anticompetitive effects of many forms of regulation,⁴² few distortionary rules and regulations are overturned once the explicit link between regulatory barriers to competition and the influence of interest groups in the political process is noted. Policies to sever government's role in obtaining market power for interest groups are rarely discussed. Policies that do confront government protection of rent-seeking interest groups are generally limited to small competition advocacy programs.⁴³

Antitrust policy in developing countries (or anywhere else, for that matter) is ill-suited to challenge this "new protectionism" of non-tariff barriers. As such, the impact of trade liberalization on domestic competition often depends critically on both the institutional structure of the government and how amenable that structure is to interest group influence.

III. The Economics of Protective Regulation

Many analysts have noted a tendency for non-tariff barriers to increase as tariffs decline.⁴⁴ If non-tariff barriers replace liberalized tariffs, effective government protection may remain unchanged after trade reform. One needs to assess this reaction of higher non-tariff barriers to trade liberalization when evaluating the potential of antitrust policy changes.

All else equal, competitive markets tend to keep prices close to costs and there are few incentives for foreign firms to import.⁴⁵ In contrast, the wide differences between prices and costs found in anticompetitive industries are likely to invite import discipline.⁴⁶ Import competition is thus expected to constrain prices more in highly concentrated industries that face foreign competition. Put differently, import competition is a countervailing force against whatever power domestic firms may have to raise prices above the competitive and socially efficient level.

The responses of producers to trade liberalization are determined

⁴¹ Easterbrook, *supra* note 40, at 1701.

⁴² See Robert W. Hahn & John A. Hird, *The Costs and Benefits of Regulation: Review and Synthesis*, 8 YALE J. ON REG. 233 (1991).

⁴³ See Coate et al., *supra* note 6, at 57 ("Government economists and attorneys prepare comments on proposed policies of other federal and state government agencies. . . . [Thus] the antitrust agencies ensure that the relevant decision makers are exposed to the competitive consequences of their proposed actions.").

⁴⁴ See Trefler, *supra* note 24; Nelson, *supra* note 24.

⁴⁵ Obviously, if foreign firms have a cost advantage over domestic firms, there may be plenty of incentives to import, regardless of the institutional details of the particular market.

⁴⁶ William F. Chappell & Bruce Yandle, *An Entry Model of Import Penetration*, 19 ATLANTIC ECON. J. 22, 27 (1991) (finding that "increases in imports are positively related to the level of pre-level concentration."). But see Don P. Clark et al., *Domestic Market Structure and International Trade in an Open Economy*, 32 Q. REV. ECON. & FIN. 3, 12 (1992) ("Results fail to confirm that industry concentration exerts a positive influence on imports.").

by the resulting distribution of winners and losers from this policy. With a prospective reduction in rents due to increased import competition—clearly a threat to producer group stability—the threatened group will establish or increase its lobbying pressure on political powers. One commentator has argued an interest group's influence is affected not only by the number and size distribution of its members, but also by the extent to which its common interests are threatened.⁴⁷ Government favors and the resulting supracompetitive prices are collective goods to the interest group; the benefits obtained go to each producer in the favored industry. Developing economies often have few firms in many industrial sectors and thus have small producer interest groups.⁴⁸ Because each member gets a significant fraction of the benefit from action, these interest groups are relatively easy to organize in response to a potential loss of rents. Thus, one would expect, *a priori*, that defensive responses by domestic interest groups to trade liberalization are likely to be more vigorous in concentrated industries where potential for losses of rents is higher.

The link between group dynamics and the seeking of preferential treatment via non-tariff barriers is well understood.⁴⁹ Often these non-tariff barriers are in the form of government regulation, which often benefits the regulated producers rather than the public. Models that endogenously predict when interest groups will seek preferential treatment offer useful insight in our analysis of the importance and usefulness of antitrust in developing countries. These theories assume the rationality of *homo economicus* in studying politics and government.⁵⁰ As such, theorists assume that interest group behavior is a determinant of protectionist government policies. Until recently, it was customary to analyze economic policies and their effects assuming the policies were determined exogenously. Tariff and non-tariff trade barriers, as well as other types of anticompetitive regulation, arise when government officials, politicians and bureaucrats—acting formally in the

⁴⁷ See generally MANCUR OLSON, JR., *THE LOGIC OF COLLECTIVE ACTION: PUBLIC GOODS AND THE THEORY OF GROUPS* (1965) (arguing that an interest group's influence is affected not only by the number and size distribution of its members, but also by the extent to which its common interests are threatened).

⁴⁸ Partrio Meller, *Industrial Concentration in Latin America*, 27 J. INDUS. ECON. 41, 45 (1978) (arguing, on the basis of a survey of the structure of industrial concentration, that in manufacturing sectors, "Latin American countries that have smaller (larger) market sizes systematically show higher (lower) levels of industrial concentration.").

⁴⁹ See *supra* notes 22-23; MANCUR OLSON, *THE RISE AND DECLINE OF NATIONS: ECONOMIC GROWTH, STAGFLATION, AND SOCIAL RIGIDITIES* (1982); PEDRO FRAILE-BALBIN, *INDUSTRIALIZACIÓN Y GRUPOS DE PRESIÓN: LA ECONOMÍA POLÍTICA DE LA PROTECCIÓN EN ESPAÑA 1900-1950* (1991) (providing a recent examination of Olson's approach applied to tariff dynamics).

⁵⁰ The term *homo economicus* refers to people acting rationally to explain their social, economic, and political behavior. See SHAUN H. HEAP ET AL., *THE THEORY OF CHOICE: A CRITICAL GUIDE* 62 (1992) ("*Homo economicus* is an instrumentally rational and calculating seeker of preference satisfaction. He is the figure who typically appears in neoclassical economic theory as a maximizer of utility."); Jack Hirshleifer, *The Expanding Domain of Economics*, 75 AM. ECON. REV. 53 (1985).

state's interest, but whose underlying motivation may be the maximization of private gains—"sell" protectionism demanded by producer interest groups.

