

# Robust political economy: The case of antitrust

Stefan Voigt\*

© Springer Science + Business Media, Inc. 2006

**Abstract** The notion of robust political economy is applied to antitrust. It is argued that the universalizability of policy rules is crucial if both the knowledge problem and the incentive problem in antitrust are taken seriously. Policy recommendations of Williamson are compared with those of Hayek. It is further argued that the notion of universalizability is central not only with regard to antitrust but also with regard to a host of other policy areas.

**Keywords** Antitrust · Knowledge

**JEL Code** B52, B53, D02, D80, K21, K40, L40.

## 1. Introduction

The concept of “robust political economy” has recently been proposed by Boettke and Leeson (2004). They call a theory robust if its policy implications are not sensitive to specific assumptions being fulfilled. They identify two general criteria that all policy-relevant theories would have to cope with namely (1) the incentive problem and (2) the knowledge problem. The questions that a robust political economy would have to pass are: (1) do the policy implications still hold if we assume less than benevolent decision-makers and (2) do they still hold if knowledge in a particular case is limited, asymmetrically distributed etc.?

In this paper, the notion of robust political economy is applied to antitrust or competition policy. From a liberal perspective that is based on the assumption that a functioning market can help us deal rationally with both incentive as well as with knowledge problems, this is a pertinent question as antitrust institutions belong, at least potentially, to those institutions that

---

\*The author thanks his collaborators Lorenz Blume, Kim Eun Young, Janina Satzer and Michael Seebauer as well as Anne van Aaken for helpful comments and suggestions.

---

S. Voigt (✉)  
Professor of Economic Policy, Economics Department, University of Kassel, Nora-Platiel-Str. 4,  
D-34127, Kassel, Germany  
e-mail: voigt@wirtschaft.uni-kassel.de.

are set up and enforced by the state in order to safeguard the proper functioning of markets. Hence, it is one of the instances in which the visible hand of the state is often believed to be needed in order to enable the invisible hand of the market to function more effectively. Applying the notion of robust political economy to competition policy is also interesting as the European Union as well as some of its member states have recently declared that they want to reform their competition policy towards a “more economic approach” (European Commission 2001, Monti 2002) which explicitly takes economic models into account—and leaves, correspondingly, less room for general rules. It is hence timely to discuss whether such a more economic approach passes the robustness test.

It will be argued here that implementation of a “more economic approach” does often not pass the robustness test. Many industrial organization models crucially depend on some very sensitive assumptions being fulfilled. In line with robust political economy, it is thus argued that the recent trend in European competition policy is rather problematic. Of course, the notion of robust political economy can be applied to a host of other policy areas some of which will be shortly alluded to in the section on more general policy implications.

The rest of the paper is organized as follows: the next section tries to develop the notion of robust political economy in a little more detail. Section three contains the application of the notion to antitrust policy. Section four discusses some other policy areas and section five concludes.

## 2. Robust political economy—A subjective primer

A market economy is best described as a system of decentralised exchange in which often millions of actors participate who are free to set their own goals. Ideally, exchange based on voluntarily entered-into contracts indicates that the parties involved expect to be better off as a result of the contract, otherwise they would not have consented to it in the first instance. But some contracts that make the participating parties better off might have welfare-reducing effects on other, third parties. Contracts might also be the result of asymmetrically distributed bargaining power e.g. due to monopolistic positions. From an economic point of view, the function of legislation in a market economy consists in (a) making welfare-enhancing exchange as easy as possible, and in (b) making welfare-reducing exchange as difficult as possible.

Properly functioning markets generate incentives for all participants to behave in ways that will also increase the welfare of others—although this is only the unintended consequence of the actions of those participating in the market. In order to function properly, markets need to be based on some rules that make welfare-enhancing activity more attractive and welfare-reducing activity less attractive. Even when the rules that constitute markets are in place and are factually enforced, there might remain the necessity for additional action in areas where markets are believed to fail, i.e. in the provision of public goods, regulation of natural monopolies or the problem of asymmetrical information. Yet, not only markets can fail but also states. Before the state is empowered with some task, the costs and benefits of state action should be compared with those of the market solution, no matter how “imperfect” that might be. At the end of the day, a number of tasks will be allocated to the state, because markets consistently fail *and* the state can be expected to do a better job than the (failing) market. In order to ensure that state action does not result in even larger failures, adequate institutions and measures need to be taken.

