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# Liberty versus Monopoly

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Over the last half-century, business interests and philosophical libertarians have formed a powerful alliance. Business leaders frequently claim to be libertarians and draw on the rhetoric of the free market to criticize government regulation. In turn, libertarians frequently defend businesses against what both groups see as an overbearing regulatory state. The connection is best represented by the Koch brothers, who call themselves libertarians and fund libertarian scholars through their foundation, and at the same time operate one of the largest businesses in the United States. Silicon Valley tech titans also frequently claim to be libertarians, and argue that their internet companies advance liberty by enabling people to communicate freely and form organizations while limiting the reach of government censorship and control.

Yet this alliance is one of convenience, not logic, and it is on the verge of collapse. As businesses expand and obtain monopoly power, they become threats to the values that libertarians hold dear. The business-libertarian nexus of the late twentieth and early twenty-first century is thus an aberration, with a brief history and no future.

Modern libertarianism developed from the classical liberal tradition of the eighteenth and nineteenth centuries. Both modern libertarians and classical liberals celebrated personal freedom and defended individual rights. But the classical liberals, from Adam Smith to John Stuart Mill, were hardly cheerleaders for business. Smith believed that merchants were naturally inclined to cartelize markets and fix prices and wages. He railed at the corporations of his time, the monopolies established by the British crown. Smith took the side of American revolutionaries who complained that those monopolies unfairly dominated trade, writing in The Wealth of Nations (1776) that, in the imperial system regulating colonial trade, the interest of consumers "has been sacrificed to that of the producer with a more extravagant profusion than in all our other commercial regulations."

By the time of J. S. Mill, the monopolistic tendencies of vast corporations were clear. Mill argued that they should be regulated or even nationalized. By the late nineteenth and early twentieth centuries, nothing was more obvious to economists than that monopolies were inevitable under the "laissez-faire" capitalism of the time. The fundamental problem was that private property (especially over critical pieces of land), combined with the productivity gains typically associated with the geographic concentration of commercial activity in prosperous cities or along crucial railway lines, tended to create monopoly power for those who owned these critical assets. This made monopoly inevitable if capitalists were allowed to freely coordinate and pool their assets.

Political economists blamed the resulting, massive levels of monopolization and corporate cooperation—exemplified by the great trusts—forimmiserating workers, destroying small businesses, overcharging consumers, and corrupting the government. The only question was what to do about the problem.

Much of the most important analysis of monopoly was conducted by the successors of Smith and Mill. William Stanley Jevons and Léon Walras, who launched the "marginal revolution" in economics, reviled monopolies. So did Henry George, an immensely influential journalist, political economist, and close friend of Walras, whose best-selling book Progress and Poverty inspired the Progressive movement in the United States. This new generation of political economists saw monopolies as an oppressive form of centralized authority, just as libertarians today see the state. As George wrote, "The accumulation of large amounts of capital under consolidated control creates a new kind of power. . . . Power from accumulation is destructive. It is often exercised with reckless disregard, not only to industry but to the personal rights of individuals." Indeed, the political economists of that era made the parallel explicit by noting that the markups charged by monopolies on consumer goods, and the "markdowns" on the wages they paid, were conceptually no different from taxes.

Perhaps the most eloquent summary of this connection came from the Ohio Republican senator John Sherman, follower of the great political economists of the late nineteenth century. In defending the Antitrust Act that bore his name before Congress, Sherman argued, "Monopolies are inconsistent with our form of government. . . . If we will not endure a king as a political power, we should not endure a king over the production, transportation, and sale of any of the necessaries of life. If we would not submit to an emperor, we should not submit to an autocrat of trade."

**Classical Liberal Opposition to "Monopoly Taxes"**

To understand this logic, we need to recall the classical liberal objection to the taxation of labor. Classical liberals believed that taxing labor income (or consumption) discouraged work. Since workers dropped out of the workforce or cut back on effort in response to taxes, taxes caused the economy to perform below its potential. Classical liberals also believed that labor income taxation was unjust because it denied workers their natural reward.

Now imagine that rather than imposing a tax on income or consumption, the government creates a cartel of all the businesses in each industry and induces them to raise their prices, while skimming off the difference between this elevated monopoly price and the competitive price as government revenue. This "markup" would be effectively the same as imposing a tax on consumption. In fact, liquor monopolies that many states use as an alternative to taxing alcohol function almost precisely in this manner. Jevons, Walras, and George noted that private monopoly does essentially the same, except that rather than this tax being paid openly into public coffers, where it can be used for the public good, it accrues more discreetly into the pockets of the private monopolist. To quote George again:

Certain forms of monopoly exercise powers analogous to taxation, and may be treated likewise. . . . When the king granted his minion the exclusive privilege to make gold thread, the handsome income enjoyed as a result did not arise from interest on capital invested in manufacturing. Nor did it come from the talent and skill of those who actually did the work. It came from an exclusive privilege. It was, in reality, the power to levy a tax (for private enjoyment) on all users of such thread.