If interest groups face low transaction costs in agreeing to petition the government, their incentives to support a competitive market are less than the potential gains from seeking rents through political action.⁵¹ The ease of access in the structure of government and the political process in most Latin American countries result in preferential treatment through protectionism.

Government intervention in the marketplace distorts prices and resource flows from socially efficient levels.⁵² Although it is an important issue in all countries, government intrusion is particularly problematic in Latin America and other developing countries. This is because policy making tends to be less visible, more closed, and more centralized in these countries. Often the political process is so closed that citizens learn of new policies when they are formally announced or decreed by the political leadership.⁵³ In general, policy making is dominated by high level administrators and politicians.⁵⁴ It is the executive branch, not the legislative branch, which tends to be the target of those seeking political favors.⁵⁵ Many members of the executive do not face electoral review and often their tenure in office is highly indeterminate.⁵⁶

Because of the difficulty of organizing large groups, producer groups tend to be more influential than consumer groups. Olson's free-rider problem suggests that large, diffuse interest groups find protecting their interests difficult.⁵⁷ Although a protective policy may greatly and adversely affect consumers in a group, the stake of any particular consumer is normally too small to justify individual political investments. Moreover, organizing consumers to aggregate their

⁵¹ See William Glade, *Privatization in Rent-Seeking Societies*, 17 *WORLD DEV.* 673, 680 (1989) ("For decades, rent has been distributed lavishly to buy political support. Constituency building, in turn, has been used to yield a kind of political rent to the governments in charge of this extensive system of differential reward.").

⁵² Resource allocation in the production of widgets is said to be "socially efficient" if the price (marginal social benefit) of widgets equals the marginal (social) opportunity cost of producing another widget. If the opportunity cost of producing another widget, which is the value of the resources if diverted to their highest-valued alternative use, is less than the price of widgets, which is the marginal consumer's valuation of widgets, then it would be socially efficient to produce more widgets. Competition tends to equalize the marginal opportunity costs of production with the price of goods. Distortional government intervention drives a wedge between prices and marginal opportunity costs and hence will not be socially efficient.

⁵³ For a more accurate and detailed description of the process summarized in this section, see MERILEE S. GRINDLE, *THE NEW POLITICAL ECONOMY* 24 (World Bank Working Paper No. 304, 1989), reprinted in *POLITICS AND POLICY MAKING IN DEVELOPING COUNTRIES* (Gerald M. Meir ed., 1991).

⁵⁴ *Id.* at 24.

⁵⁵ *See id.*

⁵⁶ *See id.*

⁵⁷ *See OLSON, supra* note 47.

political investments is difficult because any benefits will be spread over all consumers—regardless of whether they actually invest. Well-organized consumer groups could, in principle, provide an effective counterweight to producer groups in the fight for political influence.⁵⁸ The producer interest groups, by comparison, are often compact, focused, and their members highly interested in proposed policies, and therefore better able to marshal political investments.⁵⁹ Indeed, an optimal policy for firms in oligopolistic markets who are under severe import competition may be to take actions, such as reducing production and laying off workers, that increase the likelihood of receiving import protection from the government.⁶⁰

Interest groups, especially the well-organized and well-connected, wield their political influence behind the scenes in informal interactions with political leaders rather than through more visible activities such as getting-out-the-vote campaigns. Other interest groups, although engaged in less intimate lobbying efforts, nonetheless make their interests known. In the case of the military, the implicit threat of a coup is a powerful, legitimate, and always credible threat that tempers any legislator's desire to challenge the generals' interests.⁶¹ Similarly, large foreign investors may articulate their desires in a nonpublic manner.⁶² In other cases, interest groups may be in a mutually dependent relationship with particular government agencies, politicians, or political parties.⁶³ These bureaucracies, politicians, or political parties

⁵⁸ Some of these disenfranchised groups, often not organized for sustained political activity, frequently make demands by striking, rioting, or marching in protest.

⁵⁹ See Russell Pittman, *Market Structure and Campaign Contributions*, 31 PUB. CHOICE 37, 38 (1976) (showing, with American data, that individuals associated with firms in concentrated industries were more likely than those associated with firms in unconcentrated industries to make contributions to President Nixon's re-election committee, if the industries were dependent in certain important ways upon government decisions).

⁶⁰ See Michael P. Leidy & Bernard M. Hoekman, *Spurious Injury as Indirect Rent-Seeking: Free Trade Under the Prospect of Protection*, 3 ECON. & POL. 111 (1991).

⁶¹ The two coup attempts in Venezuela, the impeachment of President Carlos Andres Perez, and the subsequent reversal of the liberalization process underscore this argument. See M. Delal Baer, *Revenge of the Venezuelan Dinosaurs*, WALL ST. J., June 18, 1993, at A13 (directly linking the impeachment of President Perez to the threatened interests of influential Venezuelan industry groups); Carlos Ball, *Venezuela's Crossroads: Market Revival or Socialism Redux*, WALL ST. J., Aug. 27, 1993, at A7. Albeit somewhat extreme, a coup attempt is a rather effective non-tariff barrier to trade.