It is here that robust political economy comes in. It posits that institutions should be established such that the probability of state failure is minimized. These institutions should

constrain government representatives who are not benevolent in such a way that they cannot do much harm although they only strive to maximize their own utility. Institutions should further constrain government representatives if they possess only limited information. It is argued here that universalizable rules are the single most important tool towards a robust political economy. The concept of universalizability can be traced back at least to Kant (1797/1995). It became influential among economists after it had been taken up by Hayek (1960, 1973) who argued that rules ought to be (i) *general*, i.e., applicable to a multitude of cases in which a multitude of actors will be engaged, (2) *abstract*, i.e., are formulated negatively and thus not prescribing a certain behaviour but simply prohibiting a finite number of actions, and (3) *certain*, i.e., interested individuals can know whether a certain action is within the legal domain or not. It can be argued that for Kant, a fourth trait came in namely that universalizable rules could be *justified* to anybody who was supposed to live under them. Neither Kant nor Hayek used the terminology of robust political economy. Yet, it can be argued that the two central problems identified by Boettke and Leeson, namely decision-makers who are not necessarily benevolent and do not necessarily dispose of complete information can best be dealt with by setting up meta-rules that force them to rely primarily on universalizable rules as a government instrument. Both meta-rules and (universalizable) rules are defined by way of their form—not of their substance. It could be argued that this might be a necessary condition for robust political economy, but could not possibly be a sufficient condition. Yet it is argued that universalizability is a sufficient condition: if—thanks to the generality characteristic—all legislators will be subject to the rules they pass, this is sufficient incentive to secure that they will not pass laws that are detrimental to large parts of the population.<sup>1</sup> The meta-rules which are to secure that all new legislation abides by the characteristics of universalizability, are part of the constitution, whereas the production of universalizable rules itself occurs on the post-constitutional stage. A constitution that contains legislatures in such a way would have a number of advantages that we now turn to (see also Buchanan and Congleton 1998).<sup>2</sup>

- (1) If the constitution factually constrains non-benevolent decision-makers to enact only legislation that passes the universalizability test, legislation will be more transparent because legislation promising special treatment to specific interest groups will be impossible; loopholes and other transparency-reducing measures will be excluded. The increased degree of legislative transparency will lead to a higher degree of knowledge among the population at large concerning the content of legislation. This will, in turn, increase the accountability of the legislators.
- (2) Universalizable rules also make rent seeking less attractive. If there are general rules it is less likely that interest groups will be able to receive privileged treatment which is often to the detriment of society at large.
- (3) General rules will lead to a high degree of predictability of state decision-making which enables private parties to make more reliable plans for the future. Predictability can be defined as the capacity to make predictions concerning the actions of others that have a high chance of turning out to be correct. It could be argued that general rules would allow for a high degree of discretion in the implementation of rules, yet the more general a rule is, the less uncertainty will there be in linking a specific case to a specific rule.

<sup>1</sup> A necessary assumption of this conjecture to hold is that the legislature represents all walks of life present in the entire society.

<sup>2</sup> For the moment, the question who is to secure that politicians play by the rules of the constitution need not concern us.

Given that universalizable rules have so many advantages, why would we want to use any other kind of governmental decision-making? In other words: what are the limits of their application?

The generality trait of rules means that they are applicable to a great many interaction situations. This implies that one single rule is used to structure interaction situations that are not perfectly identical but that only share some substantial commonalities. The question is whether rules can ever be too general. This could imply that the principle of equality is violated according to which like cases are to be treated alike—but cases not identical are not to be treated alike. These questions have, of course, been discussed for a long time, but remain unsettled until today. In his *Law of the Constitution*, Dicey (1885/1982, 152ff.) compares the way in which the freedom of the press is guaranteed in England with the way it is guaranteed in France. He observes that the French have a special law whereas in England, a special press law is superfluous as the freedom of the press is just one particular way of realizing one's freedom of speech, special rules would hence not be necessary. Easterbrook (1996) argued against specific property rules for cyberspace reminding us that there is no "Law of the horse".<sup>3</sup> Mahoney and Sanchirico (2005) show that general rules for the regulation of various branches can maximize welfare because the influence of particular industries requesting specific rules that are in their private interest can be constrained. Their argument is based on the insight that so-called first-best regulation depends on the availability of information with the regulators, that often only the regulated dispose of. They thus reach their solution—general rules—as a consequence of the asymmetrical distribution of information, the second of the two basic problems dealt with in Boettke and Leeson (2004). Yet, the need to have regulation that only applies to a limited number of industries shows that general rules applying to all industries are considered to be too general.