Something similar can happen in labor markets. Suppose that the government organized all employers into a cartel which held down workers' wages, and that the government taxed the employers on their labor savings, pocketing the "markdown" between these newly depressed wages and the competitive wage as revenue. This is functionally the same as a labor income tax. And in the same way, if, even without government involvement, employers are able to enter cartels, or use their unilateral dominance in labor markets to suppress wages, the wage suppression that is felt by the worker is the same as a labor income tax, except now the "tax" revenues go to the employers rather than to the government. Rather than "monopolists," employers who act this way are "monopsonists"—a phenomenon highlighted by Beatrice and Sydney Webb in the 1890s and named by economist Joan Robinson in the 1930s. But the logic is the same. To roll back the consumption and labor taxes imposed by private monopolies and monopsonies, respectively, Jevons, Walras, and George advocated attacking a wide range of monopolies and helped inspire the antitrust laws promulgated by lawmakers like Senator Sherman.

Thus, as the nineteenth century rolled into the twentieth, the dominant view of the newly emerging profession of economics was that government and business posed a threat to liberty—the liberty to earn and live off a fair wage. Of course, these economists did not oppose business any more than they opposed government; small businesses operating in competitive markets were fine. Rather, they believed that the government should refrain from creating monopolies itself, prevent firms from assembling monopolies through mergers, and punish (or regulate) those businesses that obtained monopolies through other private actions. These economists would not have been impressed with the modern libertarian view that the government should keep its hands off business. The entire experience of laissez-faire capitalism in the nineteenth century contradicted such a view.

### The Misguided Embrace of Monopolies

All of this changed with the rise of Communism, especially in the wake of World War II. With the growing prestige of government planning, whose merits seemed, at the time, to have been vindicated by the rapid economic development of the Soviet Union and the success of war planning in many countries, defenders of individual liberty turned their attention back to the dangers of state power. Soviet and Nazi totalitarianism was a far greater threat to individual liberty than the economic behavior of private businesses could ever be. Liberals of the time feared that the attractions of statism—that it seemed to promise organized economic growth while protecting people from the hazards of capitalism—would reconcile people to the loss of individual liberties. In their increasing isolation, liberals saw business leaders, and especially financiers, as natural allies in the fight against statism. As Angus Burgin documents in The Great Persuasion (Harvard University Press, 2015), his magisterial history of the rise of "neoliberalism," business leaders saw the theories of thinkers like Friedrich von Hayek and Milton Friedman as the most potent antidote to burdensome state regulation. To help spread their ideas, the business leaders poured money into foundations and other organizations that supported them.

The most potent outgrowth of this development was the school of economic thought that originated at the University of Chicago, to which both Hayek and Friedman contributed. But the most important figure in that school for the theory of monopoly was a less well-known economist named Aaron Director. Director founded the "Chicago School" of antitrust, which argued that private monopolies and cartels were naturally unstable, and for that reason antitrust enforcement could, and should, be scaled back.

Director's arguments were effective for two reasons. First, he (and his followers) pointed out that the government's legal theories about the problems posed by monopolies, which had been mostly accepted by the courts, were a mess. Courts had agreed that certain common business practices—for example, "resale price maintenance," where a manufacturer of a product would mandate a minimum price at which that product could be sold—were almost certainly monopolistic, when in fact it was possible to justify them with quite innocent explanations. The courts' lack of economic sophistication led to poorly reasoned judicial opinions that were easy targets for a clever economist.

Second, when Director developed his ideas, in the 1950s and 1960s, it seemed plausible that the monopoly problem had largely been contained. The big trusts were gone. Many industries—banking, for example—were highly fragmented, even more so than in other countries. A recent study finds that during this period the "tax" attributable to market power (i.e., the markups made possible by a lack of competition) on the economy was roughly 20 percent, low by historical standards, while all told government taxes were about 35 percent and much higher on the highest incomes. Thus, to an economist, the major threat to liberty in the form of a "taxing power" was government, not private business, at this time.

Director and his followers made a crucial mistake, however. They attributed the weakness of monopoly to the inevitable laws of capitalism. Chicago School economists like George Stigler proposed theories that explained why cartels were hard to form and inherently unstable. But the healthy market of that period was created by vigorous government enforcement that picked up dramatically during

Franklin Roosevelt's New Deal. It's as if the economists looked at a low-crime city like New York today and concluded that, because crime is low, a police force is not needed.