⁶² See Tor Skalnnes, *The State, Interest Groups and Structural Adjustment in Zimbabwe*, 29 J. DEV. STUD. 401 (1993) ("[A] government's economic policies . . . are the outcome of pressures both from domestic and external authors."). Note that Zimbabwe recently passed anti-trust legislation. See Kovacic, *supra* note 6, at 257; see also Paul Mosley, *On Persuading a Leopard to Change His Spots: Optimal Strategies for Donors and Recipients of Conditional Development Aid*, in TOWARD A POLITICAL ECONOMY OF DEVELOPMENT 47, 47 (Robert H. Bates ed., 1988). See generally Symposium, *The Political Economy of Debt*, 39 INT'L ORG. 357 (1985).

⁶³ See Peter H. Schuck & Robert E. Litan, *Regulatory Reform in Peru*, REG., Jan.-Feb. 1987, at 36 [hereinafter Schuck & Litan I] ("Large corporations, engaged in classic anti-competitive, rent-seeking strategies, had developed a symbiotic relationship with the national government which was willing to secure rents for its corporate allies through the exercise of its regulatory authority."). See also Peter H. Schuck & Robert E. Litan, *Regulatory Reform in the Third World: The Case of Peru*, 4 YALE J. ON REG. 51 (1986) [hereinafter Schuck & Litan II].

may find it difficult to terminate or even weaken these relationships.⁶⁴

Krueger, describing the dynamics of rent-seeking, observes that market responses to economic policies affect the political equilibrium and, in turn, induce changes in economic policy.⁶⁵ The adoption of lower tariffs with the expectation of increased imports enhances certain groups' ability to influence the political process relative to others'. By changing the relative strengths of different interest groups, the political equilibrium is altered.⁶⁶ The lowered tariffs may have unanticipated effects and fail to achieve its supporters' expectations.⁶⁷ These effects may strengthen or weaken the policy regime and may lead to pressure to eliminate or change various policies to favor particular sectors. Political equilibrium is not just a function of competing interests, but also a function of overall economic performance. When a liberalization program affects economic performance, particularly the level of consumption, it will also influence the government's overall level of support.⁶⁸ This, in turn, may constrain or change policy decision-making. Indeed, poor economic performance may make legislators and government officials more responsive to claims of disproportionate duress caused by economic liberalization.⁶⁹

IV. The Effect of Antitrust

We have discussed how the fundamental competition problem in developing economies is the interest groups' ability to influence government to raise non-tariff barriers in response to liberalization policies. Indeed, governmental institutions in these countries seem to be exceptionally vulnerable to pressure from interest groups. Although many analysts have recommended competition advocacy programs to

⁶⁴ See Ana Julia Jatar, *Competencia o Componenda*, ECONOMÍA HOY, Oct. 5, 1993, at 6 (describing mechanisms used by interest groups in Venezuela to obtain private benefits from the state).

⁶⁵ Anne O. Krueger, *Virtuous and Vicious Circles in Economic Development*, 83 AM. ECON. REV. 351 (1993).

⁶⁶ See Paul H. Rubin & Mark A. Cohen, *Politically Imposed Entry Barriers*, 18 E. ECON. J. 333 (1992) (finding that political entry barriers are endogenous).

⁶⁷ See Dani Rodrik, *Policy Uncertainty and Private Investment in Developing Countries*, 36 J. DEV. ECON. 229 (1991).

On the one hand, entrepreneurs, workers, and farmers must respond to the signals generated by the reform for the new policies to be successful. On the other hand, rational behavior by the private sector calls for withholding investment until much of the residual uncertainty regarding the eventual success of the reform is eliminated.

Id.

⁶⁸ See Rolf J. Luders, *Massive Divestiture and Privatization: Lesson from Chile*, 9 CONTEMP. POL'Y ISSUES 1 (1991) (noting that the initial Chilean privatization effort failed "partly due to the economic and financial crisis affecting most Latin American countries in the 1980s").

⁶⁹ All else equal, a comparatively disadvantaged industry is likely to receive tariff protection since it can generate greater sympathy from policymakers and the general public. Thus, such an industry is likely to bear the brunt of trade liberalization. See ANDERSON & BALDWIN, *supra* note 22; LAVERGNE, *supra* note 22.

advise agencies against establishing trade restraints, these advocacy programs have generally lacked enforcement powers.

In fact, antitrust laws have been on the books of several developing countries for a long time, but they have done little to reduce anticompetitive behavior. This suggests that the laws have been ignored because they run counter to the perceived national interest, that the agencies in charge of enforcement have been captured, or that the laws simply could have been ineffective.⁷⁰

The fundamental objective of proposed antitrust regimes is to attack horizontal price-fixing under a *per se* standard.⁷¹ All proposals also contain a competition advocacy function as an essential component.⁷² However, all these proposals recommend a passive advocacy role, whereby the antitrust agency will only advise when other agencies request comments.

There are several limitations to advocacy roles as proposed. First, these advocacy programs often require administrative procedures that are either undeveloped or unknown in developing countries.⁷³ Second, without a formal administrative law procedure that invites public comment, it is difficult for the competition advocate to discover potentially anticompetitive regulations on the drawing board.⁷⁴ Third, the antitrust agency would be unable to force other agencies to heed its recommendations. Fourth, even if the antitrust agency were successful in opposing anticompetitive regulation, it may find itself vulnerable to bureaucratic turf warfare.⁷⁵

⁷⁰ See George J. Stigler, *The Economic Effects of the Antitrust Laws*, in THE ORGANIZATION OF INDUSTRY 259 (1968); UNCTAD Secretariat, *Control of Restrictive Business Practices in Latin America*, 21 ANTITRUST BULL. 137 (1976) ("Direct control of restrictive business practices through antimonopoly legislation has in general been of only marginal significance.").

⁷¹ See Coate et al., *supra* note 6, at 81.

⁷² See *id.* at 56-57. See also Schuck & Litan II, *supra* note 63, at 63-67. A competition advocacy program was implemented in Peru in the late 1980s as part of a broader regulatory reform program. *Id.* The advocacy program consisted of technocratic and regulatory analysis "designed to expose and limit rent-seeking regulation that chiefly benefits politically influential economic interests and imposes large costs on society." *Id.* at 53.