Some of the interactions between the state and the citizens cannot be structured according to the notion of universalizability: If a citizen owes the state a certain amount of taxes, the amount should be calculated on the basis of general rules, yet the request to pay them will be rather concrete, and hence not in accordance with the trait of abstractness. Universalizability is thus difficult to apply to much of public law, i.e. the law structuring the interactions between the state and the citizens. Yet, it can be argued that even where the state interacts with citizens bilaterally as in administrative law and makes very specific commands, these ought to be based on general rules. Hence, even in these areas of law, the generality trait is of overwhelming importance.

In the next section, we ask what the notion of robust political economy could imply for antitrust policy.

### 3. Robust antitrust policy

As already pointed out in the introduction, antitrust is chosen as an area to which the notion of robust political economy is applied because (1) it is conventionally argued that competition needs to be safeguarded by the state and (2) the European Commission has been trying to move towards a "more economic approach", probably implying less reliance on universalizable rules. It is impossible to deal with all the relevant problems of antitrust policy here. We develop our argument mainly with regard to merger policy as one of the most visible (and more controversial) areas of antitrust. In order to highlight the policy relevance of our topic, we begin this section by referring to the debate currently taking place in the European Union.

<sup>3</sup> Meaning that if I want to buy a horse, general contract law will do—and no special "law of the horse" is needed.

In a number of statements (e.g. European Commission 2001, Monti 2002), the European Commission has emphasized that it strives for a “more economic” approach in its competition policy. Supposedly, this is to mean that recent theorizing in industrial organization ought to be integrated into competition policy. The recognition that a merger can have non-coordinated or unilateral effects to the detriment of effective competition is such a new insight that the Commission wants to cover.<sup>4</sup> “Economic” can mean different things here, namely (i) that the reasoning is based on economic models, (ii) that the resources needed to implement the policy are fewer than drawing on other, “non-economic” approaches, or (iii) that competition policy aims at explicitly recognizing its general consequences on welfare.

We wish to argue that a truly “economic” approach should encompass all three elements whereas the approach chosen by the Commission has its primary focus only on the first of these three aspects. Economic models are often very sensitive to the assumptions made. Models that are theoretically convincing due to their consistency and elegance might be difficult to apply in practice as the identification of certain crucial variables might be difficult or even impossible. Moreover, they might only cover part of the picture and leave relevant actors unmodelled as this would introduce too much complexity. Lastly, models are subject to business cycles, too: last year’s best-seller might be this year’s white elephant.

These objections contain already an implicit list of characteristics that economic models should fulfill before being applied to competition policy: (i) they should be rather robust to their assumptions, (ii) relevant variables should be attainable without many complications, (iii) the empirical evidence in their favor should be rather undisputed, (iv) they should have survived for a number of years, and (v) their reasoning should be widely accepted.

Even if all these requirements are met and the potential benefits of drawing on these models in merger policy seem substantial, a truly economic approach would still require that the potential costs be weighed against the potential benefits. Applying economic models will often mean having to draw on input by economists. The resources necessary to administer an “economic” approach might thus be higher than of administering a “non-economic” approach. The general insights regarding predictability that were developed in the last section will be shortly spelled out with regard to antitrust policy. It will be shown that flexibility is not necessarily a blessing as a high degree of flexibility will often be accompanied by a low degree of predictability. Before hastily applying economic models, the costs of unpredictability better be taken into account. It might well be that potentially welfare enhancing mergers are not initiated due to the fear that they could be prohibited. This could cause substantial costs to the society drawing on “more economic” approaches.

Merger policy is about classifying notified mergers into one of two groups: they are either compatible with the relevant notion of competition or they are not. If they are, they can be consummated, if they are not, their consummation is prohibited. The criterion according to which notified mergers are classified in either of these two groups is thus the central element of merger policy. Its concrete institutional set-up will not only determine the ratio of allowed to prohibited mergers but will also influence the number and quality of the mergers notified to the competition authority as firms interested in merging will generate expectations concerning

<sup>4</sup> Unilateral effects arise when two or more closely competing products are brought under common ownership. They refer to the fact that the post-merger firm has an incentive to set higher prices even if the merger has no effect on the behaviour of the competing firms. Where a firm merges with one of its rivals, this may reduce the elasticity of the firm’s residual demand curve. In the pre-merger market, price increases by an individual firm will lead to a reduction in sales. Some of these lost sales will be transferred to the other merging party. Hence, the impact of the price increase on profits is potentially smaller after a merger because some of the lost sales are recaptured in higher sales of the other merging party. They are not to be confused with price effects resulting from monopoly power or collective dominance (Bishop/Walker 1999).

the probability that their merger will be deemed compatible with competition legislation. The number and quality of notified mergers is thus determined by expectations which are, themselves, based on the substantive test.

