# FUNDAMENTAL CHARACTERISTICS OF THE AMERICAN ECONOMY

## Degrees of Competition, of Monopoly, and of Countervailing Power; Theoretical Significance

## COUNTERVAILING POWER

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### I

One is greatly favored in being allowed to speak about a book which he himself has written. He can fairly claim to be an authority on what the author said or meant to say. He is not expected to conform to especially high standards of scientific detachment. On the contrary, a certain partiality and even admiration for the work under discussion is permissible—in fact commonplace.

The only problem of such a speaker, in fact, is what to say. Obviously, if he has any bright ideas on the subject, he should have had them when he wrote the book.

My own solution to this latter problem is to confine my observations on countervailing power to an introductory word and give my attention largely to my critics. To some of these I have long been wanting to address a loving word.

### II

We are concerned here with the oldest of economic problems—that of the mitigation or regulation of economic power. Anciently, two solutions have been recognized to the problem of economic power. One is competition. The other—always assuming that anarchy and exploitation are not solutions—is regulation by the state. I have argued that there is a third mitigant of substantial, and perhaps central, importance in our time. That is the neutralization of one position of power by another.

The focus of the use and also of the abuse of economic power is the market. Competition mitigates economic power by making the behavior of any participant in the market contingent on the behavior of other and like participants. It makes sellers subject to the independent actions of other sellers, and buyers subject to the independent action of other buyers. The undoubted effect is to limit or dissolve the opportunity for arbitrary, or self-interested, or perhaps any effective use of market power which would limit or lower the real income of others. With the decline of independent market behavior—or perhaps more accurately its decay as a plausible assumption—a gap has been left in our explanation of the operative mechanics by which the economy is governed. This gap has certainly not been filled by the state in any general way. I have argued that economic power has been mitigated—the gap filled—by countervailing power. Those who are subject to the aggressions of economic power—to a monopoly or to a strong buyer of their labor or of their products—have both a negative and a positive incentive to organize resistance. They are impelled to do so for their protection; they are encouraged to do so by the prospect of splitting off some of the gains associated with the original power position. The methods of organizing this answering bargaining power—this countervailing power—are exceedingly various. Yet a broad identity of motive and of result seems to me evident. It has become a significant and perhaps a principal reliance of the weak seller or the weak buyer when faced with a strong position across the market.

I have ventured to suggest that much recent controversy over labor and farm policy and over many of the interstitial market relationships—those between large sellers and mass buyers for example—become intelligible only in light of the implicit recognition of economic groups of the importance of countervailing power.

## III

Now for the criticism. Let me make clear at the outset that I have no serious ground for complaint at the way these ideas, in their more developed form, have been received. The number who have objected, per se, to an economist's playing with reality has so far seemed quite surprisingly small. And we must have men who resist any tampering with the rigidly idealized world of our ancestors. They do not contribute to movement. But they do provide a valuable benchmark by which we can measure progress.

From my own somewhat biased vantage point, I have had no sense whatever of the equal and opposite danger of a too ready and uncritical acceptance of a new viewpoint.

As a result of such criticism, were I now so engaged, I would want to revise my contentions on two or three important points. I fear I did not make as explicit as I should the welfare criteria I was employing. In partial equilibrium situations, economics has long made the maximization of consumer welfare a nearly absolute goal. Any type of economic behavior which lowered the prices of products to the consumer, quality of course being given, is good. This standard weighs heavily on the conscience of the economist.

There is much history behind this standard. Economics originated in a world that was very poor—where bleak poverty was the normal lot of man and always had been. Increased real income of consumers was the simplest test of improved welfare. There was a strong pragmatic justification for this test and for a policy which justified no breaches. The particular could easily become the general and even the particular could not be afforded.

In our own time, however, we regularly reject the particular equilibrium test of maximized consumer well-being. We regularly accept measures which raise product prices to ameliorate the grievances or alleviate the tensions of some social group. And it is well that we do. An opulent society can afford to sacrifice material well-being for social contentment. Higher prices of coal or clothing we regard as a small price for freedom from disorder in the coal fields or destitution in the sweatshops.

I doubt whether, in entering a defense of the social utility of countervailing power, I made sufficiently clear whether my standard was the welfare of the consumer or the minimization of social tension. It was natural that perceptive critics would take up the attack on the test of consumer welfare. Had I been less under the influence of this norm myself I would have invited the battle in the area of social harmonies. This, I submit, is also the critical test. American society has not recently been threatened in peacetime (or even in wartime) by a shortage of food. There have been times when the tensions of the farming community were a threat to orderly democratic process. The evolution of countervailing power in the labor market has similarly been a major solvent of tensions in the last half-century. Most would now agree, I think, that this has been worth a considerable price.

I am also grateful to numerous critics for a second correction. I have argued that one important manifestation of countervailing power—different in form but not in kind from that exercised against the cartels by the great European consumer co-operatives—is that of the modern mass buyer. The gains from this bargaining by the chains, department store buying groups, the great mail order houses, and the like are, in turn, passed along to the consumer. The consumer, as a result, is in a far happier position than were he or the small independent merchant to bring his negligible bargaining power to bear on the characteristic market power of the large manufacturer or processor.