⁷³ See *id.* at 65.

The system of administrative law so familiar to the U.S. system was quite alien to Peru. The process of rule making in Peru was remarkably straightforward: a ministry wishing to adopt a rule simply published it in the final form in *El Peruano*, the official government newspaper. Private individuals or groups had no legal right to participate in the rule-making process in any way, and there were no sanctions, judicial or otherwise, for routine bureaucratic illegality.

Id.

⁷⁴ In the case of Venezuela during the Perez administration, the competition office, known as Procompetencia, was able to monitor closely proposed rules and regulations because a member of that office was married to one of the most important ministers and had close friendships with most of the rest of the cabinet. Thus, the competition office effectively opposed many anticompetitive initiatives at the cabinet level. Venezuela, like most code law countries, has no administrative procedures inviting public comment on proposed rules and regulations.

⁷⁵ The fate of Vice President Quayle's Competitiveness Council is illustrative. See Kenneth J. Cooper, *Divided House Bars Funds for Quayle Competitiveness Council*, WASH. POST, July 2,

We now examine the effects of a traditional antitrust regime that concentrates on attacking horizontal price-fixing. Market and government structures in developing economies allow producers to choose whether to obtain anticompetitive rents from either cartelization or seeking favors from the state. Interest groups will choose that combination of collusion and government protection which maximizes expected rents.

As shown below, rent-maximizing interest groups will devote resources between attempted cartelization and government influence based on the relative costs of the two activities.

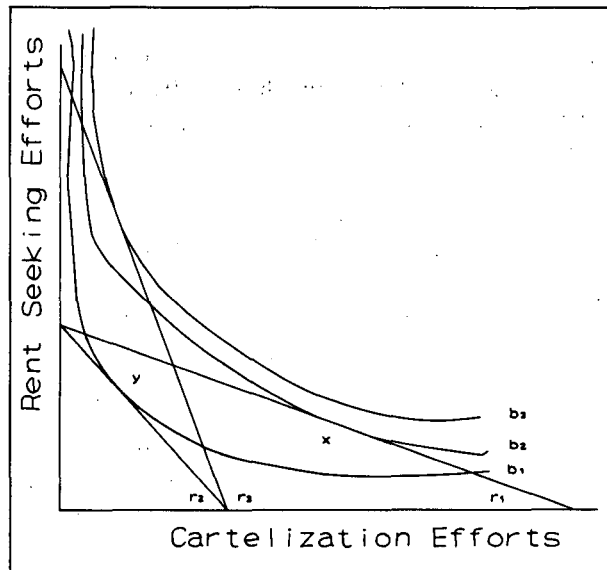


Figure 1

Figure 1 demonstrates this tradeoff. The level of benefits (excess rents) obtained by the interest group increases in both the amounts of rent-seeking and cartelization effort the group undertakes. Iso-benefit curves b_1 , b_2 and b_3 draw out sets of the amount of effort devoted to the two strategies (lobbying the state or organizing a cartel) that yield the same levels of expected benefits to the group. In the drawing, if the interest group chooses a point on curve b_2 , it expects greater profits than a point on b_1 . Similarly, b_3 offers greater profits than b_2 . The iso-resource lines follow equations of the form $r = p_L L + p_C C$, where r is

1992, at A6 (the House voted to deny funding to the Competitiveness Council chaired by Vice President Quayle); Bob Woodward & David S. Broder, *Quayle's Quest: Curb Rules, Leave No Fingerprints*, WASH. POST, Jan. 9, 1992, at A1 (looking into how Vice President Quayle used "his chairmanship in the President's Council on Competitiveness as a command post for a war against government regulation of American business"). Similarly, the Federal Trade Commission's weak competition advocacy function may be due to the Commission's general reluctance to antagonize other agencies.

the total resources that the group will allocate to these activities, p_L is the unit price of lobbying the government for protection, L is the level government lobbying, p_C is the unit price of organizing, monitoring, and enforcing a cartel, and C is the level the cartel activities. For any given level of resources r , the group will attempt to reach the highest iso-benefit curve. Thus, a group will choose its level of activity at the point where the iso-revenue line is tangent to the iso-benefit curve.⁷⁶

Consider for the moment an interest group having iso-resource curve r_1 . With this constraint, it will choose x on curve b_2 where its expected benefits are maximized. If an antitrust agency is established, p_C , the unit price of cartelization efforts, rises and this shifts the group's iso-resource curve to r_2 . Note that r_2 intersects the rent-seeking effort axis at the same point as r_1 because the cost of rent-seeking has remained the same. The group then shifts its composition of efforts to point y on curve b_1 . Obviously, economies of scale and scope in political influence may cause different firms to face different relative prices for particular resources. However, as the costs of cartelization rise relative to rent-seeking, at the margin,⁷⁷ the interest group will seek more rents through government protection. The establishment of an antitrust regime may cause an increase in other forms of government protection. If the starting of an antitrust agency only makes it more difficult to cartelize, the special interest group is worse off than before.

The intent of antitrust initiatives is to encourage market competition. In reality, however, interest groups will follow their incentives and shift resources into monopolization through government protection.⁷⁸ Lobbying the government for protection may be highly substitutable for organizing cartels. Private monopolists have the same incentives as competitive firms to minimize costs by producing efficiently with the appropriate technology and factor mix. In addition to allowing prices above costs, government non-tariff barriers may encourage firms to no longer minimize costs. In this sense, antitrust may cause inefficiencies that are worse than the allocative losses that it is designed to defend against.