Lack of predictability in competition policy can be detrimental to the realisation of welfare gains. If market actors are uncertain as to what competition rules mean or how they will be interpreted by the competition authorities and/or the courts, a number of negative welfare effects can result: if market actors believe that a merger will not be cleared, mergers whose consummation would allow the realisation of efficiency gains will not take place. This means that productive efficiency is lower than it could be were the merger carried out. On the other hand, if market actors believe that a proposed merger will be cleared, they might already invest in the entity to be created as the result of the merger. Prohibition of a merger can, then, be interpreted as a case of disappointed expectations, or: unpredictability of the competition policy as currently implemented.

Decisions on single cases have effects that often go far beyond a single case: they are observed by a multitude of other actors and thus become precedent. Precedent that signals a tough stance on proposed mergers can also be a barrier to the realisation of welfare gains: potentially welfare-enhancing mergers might be discouraged by precedent right from the outset. As just pointed out, this will prevent the realisation of higher levels of productive efficiency. Predictability allows market participants to make predictions concerning the decisions of competition authorities that have a good chance of turning out to be correct. The existence of precedent as such is not sufficient to secure a high level of predictability. Rather, the criteria used by the competition authorities should be as clear-cut as possible. Additionally, the analytical tools used to translate criteria into operational data should be as transparent as possible.

Merger policy can, however, also increase uncertainty if competition authorities are granted too much discretionary power and if they draw on various economic theories eclectically. It has been shown empirically that the stability of the framework within which companies act is decisive for economic growth and development (e.g. Brunetti et al. 1997). This includes, of course, the predictability of competition policy. In this section, it has been argued that a “more economic” approach as currently postulated by the European Commission can increase uncertainty and lead to unwanted (economic) consequences. Until now, the notion of a “more economic” approach has not been dealt with in terms of robust political economy which is what we now turn to.

### Ignorance in antitrust

Robust political economy is interested in the identification of institutions that minimize the likelihood of state failure. In this section, we ask what that means for antitrust policy. More specifically, we will begin with the assumption that the incentives of those responsible for implementing antitrust policy (the “competition agency” for short) are not a problem which allows us to focus on the knowledge issue. We hence assume that the competition agency only commands incomplete knowledge. The knowledge of the competition agency is incomplete in various ways—and some of these will be pointed out more explicitly.

First of all, it seems to make sense to distinguish between nomological knowledge and situational knowledge. Nomological knowledge refers to general knowledge and is necessary for passing legislation, situational knowledge refers to knowing the initial conditions in a specific situation and is hence necessary when applying legislation to specific cases. Concrete policy measures can only be rational if both kinds of knowledge are present, at least to a degree. If we do not dispose of any nomological knowledge in the sense of “if and everywhere

when  $x$ , then  $y$ ”, it will be impossible to rationally choose an adequate policy. But situational knowledge is also indispensable: if we are not able to identify a situation  $x$  with sufficient certainty, we might end up using a policy measure that was adequate for different situations, but not for this one.

What about the availability of nomological knowledge with regard to antitrust, and what about the reliability of situational knowledge? Ever since Schumpeter (1942), the consequences of market structures on economic outcomes have been hotly debated. Schumpeter argued that intense competition which comes along with low market shares of the competitors and with low profits due to intense competition would not be conducive to high levels of Research & Development, which would, in turn, mean lower rates of innovation and, ultimately, lower growth. This argument has been picked up in some growth models recently (e.g. Aghion and Howitt 1992 or Aghion *et al.*, 2005). The theoretical argument is still contested and the empirical evidence highly ambiguous (Cohen/Levin 1989 and Rey 1997 are overviews). Yet, the Schumpeter hypothesis has had important policy implications as it has been used to justify the creation of national champions. Given that our nomological knowledge concerning the effects of market structures is everything but settled, rational antitrust policies will be difficult to achieve: if the optimal intensity of competition is unclear, then the market structure that competition policy should strive to bring about is just as unclear. Yet, some 90 states have passed general competition laws which could have effects on the ensuing market structures by prohibiting mergers, cartels etc.

Yet, this is not the only important lack of nomological knowledge that we face with regard to antitrust policy. A second area are the effects of various instruments used in competition policy: does it make any difference for economic development whether the consummation of mergers is only prohibited if they create or strengthen a dominant position or if they promise to substantially lessen competition? Does it make any difference whether an efficiency defense exists that posits that mergers that would have to be prohibited are allowed if they are expected to have offsetting efficiency effects? Does it make any difference whether firms wanting to merge can offer remedies in order to cure the expected negative effects of the merger? Does it make any difference whether cartels are prohibited *per se* or whether the potentially offsetting virtues are tested in every individual case? It is amazing how little nomological knowledge is available with regard to these questions.

