Fed Paper's Inadvertent Antitrust Policy Questions For Biden

By **Christopher Kelly** (September 8, 2020)

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No one confuses the Federal Reserve Board with the American Antitrust Institute. The Fed's concern is financial stability, not competition. But a recent working paper from two Fed staff economists[1] points up a potentially major role for antitrust enforcement in a Joe Biden administration, one well beyond heightened merger scrutiny and tougher standards for platform industries.

By identifying increased market power as a cause of the income and wealth inequality that has become a subject of intense public debate and, not coincidentally, a key issue for Democratic presidential candidate Biden's campaign, the paper implicitly raises the possibility that antitrust enforcement could take on urgency and aggressiveness well beyond what the predictable campaign positions have suggested and be used to address a core societal issue.

The paper's focus is narrow: Consistent with the Fed's mission to "foster the stability, integrity, and efficiency of the nation's monetary, financial, and payment systems and to promote optimal economic performance,"[2] it examines a collective increase in firms' market power over the past 40 years as a cause of an increased risk of financial crises like that of 2008 (defined as "events during which a country's banking sector experiences bank runs, sharp increases in default rates accompanied by large losses of capital that result in public intervention, bankruptcy, or forced merger of financial institutions").[3]

But the paper concludes that the market-power increase raised that risk by triggering a chain reaction of noncyclical (in economics terms, "secular") trends that themselves are major policy hot buttons. To simplify the paper's chain reaction:

- The increased market power, in both product and labor markets, has reduced the labor income share and, to a much lesser degree, the capital share of total output.

- The reduced labor and capital shares necessarily increase the profit share of output.

- The increased profit share increases income inequality by raising the income of the most wealthy households, whose income is driven by stock ownership, relative to the less wealthy, whose income is based primarily on wages.

- Because the wealthy have a relatively high marginal propensity to save, the skewed income also increases wealth inequality between wealthy and less wealthy households.

- Less wealthy households respond to their decreasing relative income and wealth by increasing borrowing (from, in effect, the wealthy households).

- The resulting increased credit-to-GDP ratio leads in turn to a significantly increased probability of a financial crisis.

From the Fed's standpoint, the critical policy concern is that the rise of market power has made financial crises like that of 2008 more likely. But the findings that, along the way, market power led to increased income and wealth inequality play directly into the broader discussions of economic equity that have become part of this year's presidential campaign.

The paper's implications for antitrust enforcement seem inadvertent. The word "antitrust" appears only once, in a sidelong mention in a footnote, so antitrust law does not appear as a potential solution to the problem.

To the contrary, the authors propose a back-end fix: They suggest redistributing the market-power-driven profits back to the working class through an income tax specifically because the tax (unlike antitrust enforcement) would not distort marketplace decisions. But no one interested in shaping antitrust policy in a potential Biden administration would miss the underlying questions of whether antitrust law's retreat at the outset of this 40-year period into "a mild constraint on a relatively small set of practices that pose a threat to allocative efficiency"[4] contributed to these secular trends and, if so, whether shifting antitrust law's goal from mere allocative efficiency to economic equity could be an important part of the solution.

Of course, these questions still leave unanswered the nagging issues of whether existing U.S. antitrust law can counter the mere increase of market power, and even whether it should do so, especially where many such increases may have nothing to do with anti-competitive conduct and, in fact, may even be the result of pro-competitive conduct.

But the paper could increase the urgency with which policymakers explore both of these issues — that is, not only new enforcement approaches under existing law but also new laws altogether, such as an abuse-of-dominance prohibition that most of the rest of the world uses to corral market power or a regulatory regime that somehow looks to limit market-share accumulation at all costs. In this regard, the paper could give a significant boost to New York's S.B. 8700A,[5] which would introduce abuse of dominance as an offense under New York state antitrust law, and comparable legislation introduced in any other state whose lawmakers do not wish to wait for a federal response.

The paper evidently has not yet been peer reviewed. But whether or not its authors' conclusions hold up, they have raised the stakes enormously for antitrust enforcement in a potential Biden administration. The paper's finding that a marked increase in market power, which — all other things being equal — most would agree antitrust law should prevent, has increased income and wealth inequality over 40 years and offers antitrust enforcers in a new administration a basis for expanding their mandate well beyond that of the "consumer welfare prescription"[6] that has narrowly defined its mission over that same period.

The prospect that antitrust law could be used to protect working people not only as consumers, but as full participants in American economic growth, gives antitrust enforcers a strong incentive to claim a more prominent seat at the policy table in a new administration, and with it, the impetus to develop new enforcement tools that will bear out that claim.

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[1] Isabel Cairó & Jae Sim (2020). Market Power, Inequality, and Financial Instability, Finance and Economics Discussion Series 2020-057. Washington: Board of Governors of the Federal Reserve System, https://doi.org/10.17016/FEDS.2020.057.

[2] Board of Governors of the Federal Reserve System, Government Performance and Results Act Annual Performance Report 2019-June 2020, https://www.federalreserve.gov/publications/2020-annual-performance-report.htm.

[3] Paper at 2 n.3 (quoting Moritz Schularick & Alan M. Taylor, Credit Booms Gone Bust: Monetary Policy, Leverage Cycles, and Financial Crises, 1870-2008, Am. Econ. Rev. 102 (2) (2012) 1029, 1038).

[4] Daniel A. Crane, The Tempting of Antitrust: Robert Bork and the Goals of Antitrust Policy, Antitrust L. J.79, no.3 (2014) 835.

[5] Senate Bill S8700A, 2019-2020 Legislative Session https://www.nysenate.gov/legislation/bills/2019/s8700/amendment/a ("[r]elating to actions or practices that establish or maintain amonopoly or restraint of trade, and authorizes a class action lawsuit in the state anti-trust law").

[6] Robert H. Bork, The Antitrust Paradox 66 (1978).