⁷⁶ This methodology is discussed in any good introductory or intermediate microeconomics textbook as a basic model of consumer behavior. See, e.g., EDWIN MANSFIELD, *MICRO-ECONOMICS* ch. 2 (2d ed. 1975); PAUL A. SAMUELSON, *ECONOMICS* ch. 22 (11th ed. 1980).

⁷⁷ The marginal rate of substitution is the instantaneous slope of the iso-benefit curve. This slope is steeper at point y than point x .

⁷⁸ Trade protection is designed to protect domestic industry from international competition. Such protection establishes monopoly rents in markets where long-run domestic supply elasticities are finite. Inevitably, trade protection has a domestic rent-seeking constituency prepared to fight for the creation and retention of protectionist policies. Interactions between these rent-seeking constituencies determine the precise protectionist policy that will emerge in the political marketplace. Charles K. Rowley & Robert D. Tollison, *Rent-Seeking and Trade Protection*, in *PROTECTIONISM AND STRUCTURAL ADJUSTMENT* 154, 154 (Heinz Hauser ed., 1986).

Indeed, the previous analysis assumes that antitrust will be effective in raising the costs of cartelization. By establishing an antitrust agency, these proposals may also establish yet another target for rent-seeking by interest groups.⁷⁹ This can be analyzed as a fall in the price of rent-seeking effort.⁸⁰ Referring to the previous figure, the fall in that price will shift the firm resource constraint from r_2 to r_3 . The interest group would then maximize its expected benefits on the iso-benefit curve b_3 at point z . If the price of rent-seeking falls, interest groups will seek even further protection at the margin. Indeed, the special interest groups may be better off with both the increased price of private cartelization and the reduced price of rent-seeking if b_3 is to the right of b_2 (as shown).⁸¹ The establishment of an antitrust regime may actually advantage targeted special interest groups that act anticompetitively.

Also note that interest groups will lobby to obtain exemptions from antitrust enforcement. In the United States, numerous statutory exemptions, which may be partial or complete and can apply to particular industries, organizations, or activities, are a measure of how competition policy can be compromised.⁸² All these exemptions were

⁷⁹ There is a voluminous literature on this point. See Richard A. Posner, *A Statistical Analysis of Antitrust*, 13 J. L. & ECON. 365 (1970); Richard A. Posner, *The Federal Trade Commission*, 37 U. CHI. L. REV. 47 (1969) (claiming "that Federal Trade Commission investigations are undertaken at the behest of corporations, trade associations and trade unions whose motivation is at best to shift the cost of their private litigation to the taxpayer and at worst to harass competitors"). See also WILLIAM F. SHUGHART II, *ANTITRUST POLICY AND INTEREST GROUP POLITICS* 36-49 (1990) (advancing a private interest theory of antitrust, suggesting that enforcement was seldom in the public interest and often used to protect particular competitors at the expense of competition and efficiency); Bruce L. Benson et al., *Interest Groups and the Antitrust Paradox*, 6 CATO J. 801 (1987) (arguing that "the antitrust laws are a result of a special interest struggle between small and large economic entities seeking changes in the general economic environment rather than the specific favors usually associated with special interest legislation"); Roger L. Faith et al., *The Antitrust Pork Barrel*, 15 J. L. & ECON. 329 (1982). But see Russell Pittman, *Antitrust and the Political Process*, in *EMPIRICAL STUDIES IN INDUSTRIAL ORGANIZATION* 147, 147-60 (David B. Audretsch & John J. Siegfried eds., 1992); Russell Pittman, *William Shugart's Antitrust Policy and Interest Group Politics*, 7 REV. INDUS. ORG. 91-95 (1992) (book review).

⁸⁰ As the technology to rent-seek expands, the costs of rent-seeking cannot go up *ceteris paribus* and if the new technology, lobbying the antitrust agency, is more efficient than other technology, lobbying congressmen, for example, then the cost (price of effort) of rent-seeking falls.

⁸¹ Whether the interest group is better off depends upon the size of the shifts in prices of rent-seeking and cartelization, as well as the position of the original equilibrium and the shape of the iso-benefits curves.

⁸² Most sectors have received their exemptions from Congress. Major league baseball, exempted through a 1922 Supreme Court decision stating that games are not interstate commerce, is a notable exception. See *Federal Baseball Club v. National League of Professional Baseball Clubs*, 259 U.S. 200 (1922); accord *Flood v. Kuhn*, 407 U.S. 258 (1972). See generally Thane N. Rosenbaum, *The Antitrust Implications of Professional Sports Leagues Revisited: Emerging Trends in the Modern Era*, 41 U. MIAMI L. REV. 729 (1987). Other exemptions based on the scope of the Commerce Clause have been overturned only recently. For example, as late as 1974 the federal courts held that the practice of law was a learned profession and, therefore, not part of commerce. *Goldfarb v. Virginia State Bar*, 497 F.2d 1 (4th Cir. 1974), *rev'd*, 421 U.S. 793 (1975).

secured by rent-seeking interest groups seeking preferential government treatment, yet claiming some legitimate public purpose.⁸³

The United States experience with antitrust exemptions is not impressive and suggests little to recommend it to other nations. However, none of the antitrust proposals advanced for developing economies contain mechanisms that would effectively limit interest groups from engaging in rent-seeking behavior. Assuring that decision makers receive a well-balanced analysis of the competitive repercussions of proposed legislation appears to be the sole alternative available to a competition agency's efforts to limit interest group influence.