But there is also a serious lack of knowledge regarding the relevant initial conditions, i.e. situational knowledge in our terminology: to give just one example, ascertaining the relevant market in a particular case is not self-evident. What is more, the competition agency often depends on the information supplied by the competitors under scrutiny, i.e. we face the problem of asymmetrical information. But the lack of situational knowledge cannot be reduced to a problem of asymmetrical information. Many competition policies depend on predictions, or rather evaluations, concerning some future developments. How large a market share will be three years from now, how many competitors will be in the market, how substantial the efficiencies to be reaped from consummated mergers are; these are all questions that cannot be answered with certainty by anybody, the participating firms included.

## Two competing views on how to deal rationally with our ignorance

Given that both the nomological as well as the situational knowledge fall far short of anything like complete or perfect knowledge how can we rationally deal with our ignorance? In the past, two approaches have paid special attention to such knowledge problems, namely market process theory—or Austrian economics—on the one hand and transaction cost economics

(TCE) on the other. Two leading representatives of these approaches (Hayek and Williamson) derive dramatically different policy conclusions and we deal with some of them here.

Representatives of market process theory would refrain from identifying some ideal result of the market process. Since market processes are open processes that discover us knowledge that would not be attainable were we to refrain from using competition (Hayek 1978), it is completely besides the point to try to identify any “ideal” results. Representatives of TCE would not refrain from some ideal result of competition, yet they would ask whether this ideal result should have any implications on real world policies. Ever since Coase (1964), representatives of this branch have argued in favor of comparative institutional analysis in which only factually realizable institutions are to be compared with each other. In this analysis, there is no place for institutions that would be ideal were the world a different place (or were our knowledge better than it actually is).

As a consequence of these reflections, Williamson (1996, 1995) introduced the term “remediableness” as a decision criterion into economics: “An outcome for which no feasible superior alternative can be described and implemented with net gains is presumed to be efficient.” His argument is, hence, that it is undue to leave questions of political enforceability aside. If the transaction costs that are the consequence of the currently valid institutions are so high that no other than the currently chosen policy is enforceable, then he calls this policy “efficient”. When deducing theoretical optima, economists often disregard the politically relevant restrictions which leads them to classify situations as “inefficient” even if they are not able to spell out any implementable improvements.

It seems to make sense to spell out some policy implications that representatives of both market process theory and TCE could presumably agree on:

- (1) Rules and their application by way of enforcement serve to channel the behavior of all actors concerned. Rules-cum-enforcement are good if interested actors are able to ascertain the legality (or illegality) of various kinds of behavior *ex ante*. Such rules promise to yield a double-dividend: they increase legal certainty on the one hand, and they reduce the number of cases that end up in court, thus reducing one kind of transaction costs.
- (2) No matter who decides on the implementation of a given rule (judges or bureaucrats e.g.), these decision-makers will always face the lack of situational knowledge. Hence, rules should be such that a serious lack of knowledge will not induce a high probability of making the wrong decision. Ideally, the implementation of rules would thus only depend on a very limited amount of situational knowledge.
- (3) As our nomological knowledge is severely limited, the nomological knowledge that enters into the rules is also severely limited. Hence, we simply cannot know the best rules. But as long as we can hope that our nomological knowledge could still increase, we have an interest in establishing meta-rules that would allow us to modify the rules as soon as superior nomological knowledge is available. This could mean various things: (i) it could mean that meta-rules only demand simple majorities for a change of the relevant rules. (ii) it could also mean that rules are formulated in a deliberately vague language that enable those who are to enforce the rules to take the increased stock of knowledge into account as soon as it is available.

These signposts make a lot of sense, yet their simultaneous implementation is impossible. Being able to improve competition legislation at low cost in order to be able to integrate improved nomological knowledge seems desirable, yet it reduces the predictability of competition policy and is thus in conflict with the first signpost. Hence, trade-offs need to be made.