This was not a mistake that an economist writing in an earlier era would have made. Indeed, the early Chicago School economist Henry Simons, writing in the 1930s, advocated A Positive Program for Laissez-Faire, in which vigorous antitrust policy would make a competitive free market economy possible. Yet this sat uneasily with a fear of government power. How could we depend on a powerful government to maintain a free market while at the same time claiming that powerful governments posed a threat to liberty? Director's claim about the relative unimportance of monopoly largely resolved this dilemma. Friedman, one of Simons's students but Director's son-in-law, embraced the latter's views in Capitalism and Freedom, writing "I am inclined to urge that the least of the evils is private unregulated monopoly. . . . Dynamic changes are highly likely to undermine it." Friedman was thus able to overcome his own earlier anxiety about the problem of monopoly and make his name as the founder of contemporary libertarianism or what some call, often derisively, "neoliberalism."

It was this resolution of what one might call the paradox of libertarianism—that otherwise a strong state is needed to maintain a free market—thatmade the libertarian creed irresistible to big business. If monopoly is naturally unstable, but government power durable, then antitrust law and other forms of regulation can be scaled back, and the focus placed on attacking government power. Hence the alliance between big business and libertarianism.

#### Threats to Markets from Reduced Competition

This alliance led to a decline in antitrust enforcement. Chicago School economists and their followers in law schools convinced the Supreme Court to cut back on earlier legal precedents that had blocked monopolization. These ideas also made their way into the Reagan administration, which started a trend toward weaker enforcement of the antitrust laws by the government antitrust authorities, the Department of Justice and the Federal Trade Commission.

Most important was what Jacob Hacker and Paul Pierson have called "policy drift": the failure of regulatory enforcement to respond to changes in the activities of those being regulated. Over this period, important new threats to competition—and important new forms of the agglomeration feared by classical political economists—emerged. Market power over labor markets soared while the power of unions declined. Institutional investors came to increasingly control and coordinate the corporate economy. Tech giants blossomed based on their control over network effects. And antitrust policy watched from the sidelines.

These developments combined to produce a massive decline in competition, especially in new and growing areas of the economy such as finance and technology, setting the stage for a reprisal of the Gilded Age. A recent study finds that the "monopoly tax" on the economy has risen from about 20 percent, or half the tax imposed by governments in the 1950s and 1960s, to nearly 70 percent today—more than twice the tax imposed by governments, which shrank slightly over this period due to the influence of libertarians. While other studies have found a more modest increase, a wide range seem to agree that the monopoly tax is exploding far faster than government taxes are contracting.

Shareholders benefited from the monopoly tax and the resulting explosion in stock market values at the expense of the rest of society: consumers paid higher prices, and workers were paid lower wages. Most people do not own much stock: less than half the population has any at all, and 81 percent of stock is owned by the top 10 percent of stock owners. Thus the boom of the stock market and the stagnation of wages has widened inequality, leading to many of the ills of our day. It's as if the government enacted a policy of taxing workers and consumers and redistributing to the rich—but through the mechanism of weaker antitrust enforcement.

The most striking area in which market power has grown is the least familiar to students of antitrust: the power that employers have over workers. That monopsony power can be a greater threat than monopoly power is mostly common sense. Consider a typical purchase you make and how many reasonable alternatives you have. Even in a relatively concentrated industry like automobiles, you can choose among a dozen or so manufacturers. Thus, if the price of a car increases by 5 percent, you can probably select another car. For most consumer products the choice is probably between five and ten options. In contrast, after people initially choose a job, it is hard to switch to a new job. If wages decline by 5 percent, most workers would complain but not leave their jobs. Thus, it is obvious that labor markets are far less competitive than product markets are.

Economic theory also gives an elegant explanation: competition in product markets is defined by the range of options a consumer is willing to consider. Competition in labor markets, however, is defined by the range of jobs a worker is willing to consider, but is further narrowed by the fact that firms are only willing to employ workers they find qualified and compatible with the rest of their workforce. This "double coincidence of needs," what economists call "matching," makes labor markets inherently thin. Contemporary antitrust policy, however, under the influence of the Chicago School's focus on consumers and business groups hostile to labor, has almost completely ignored employer power over workers as a target for antitrust policy. There are very few cases, and very few enforcement actions, involving an effort to punish employers who enjoy market dominance over their workers and underpay them as a result. A series of recent economics papers suggests that labor market power has become far more important than product market power, not just because of the inherent features of labor markets but also because the cops have been off the beat.