V. Policy Alternatives

In the previous section, we noted that effective antitrust raises the costs of cartelization. Unfortunately, especially in developing economies, these higher costs increase the relative attractiveness of seeking

Other exemptions to antitrust laws abound. The insurance industry enjoys exemptions. See JONATHAN R. MACEY & G. MILLER, *COSTLY POLICIES: STATE REGULATION AND ANTITRUST EXEMPTION IN INSURANCE MARKETS* (1993). So does the agricultural industry. See Alan M. Anderson, *The Agricultural Cooperative Antitrust Exemption*, 67 CORNELL L. REV. 396 (1982); Alice S. Horneber, Comment, *Agricultural Cooperatives: Gain of Market Power and the Antitrust Exemption*, 27 S.D. L. REV. 476 (1982). The petroleum industry is in some cases exempt. See Gary D. Libecap, *The Political Economy of the Establishment of the Interstate Oil Cartel, 1933-1940*, in *RESEARCH IN ECONOMIC HISTORY* 53 (Supp. 4 1985).

As noted, some exemptions are statutory, as in the case of the export trading firm exemption. See the Webb-Pomerene Export Trade Act of 1918, 15 U.S.C. §§ 61-65 (1918), amended by the Export Trading Company Act, 15 U.S.C. §§ 4011-21 (1988), under which firms in the United States may cartelize their export operations with immunity from the antitrust laws. 15 U.S.C. § 4016(a) (1988). Moreover, firms may set a common industry export price, establish export quotas for members and assign exclusive trading areas overseas. See Wilbur L. Fugate, *The Export Trade Exception to the Antitrust Laws: The Old Webb-Pomerene Act and the New Export Trading Company Act*, 15 VAND. J. TRANSNAT'L L. 673 (1982). For a more detailed exchange over the antitrust immunity for shipping conferences, see David A. Butz, *Ocean Shipping Economics: Free Trade and Antitrust Implications*, 11 CONTEMP. POL'Y ISSUES 69 (1993); James D. Reitzes, *Ocean Shipping Economics: Comment*, 11 CONTEMP. POL'Y ISSUES 81 (1993); David A. Butz, *Ocean Shipping Economics: Reply*, 11 CONTEMP. POL'Y ISSUES 86 (1993).

Other exemptions have been suggested. See, e.g., Stephen P. Paschall, *Antitrust and Hospital Mergers: A Law and Economics Rationale for Exemption*, 30 DUQ. L. REV. 61 (1991).

For a general treatment of antitrust exemptions, see HERBERT HOVENKAMP, *ECONOMICS AND FEDERAL ANTITRUST LAW* (1985).

⁸³ The rationales for antitrust exemptions are varied. Several different justifications have been suggested. Among these are: the disparity of economic power between persons in the particular category and their competitors, suppliers, or purchasers, see, e.g., *April v. Nat'l Cranberry Ass'n*, 168 F. Supp. 919, 921 (D.Mass. 1958); equity considerations, see, e.g., *Robinson-Patman Act*, 15 U.S.C. § 13-13b, (1988); the interests of Federalism, see, e.g., *Parker v. Brown*, 317 U.S. 341, 350-351 (1942); exercise of political rights, see, e.g., *Noerr Motor Freight, Inc. v. Eastern R.R. Presidents Conference*, 365 U.S. 127, 136-38 (1961) with accord given in *United Mine Workers v. Pennington*, 381 U.S. 657, 669-72 (1965). In *Noerr* the Court held generally that private parties may petition the government seeking anticompetitive relief without violating antitrust laws. *Noerr*, 365 U.S. at 136-38. In *Pennington* the Court stated that seeking such relief did not violate the antitrust laws "even though they intended to eliminate competition." *Pennington*, 381 U.S. at 670. For a more detailed description of the *Noerr-Pennington* doctrine, see generally Daniel R. Fischel, *Antitrust Liability for Attempts to Influence Government Action: The Basis and Limits of the Noerr-Pennington Doctrine*, 45 U. CHI. L. REV. 80 (1977).

government protection. However, the analysis of restraint of trade through cartelization or government protection is the same. The guiding principle of antitrust economics—restraints on competition harm consumers—applies equally well to the study of government barriers as to cartelization. This suggests that an antitrust agency is uniquely qualified for a competition advocacy role in government. Indeed, FTC Commissioner Mary L. Azcuenaga recently advocated targeting government anticompetitive restraints in the United States.⁸⁴ Because of the susceptibility of government agencies to private influence in developing countries,⁸⁵ shifting antitrust resources to competition advocacy against anticompetitive regulations is likely to be more effective there than in developed economies.

When considering regulations, it is important not to take the cynical view that all regulation is anticompetitive, protectionist, and driven by special interest influence. Indeed, some interest group regulation may be procompetitive.⁸⁶ A competent competition advocacy role must determine whether a particular regulation is, in fact, anticompetitive and whether it is the result of interest group pressure.⁸⁷

We suggest that competition advocacy should attack regulations meeting the following criteria: If a particular regulation restrains market rivalry,⁸⁸ we would then determine whether the policy was enacted at the initiative of a producer interest group. If the regulation does not restrain competition, then it should not be challenged. If, on the

⁸⁴ Mary L. Azcuenaga, *The Tariff Is Still the Mother of the Trust*, 29 WASHBURN L.J. 359 (1990).

⁸⁵ There has historically been an intense collaboration between the government and private sector in most developing countries. This traditional symbiosis has only recently been altered as liberalization policies have been adopted. Competition agencies face the daunting task of challenging, for example, accumulated human capital associated with personal contacts and traditional rules of doing business. These have often resulted in anticompetitive practices under the new competitive regime. We see this lag because liberalization regimes have focused on macroeconomic correctives and largely ignored distortional microeconomic regulations and business practices. See generally GRINDLE, *supra* note 53; Ana Julia Jatar, *Implementing Competition Policy on Recently Liberalized Economies: The Case of Venezuela*, Procompetencia Working Paper, Caracas, Oct. 1993 (on file with authors).