Hayek (1964) argues in favor of *per se* rules. He admits that their use could imply that we refrain from using knowledge that we dispose of in a concrete situation but these disadvantages are outweighed by the higher level of general certainty. Williamson (1996) develops an alternative between “inflexible legal rules” on the one hand and “flexible legal process” on the other. The legal rules approach would assume the existence of nomological knowledge or, in his language, of “economic certitudes” (1996, 284): “The legal rules approach to antitrust enforcement assumes that the relevant economic theory is already in hand and is adequately understood by the antitrust authorities.” The legal process-approach, on the other hand, would come along with a desirable gradualism (ibid., 283): “Rather than assert false certitude, the legal process approach urges that complicated issues of economic organization that are poorly understood be accorded respect. The object is to move toward a progressively more informed disposition of the issues as the relevant theory is refined and implemented, . . .” Williamson explicitly argues against “excesses of simplification” (ibid., 287).<sup>5</sup> He hopes that the flexible legal process approach will lead to evolutionary assessments of a state-of-the-art kind (ibid., 296) instead of “dispositive pronouncements of a once-and-for-all kind.” Hayek recommends general rules as a consequence of our ignorance, Williamson believes that inflexible rules only make sense under situations of rather little ignorance.

What to do with these exactly opposing policy implications? Williamson stresses his evolutionary inclinations here. Hayek is, of course, also seen as an economist who always stressed processes and evolution. The differences in the policy implications can thus not be attributed to an evolutionary outlook as such. We have already seen the overwhelming importance that Hayek attributes to the universalizability of rules, which would lead to predictability without excluding innovations. *Per se* rules are a specific kind of universalizable rules. Implicitly, Hayek seems to assume that our (nomological) knowledge concerning the details of competition processes must always remain incomplete. This assumption must also hold for the meta-level, for which Hayek must also assume that we do not have good reasons to assume that our knowledge concerning ways how we could best cope with our nomological ignorance can be substantially improved. *Per se* rules can only be a rational answer to nomological ignorance if there are good reasons to expect that no better answers can be reasonably expected to come about.

Williamson, on the other hand, argues that it could be foolish to refrain from using knowledge that we might dispose of, at least in some cases. His recommendations concerning adequate instruments for antitrust policy seem to be based on the hope that we might be able to substantially increase our nomological knowledge concerning the functioning of competition and its effects on the economy at large. One crucial question that Williamson would have to answer is this: How can we know that we do know something new? To use an example dear to economists working within the transaction cost approach: the insights regarding the possible advantages of vertical integration that had been overlooked by more conventional scholars for decades did not arouse immediate consensus among all participants. Instead, it was some judges who argued along the lines of TCE (“Schwinn”).<sup>6</sup> In the meantime, some

<sup>5</sup> This argument is not directed against Hayek but against Frank Easterbrook. In order to be able to make newly gained knowledge policy-relevant as fast as possible, Williamson proposes to include the following introductory passage to legislation (ibid., 285): “Temporarily, pending further economic analysis and deeper understanding of the economic *institutions and practices* in question, the legal rule for dealing with this class of cases will be . . .”

<sup>6</sup> The issue was whether a producer of premium bicycles (Schwinn) could legally prohibit its dealers to sell its products to other outlets such as discount chains. The TCE argument in favor of making such vertical restraints legally possible is that this would enable the dealers to offer premium advice, to offer first-class repair services etc.

of the arguments advanced by TCE-scholars seem to be in retreat (see, e.g., Joskow 2002 who describes Post Chicago Antitrust).

Hayek and Williamson start with different assumptions regarding the question what can be known. Hayek can be considered a pessimist and Williamson an optimist. But this is not the core of the matter: Hayek argues in favor of general rules because we know so little whereas Williamson argues that it only makes sense to rely on general rules if we know quite a lot. Antitrust policy has been around for well over 100 years. Especially over the last 15 years, competition laws have spread everywhere, some 90 states now have such laws. But our nomological knowledge is still very scarce. Given that the issue has been on the research agenda for more than a century, the assumption that we will gain substantial empirical insights shortly seems rather daring. What is more, dynamic processes—such as competition—might simply not be subject to any clear-cut laws at all. Williamson's optimism thus seems unfounded, his condition for applying "inflexible legal rules" unreachable. But is this the end for inflexible legal rules? We claim that it is not.

Given that situational knowledge is asymmetrically distributed (as is, e.g., the case with regard to economies of scale), how much sense does it make to rely on models that are very sensitive to assumptions that cannot be known with any degree of certainty by the antitrust authorities? Given that the most adequate instruments of competition policy are not known due to our lack of nomological knowledge, how much sense does it make to want to apply fine-grained instruments? Given that our nomological knowledge concerning the entire competitive process is very restricted, how much sense does it make to want to interfere with the process in a discretionary way?

A recent survey of US antitrust policy (Crandall and Winston 2003, for an opposing view see Baker 2003) shows that it often did not reach its goals. U.S. antitrust policy has been around for well over a hundred years and its effects are still uncertain. This implies that Williamson's optimism is unfounded. If one puts heavy emphasis on the predictability of policies—as Hayek does—one has a strong case in favor of "inflexible legal rules" precisely because there is so little economic certitude.