This is just one area of market power that has blossomed while enforcers slept. At the same time, institutional investors like BlackRock, Vanguard, and State Street have come to control almost a quarter of the corporate economy. They are four of the five largest shareholders of almost every major public company. Being perfectly diversified, they have no interest in seeing these companies compete for consumers or for workers. This is perhaps the most extreme monopoly capitalism has ever seen, yet antitrust enforcers have done nothing about it. And then there is the enormous, growing, and almost completely unchecked power of the technology platforms, such as Facebook and Google.

None of this would have surprised the classical liberal political economists, or their successors in the late nineteenth and early twentieth centuries, who vigorously fought against the power of corporations over workers and feared the agglomeration of capital, whether through finance or networked concentration of power in railroads and cities. The question is, now that we have been reminded of their wisdom, what is to be done?

### Addressing Today's Challenges

Our first point is that philosophical libertarians need to withdraw their support for big business, which has given monopolists the ideological cover that has kept the courts and government enforcement agencies at bay. If libertarians are true to their commitment to economic freedom, then they must fight for vigorous antitrust enforcement.

Fortunately, some tentative steps are being taken in this direction. Federal and state antitrust authorities have begun to take seriously the problem of labor market monopsony. When it was revealed that Jimmy John's, a sandwich restaurant chain, required their sandwich-makers to sign covenants not to compete—which restrict their ability to find new jobs if they quit—the government sued and forced the company to abandon this practice. But antitrust authorities must go further: mergers should be reviewed for their effects on labor as well as product markets. A wide range of anticompetitive practices in labor markets, from no-poaching agreements to recently documented efforts by large purchasers to suppress the wages of their suppliers, must be investigated.

Enforcement against institutional investors and the technology platforms is similarly missing. Institutional investors holding large chunks of the economy should be prohibited from fully diversifying their investments within industries. Nearly all valuable diversification is possible by holding just one company in each industry, and this would ensure investors have strong incentives to induce competition among the companies they hold. It would also reinvigorate serious corporate governance, as asset managers would be forced to emphasize quality of management in their portfolio companies rather than free-riding on and simply mimicking the overall market. Substantial progress could also be made in restraining the power of technology giants simply by preventing them from swallowing whole so many of their nascent rivals, as Facebook was allowed to do with Instagram, Google was allowed to do with Waze, and Microsoft was allowed to do with Skype.

Yet while great progress is possible, there are limits to how much a purely antitrust-based approach can or should do. Antitrust enforcers are not and should not become regulators: to remain legitimate and avoid becoming a lever for political manipulation of industry, antitrust must adhere to relatively transparent and economically grounded standards. It also must not hamper the economy by breaking up firms that are truly more efficient based on their scale, as Robert Atkinson and Michael Lind highlight in their book Big Is Beautiful: Debunking the Myth of Small Business (MIT Press, 2018). This means that restraining corporate power requires complementary approaches, especially in the case of the technology companies that harness powerful network effects.

Simply nationalizing or regulating such industries is anathema to libertarians, as it would replace one overbearing monopolistic power with an even more iron one. While it may be necessary in some limited cases, a more promising strategy, wherever possible, is to foster countervailing sources of power in the private sector that can balance the power of the network-effects-driven monopolies of today. Unions, farmer granges, artist royalty agencies, and diverse other intermediate-sized organizations served this role in the industrial era. A new “data labor movement” is critical today: its goal should be to help those who create the inputs to the digital economy that are the basis of increasingly sophisticated artificial intelligence systems bargain for the wages they are presently denied. Such a movement could also help workers whose jobs are threatened by the very technologies their digital inputs created. In addition, data labor unions could help ensure data quality without relying on overbearing platforms for censorship, and they could manage user attention without asking platforms to curate our daily experiences.

Legal changes will be important to foster such a movement, and help support the power of more traditional unions in the areas of the economy where antitrust alone is insufficient to confront the monopsony power of the largest companies. Antitrust and labor law are complementary tools to check monopoly power, just as limits on state authority and checks and balances within that authority are complementary tools to avoid government tyranny.

Libertarians must move beyond the mid-century mistakes of neoliberalism in the mold of Freidman and rediscover the insights of Henry George and Léon Walras. They should apply their tools with the same vigor against all concentrated sources of unproductive and illegitimate authority. They must recognize the threat that monopolies pose to individual freedom, and muster the political will to unite with other opponents of corporate power to meet this threat. The next great fight for individual autonomy against centralized power has begun, and libertarians must not remain stuck fighting the last war, oblivious to today's enemy.

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