⁸⁶ Examples are disclosure requirements and the creation of marketable property rights. Adequate disclosure of certain information allows buyers and sellers to make more informed choices and may lower transaction costs and allow markets to function more effectively. Externalities can be overcome, for example, by establishing marketable rights to engage in particular sorts of conduct such as pollution or production of a patented product. Eventually those willing to pay the most to exercise these rights (for example, those for whom the cost of avoiding pollution is greatest or cost of producing a product is least) will buy up the rights.

⁸⁷ See James S. Wiley, Jr., *A Capture Theory of Antitrust Federalism*, 99 HARV. L. REV. 713 (1986).

⁸⁸ If no strong historical evidence is available, this condition may be analyzed by relying on the hypothetical price test approach used by the U.S. antitrust agencies in their investigations. The antitrust agencies ask whether a firm or a group of firms acting as the only present and future seller of the product (a hypothetical monopolist) could profitably impose a "small, but significant and nontransitory" price increase. 1992 Horizontal Merger Guidelines, *supra* note 15.

other hand, a regulation is anticompetitive, it has met a necessary but not a sufficient condition for attack. There are many types of regulations that may be socially beneficial yet may restrain competition.⁸⁹ A proposed regulation should not be challenged if it directly solves a serious market (or social) failure—one that creates an otherwise unavoidable efficiency loss likely to outweigh efficiency losses caused by the regulation.⁹⁰ If the costs of the regulation outweigh its benefits, the regulation should be scrapped.⁹¹ To limit the scope of regulations that should be tested, Olson's insight suggests that we concentrate our attention on those anticompetitive proposals stemming from producer interest group lobbying.⁹²

The experience of competition advocacy runs through the anti-trust agencies in the United States has been disappointing.⁹³ Because

⁸⁹ As with the regulation of natural monopoly, the regulation of spillover costs (also known as externalities) may reduce social deadweight loss. E. Mishan, *The Postwar Literature on Externalities: An Interpretive Essay*, 9 J. ECON. LITERATURE 1 (1971). However, there are a number of scholars who have argued that externalities need not justify heavy-handed government intervention, but rather a rearrangement of private property rights. See generally Guido Calabresi & A. Douglas Melamed, *Property Rules, Liability Rules and Inalienability: One View of the Cathedral*, 85 HARV. L. REV. 1089 (1972); Harold Demsetz, *Toward A Theory of Property Rights*, 57 AM. ECON. REV. 347 (1967).

⁹⁰ Oil and gas field regulations may be necessary to counteract the "Rule of Capture" property law which gives a producer title to all oil from a well even if that well drains oil from parts of the reservoir underneath adjoining property owners. To the extent that regulations reduce such "common pool" problems, they will increase economic efficiency and consumer welfare. Alternatively, to the extent that regulation reduces production and increases prices, it reduces economic efficiency and consumer welfare. See STEPHEN McDONALD, *PETROLEUM CONSERVATION IN THE UNITED STATES* 31-33 (1971).

⁹¹ Economic "impact statement" requirements have been repeatedly proposed and often implemented both by the American Executive and Congress. Stephen Breyer notes several proposals designed to highlight the costly distortions caused by regulation. Breyer, *supra* note 32, at 353-64. For example, President Ford, by executive order, required agencies to write "inflationary impact statements." Under this order, agencies would need to determine the costs of their proposed action and alternative, less costly ways of dealing with the problem. President Carter rescinded this order, and, in its stead, ordered "regulatory impact statements." Under Carter's order, before an agency took a major action, it was required to state both the action's objectives and alternative ways of achieving them. *Id.*

Congress has also considered the impact statement approach. A 1980 reform bill by Senator Ribicoff, for example, would have agencies consider the economic consequences of major rules. Senator Kennedy introduced a bill in 1979 that would require a "competitive impact statement." An agency would have to show, before taking an action that would substantially lessen competition, that the agency's statutory objectives could not be satisfied using a less restrictive alternative. *Id.*

Breyer notes several major significant weaknesses of these proposals. The final decision-making authority often remains within the agency and that almost all regulation, even when far too restrictive and undesirable, has some plausible justification. *Id.*

⁹² Coordination becomes more difficult as the number of players increases. See RUSSELL HARDIN, *COLLECTIVE ACTION* 43 (1982); OLSON, *THE LOGIC OF COLLECTIVE ACTION*, *supra* note 47, at 53; OLSON, *THE RISE AND DECLINE OF NATIONS*, *supra* note 49, at 29; MICHAEL TAYLOR, *THE POSSIBILITY OF COOPERATION* 8 (1987).

⁹³ See BREYER, *supra* note 32, at 364-65 (recounting the futility of "competitive impact statements").

In every instance one can find claims, evidence, and argument that will support regulation. . . . Thus, it will not be difficult for agencies to reach a decision and then to write whatever impact statement is needed to justify it. The temptation

the policy has been passive, many regulations that should have been challenged have not been. The agencies are almost never asked to comment on proposed legislation. Furthermore, the agencies suffer political pressure from above, from the President and Congress,⁹⁴ who both are lobbied by producer interest groups, to limit their advocacy roles. Even if the agencies have written position papers against proposed regulation, these briefs are routinely ignored.⁹⁵ All of this suggests that if competition advocacy is to be effective in developing countries, the role and powers of the agency responsible for its implementation may need to be specified and defined in the country's legal body that is least susceptible to political pressure. Although constitutions in developing countries seem quite malleable given American standards, they may be least subject to political whim. Alternatively, competition advocacy could be established through trade treaties with other countries, which would raise the costs of abandoning such policies.⁹⁶ Although a competition advocacy agency may be made less vulnerable to the day-to-day political pressures of society, this may not guarantee its effectiveness in the long run.