### Self-interest in antitrust

Until now, our argument has been based on the assumption of incomplete knowledge (both nomological and situational) but benevolent competition agencies. To be really "robust", our policy implications should also hold if we get rid off this unrealistic assumption. This section develops some policy implications given that competition agencies are no longer assumed to be solely benevolent. Conventionally, "benevolent" representatives of government are defined as maximizing social welfare. Given that both nomological and situational knowledge are scarce, this is already no mean feat. Here, we deal with some additional problems, namely the incentives of competition agencies that might prevent them from acting such that welfare is maximized.

The behavior of competition agencies might also be driven by motives of personal income and (or) re-election. Personal income can be increased in a variety of ways including a favorable treatment of firms which they could honor by offering better paid jobs later on ("revolving door") or by paying bribes right away. Re-election prospects can be improved by prohibiting efficiency-increasing mergers that would, however, go along with substantial job-cuts. The question to be dealt with here thus reads: how can antitrust rules be specified such that non-benevolent decision-makers can only do little harm to the economy?

The answer promoted here is obvious: the antitrust rules should be as universalizable as possible. Rent seeking promises zero returns if lobbying groups do not stand a chance of

getting any tailor-made exceptions. The losses from rent seeking can thus be minimized by relying on general rules. As soon as branch-specific regulation is introduced, the regulators depend on the input of those to be regulated and they have incentives to lobby for rules that would maximize their individual advantage to the detriment of society at large.

#### 4. More general policy implications

The last section served to show that robust political economy applied to antitrust basically means “universalizable rules”. The question is: does this insight carry over to other policy areas? We will argue that it does. To do so, we begin with antitrust again and look into a couple of policy areas that are closely related to antitrust such as trade policy and industrial policy.

One crucial precondition for intensive competition to emerge is that market entry is not prohibitively costly. To a considerable degree, entry costs are determined by government regulation. It seems to make sense to distinguish between foreign and domestic aspects. If foreign firms can easily offer their products on the domestic market, a high level of competition should result. Openness and competition policy in the narrow sense should thus go hand in hand. In order to prevent all the negative effects of discretionary rules that have been mentioned in section two (lack of transparency, lack of accountability, lack of predictability, high level of rent seeking possibly combined with corruption) the rules according to which goods can be imported should be universalizable. Optimally, it should not even matter if goods are produced abroad or domestically as long as they are all subject to identical standards.

Regarding domestic barriers to entry mandated by the state, De Soto (1990) pointed to the importance of regulatory procedures as an impediment for many entrepreneurs to become legal. Governments that have an interest in strong competition should thus aim at making domestic entry easy implying that both the time and the monetary cost needed in order to become legal should be low. This will, again, be the result if market entry is not subject to a large number of special permits, licences etc. but if there is a simple way of getting one’s business legally started.

Barriers to exit can prevent a (potential) competitor from entering a market in the first place. They can thus constitute barriers to entry. Not all of these are determined by technology (the sunk cost argument), some are the effect of regulation. One relevant aspect is the governments’ willingness to let inefficient firms go bust. If politicians try to save even very uncompetitive large firms, this will prevent allocative efficiency from materializing which, in turn, will lead to lower growth rates. If governments have indeed saved technically bankrupt firms from bankruptcy in the past, this will induce firms at the edge of bankruptcy to invest resources into lobbying for a similar treatment. This does, however, only make sense if government has the capacity to do so, which is only the case if the government is not subject to universalizable rules: Saving particular firms from bankruptcy cannot be subsumed under general rules.

Industrial policy is often at odds with a policy in favor of competition. Whereas competition policy trusts in the incentives of the market actors as well as the invisible hand of the market itself, industrial policy is often based on the assumption that due to some market failures, the government could increase welfare by heavily influencing the structure of the market. Industrial policy is, however, subject to severe knowledge and incentive problems. For industrial policy to work, it must be assumed that bureaucrats have knowledge which is superior to those that the market actors possess. In addition, it must be assumed that they have incentives to use this knowledge to the benefit of their communities. Both assumptions are highly questionable, the empirical record of industrial policy is highly ambiguous, to say

the least. As industrial policy is at odds with both of the criteria of robust political economy, there is no place for it in a robust political economy world.

To sum up: this section does not contain an attempt to make a systematic case in favor of universalizable rules beyond antitrust. Instead, we have tried to show that policy areas closely related to antitrust should also be based on universalizable rules.