The gains from opposing mass retail buying to large-scale or oligopolistic production have, I think, been fairly generally conceded. The question has been asked, however, as to what eleemosynary instinct causes the gains that are won by the mass buyer to be passed along to the consumer. In my book I argued that it was the result of the shape of the production function in retailing. My critics have suggested that it is because retailing, the mass buyers notwithstanding, is still a competitive industry. (It is likely to remain one, for entry is almost inherently easy.) I suspect they are right. I am sure that I was more than a little reluctant, at this particular stage in my argument, to confess a reliance on competition. After all, it is a bit embarrassing after one has just murdered his mother-in-law to disinter the lady and ask her to help do the cooking.

## IV

I come now to some critical views which I regard with somewhat less sympathy. There are first the professional protectors of scholarly virtue in our subject. These are the men who remind us that we have said nothing new—that it is all to be inferred from the writings of Aristotle, St. Thomas Aquinas, Adam Smith, and the late John R. Commons. I shall pass these critics by. These are times, I understand, when men are fired if they can be shown to have lost their humility.

There are also the self-designated protectors of our political morality. They detect in such a concept as countervailing power the evidence of a hidden and insidious design. Their evidence may be indistinct, but their knowledge of motives is unerring. I have been amazed at some of my motives. I have been detected as supplying a mask for monopoly and a rationale for big business. (That was an economist in the *Nation.*) I have also been constructing an apologia for the New Deal and the welfare state. (That was another economist, *sic,* in the *Chicago Tribune.*) Perhaps we should be grateful for these men and to the scholarly journals in which they speak. They warn us of bad intentions and evil plots of which we are not aware. They protect us from guilt by innocence.

There have been two less romantic criticisms which I am obliged to take more seriously.

The first of these concedes the reality of countervailing power but holds that its manifestations are imperfect. It can be circumvented by vertical integration or defeated by inflation.

This I readily concede, and I am only surprised that the point should be advanced in criticism either of my book or the concept. As with competition, the role of countervailing power is uneven, as I have been at pains to make clear. The extent of its effect is essentially, as with competition, a quantitative matter. Apparently our tradition in economic analysis does not allow us to construct partial models of this sort. They must be complete, self-consistent, and harmonious. If the model-builder does not make this claim, then his critics will assume that he does anyhow and then isolate the imperfections as proof of weakness.

I have been especially struck by this mental habit as it bears on my analysis of countervailing power and inflation. An economy characterized by countervailing power seems to me especially susceptible to inflation. Then, as the demand functions become generally inelastic, there is an opportunity for coalitions between those whose interests are otherwise opposed in bargaining, and the inflationary process is accelerated. Countervailing power dissolves as a regulatory force and it is for this reason—and in a manner quite consistent with what we would expect from our a priori view of regulatory process—that there is a tendency at such times to turn to state regulation of prices and wages to fill the regulatory void. It is significant that it has been in periods of inflation rather than deflation that the American and other similar economies have been made subject to a system of comprehensive government regulation.

In making this clear I seem to have invited—in this case even from such a perceptive journal as the *Economist*—the charge that my argument is weak. In conceding the imperfections or malfunctioning of countervailing power I am apparently made responsible for it. Such criticism, in effect, requires that the social phenomenon described be both universal in application and socially benign in effect. This is silly.

## V

Many, although not quite all, of those who have followed me through the concept of countervailing power would appear to agree that, given a strong position of market power, an answering position is desirable—that it contributes to social stability and perhaps also to economic efficiency. But a good many have, it is certain, been honestly appalled by this solution. It seems, in the first place, to legitimatize market power. To many of us the notion that one individual shall be in position to control the real income of others remains more than slightly obscene. We react to it much as a Puritan to Professor Kinsey—adultery exists no doubt, but how much better not to talk about it.

The further notion of a society which finds its equilibrium in a struggle between organized power groups is also unattractive—and such an equilibrium must look inherently unstable.

Finally, there is a suspicion that the concept of countervailing power will somehow provide an excuse for abandoning antitrust enforcement. In recent times we have had quite a number of quite ingenious arguments for ditching the antitrust laws. Is this another?

These arguments—one will find them persuasively advanced in Professor Adams' interesting article in the current *Quarterly Journal of Economics*—are not without point. If economic power could be totally mitigated by law, a hope that is at least implied by Professor Adams, the case against accepting countervailing power as a fact of life might be strong. However, the practical question is, what is practical? We know—and here our debt to our chairman, Professor Chamberlin, is great—that economic power in the economy is pervasive. It goes far beyond the limits set by the classical concepts of monopoly. It is an attribute of large-scale enterprise, the most striking characteristic of the American economy. Are we, by legislative and judicial action, going to work a revolution in the American economy? The answer is no.

The answer being no, we must then cherish the safeguards by which inherently weaker groups have found protection—labor from the perishability of its product and its unique compulsion to sell, the farmer from the tendency for the terms of trade to turn so adversely with any drop in demand, and so forth. This protection is not perfect. The economy is far more viable and its tensions are greatly alleviated because this protection exists.

This—as I have made clear—does not mean an end to the antitrust laws. It does suggest some discrimination in their use. In particular, it explains why we do not now apply them to unions and to agricultural price fixing where, implicitly at least, we recognize the role of countervailing power.

Unrestrained economic power is still an enemy of the good society. I only urge that we have a full view of the processes by which it is restrained.