If such a competition advocacy role is established, its major target must be the agency making the proposed regulation. Challenging lobbying efforts by producer interest groups raises objections to limiting the traditional constitutional rights to petition one's government and to freedom of speech.⁹⁷ Given government's distaste for interagency

for the agency to do so will be great, because its staff, through inertia, will tend to favor existing regulatory directions. And in many agencies it is common practice first to reach a decision and then to have a special opinion-writing section compose a statement in justification.

Id.

⁹⁴ See B. Dan Wood & James E. Anderson, *The Politics of U.S. Antitrust Regulation*, 37 AM. J. POL. SCI. 1 (1993) (finding that the Antitrust Division of the Department of Justice is "strongly affected by the major U.S. political actors, including the president, Congress, and courts").

⁹⁵ Politicians will not necessarily embrace a program on the efficiency grounds advocated by positive economic analysis. Politicians, being human, may be driven by narrower pursuits, such as political survival and effectiveness. Stigler recognized how private incentives may affect regulation. See George Stigler, *Economists and Public Policy*, REG., May-June 1982, at 13. Several scholars have highlighted the importance of political and economic forces in understanding regulatory policies and the limitations of regulatory reform efforts. For example, Hahn & Hird, *supra*, note 42, at 259, recommend Roger Noll, REFORMING REGULATION: AN EVALUATION OF THE ASH COUNCIL PROPOSALS (Studies in the Regulation of Economic Activity, 1971).

⁹⁶ It has been suggested that the North American Free Trade Agreement is a result, at least partly, of Mexican President Salinas de Gortari's desire to "lock in" his liberalization program. See, e.g., J. William Middendorf, *Conservatives' Misguided Case Against NAFTA*, WASH. TIMES, Nov. 15, 1993, at A19; J. William Middendorf, *NAFTA's Prospects Depend on Vindicating Reagan's Legacy*, WASH. TIMES, Nov. 16, 1993, at A17.

⁹⁷ For the comments raised by critics of Professor Wiley, *supra* note 87, reflecting this objection, see William H. Page, *Capture, Clear Articulation and Legitimacy: A Reply to Professor Wiley*, 61 S. CAL. L. REV. 1343 (1988); Matthew L. Spitzer, *Antitrust Federalism and Rational Choice Political Economy: A Critique of Capture Theory*, 61 S. CAL. L. REV. 1293 (1988). But see James S. Wiley, Jr., *A Capture Theory of Antitrust Federalism: A Reply*, 61 S. CAL. L. REV. 1327 (1988).

squabbling, it is unlikely that such competition advocacy will be effective.⁹⁸ Even a limited advocacy function for a government competition agency is unlikely to be very effective challenging anticompetitive interest group influence. Perhaps competition advocacy may be better accomplished through private sector think tanks, which are not as subject to political pressure, but which may be less effective in obtaining early word of proposed regulations or the ear of the agency promulgating these rules.⁹⁹ We are not encouraged by past attempts at competition advocacy by government agencies. In the only cases we have found, the initiatives were instituted, implemented, and eventually frustrated by a lack of governmental enforcement and support from an apathetic private sector.¹⁰⁰

VI. Conclusion

We have argued that the recent antitrust initiatives proposed by antitrust experts are inappropriate or, at least, inadequate for most developing economies. These proposals have typically advocated enforcement of a *per se* standard against horizontal price-fixing. However, rather than cartelization, the salient problem in developing countries appears to be the ease with which interest groups successfully petition public authorities to raise non-tariff barriers to competition in response to reductions in tariffs, impositions of antitrust regimes, and other liberalization programs. Often, the gain to interest groups of establishing cartels or price-fixing schemes are outweighed by simply soliciting preferential treatment from the state. If potential monopolists are uninterested in cartelizing, then the role of antitrust is slight.

In analyzing the theory of interest groups, one concludes that attacking producer-backed trade restraints is an appropriate constituent in any structural reform program for developing countries. Such a competition advocacy program should speed the dismantling of private and public restrictions upon freedom to contract and contribute to the country's commitment to a market economy. In principle, an antitrust agency is uniquely qualified to do this job. Charged with countering interest group lobbying for government protection, the an-

⁹⁸ See James Q. Wilson & Patricia Rachal, *Can the Government Regulate Itself?*, 46 PUB. INTEREST 3 (1977) ("Even within the same level of government, an agency will have great difficulty in attaining its goal, if, to do so, it must change the behavior of another agency.").

⁹⁹ Due to the lack of formal administrative law procedures for incorporating public comments on rulemaking, even private think tanks would face difficulties in presenting independent opinions. In addition, no real political constituency for regulatory reform exists in developing countries. See Schuck & Litan II, *supra* note 63, at 65-66.

¹⁰⁰ See *id.* at 53. See also Ball, *supra* note 61, at A7. The new Venezuelan agricultural minister, having listened to the complaints of rich farmers and cattlemen, has proposed to reverse the great strides to a market economy in foodstuffs. New restrictions on 209 key imports will become effective September 21, 1994, when imported goods as diverse as cement, rice, auto parts, fertilizers, toys, and detergents will have to be registered and approved by a brand new government bureaucracy, the Autonomous Certification and Norms Service. *Id.*

titrust agency could help prevent subversion of economic restructuring. As such, the antitrust effort could provide a valuable stimulus to market forces and the economy. In practice, however, we doubt that any nation, developing or not, has the willingness or commitment necessary for such a controversial initiative.

Those who advocate the export of antitrust to developing economies should reconsider the effectiveness of their prescriptions and address the shortcomings of such proposals outlined here. At the very least, we believe that these advocates' rosy predictions of the potential of antitrust should be tempered.