## 5. Conclusions and outlook

Many of the ideas discussed in this paper cannot claim to be novel. Indeed, most of the ideas discussed here under the heading of robust political economy have been discussed before, sometimes decades or even centuries ago.

Epstein (1995), e.g., is a sweeping argument in favor of simple rules that appears to be largely compatible with the notion of robust political economy. To date, most attempts to curb the complexity of rules in favor of more general and more robust rules have largely failed. In order to have more of an impact in the future, an important next step in the research program of robust political economy would seem to be to identify the interests in favor of ever less robust rules and the underlying institutional settings that allow these interests to carry the day. Spelling out the negative consequences of highly complex rules is only a necessary, but not a sufficient step towards improvement. In addition, the mechanisms that lead to ever more complex rules need to be understood before institutional proposals can be made that improve the chance of changing the trends toward ever more complexity.

## References

- Aghion, Ph., N. Bloom, R. Blundell, R. Griffith and P. Howitt (2005). "Competition and Innovation: An Inverted U Relationship." *Quarterly Journal of Economics* 120(2):701–28.
- Aghion, Ph. and P. Howitt (1992). "A Model of Growth through Creative Destruction." *Econometrica* 60(2): 323–51.
- Baker, J. (2003). "The Case of Antitrust Enforcement." *Journal of Economic Perspectives* 17(4):27–50.
- Bishop, S. and M. Walker (1999). *The Economics of EC Competition Policy*. London.
- Boettke, P. and P. Leeson (2004). "Liberalism, Socialism and Robust Political Economy." *Journal of Markets & Morality* 7(1): 99–112.
- Brunetti, A., G. Kisunko, and B. Weeder (1997). "Credibility of Rules and Economic Growth." *Policy Research Working Paper* 1760; The World Bank.
- Buchanan, J. and R. Congleton (1998). *Politics by principle, not interest*. Cambridge: Cambridge University Press.
- Coase, R. (1964). "The Regulated Industries—Discussion." *American Economic Review* 54(3): 194–7.
- Cohen, W. and R. Levin (1989). "Empirical Studies of Innovation and Market Structure." In: Schmalensee, R. and R. Willig (Eds.) *Handbook of Industrial Organization* Volume II, pp. 1060–1107. Amsterdam et al.: North Holland.
- Crandall, R. and C. Winston (2003). "Does Antitrust Policy Improve Consumer Welfare? Assessing the Evidence." *Journal of Economic Perspectives* 17(4):3–26.
- Dacey, A. (1885/1982). *Introduction to the Study of The Law of the Constitution*. Indianapolis: Liberty Fund.
- Easterbrook, F. (1996). "Cyberspace and the Law of the Horse." *University of Chicago Legal Forum*, 207–16.
- Epstein, R. (1995). *Simple Rules for a Complex World*. Cambridge, MA: Harvard University Press.
- European Commission (2001). "Green Paper on the Review of Council Regulation." (EEC) No. 4064/89 COM (2001) 745/6.
- Hayek, F. (1960). "The Constitution of Liberty." Chicago: University of Chicago Press.
- \_\_\_\_\_. (1964). "Kinds of Order in Society." *New Individualist Review* 3(2): 3–12.
- \_\_\_\_\_. (1973). *Law, Legislation and Liberty*, Vol. 1: *Rules and Order*. Chicago: University of Chicago Press.
- \_\_\_\_\_. (1978) "Competition as a Discovery Procedure." In: F. A. Hayek (Ed.) *New Studies in Philosophy, Politics, and Economics and the History of Ideas*, pp. 179–90. Chicago: University of Chicago Press.

- Joskow, P.L. (2002). "Transaction Cost Economics, Antitrust Rules and Remedies." *Journal of Law, Economics, and Organization* 18: 95–116.
- Kant, I. (1797/1995). *The Metaphysics of Morals*. Introduction, translation, and notes by M. Gregor, Cambridge: Cambridge University Press.
- Mahoney, P. and C. Sanchirico (2005). "General and Specific Legal Rules." *Journal of Institutional and Theoretical Economics* 161(2): 329–46.
- Monti, M. (2002). "New Developments in European Competition Policy." Handler/Burger (Eds.), *Competition and Competitiveness in a New Economy* pp. 43–50. Vienna.
- Rey, P. (1997). "Competition policy and economic development." Mimeo.
- Schumpeter, J. (1942). *Capitalism, Socialism, Democracy*. New York: Harper.
- Soto, H. de (1990). *The Other Path—The Invisible Revolution in the Third World*. New York: Harper & Row.
- Williamson, Oliver E (1996). *The Mechanisms of Governance*. New York: Oxford University Press.