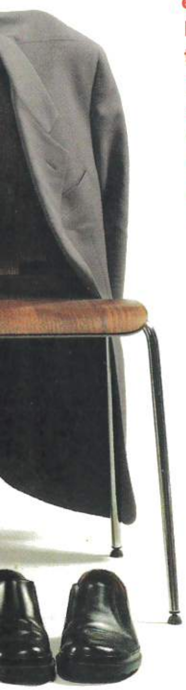

'Colin Crouch has produced the most important work on the political economy of modern capitalism since Keynes, Kalecki and Shonfield. He captures how the ideology of neoliberalism has combined with the power of giant corporations to change irrevocably the respective roles of state authorities, political parties, corporatist arrangements and mass media. And in the process, he also succeeds in explaining the most glaring political paradox of our times, namely, why – despite the manifest failure of neoliberal policies to deliver on their promises of growth, prosperity and equity – has there been such a pitiful and ineffectual reaction by voters and mass publics?'
Philippe C. Schmitter, European University Institute

'Colin Crouch shows how neoliberalism as embodied in large corporations brought about the financial crisis of 2008, and yet, ironically, they profited in wealth and power from it – at everyone else's expense. A compelling read.'
Michael Mann, University of California, Los Angeles

The financial crisis of 2008–9 seemed to present a fundamental challenge to neoliberalism, the body of ideas that has constituted the political orthodoxy of most advanced economies in recent decades. In this important new book Colin Crouch argues that neoliberalism will shrug off this challenge. The reason is that although it seems to be about free markets, in practice neoliberalism is concerned with the dominance over public life of the giant corporation. This has been intensified, not checked, by the financial crisis and by an acceptance that certain financial corporations are 'too big to fail'. Although much political debate remains preoccupied with conflicts between the market and the state, the impact of the corporation on both these is far more important today.

Several factors have brought us to this situation:
- the lobbying power of firms whose donations are of growing importance to cash-hungry politicians and parties;
- the weakening of competitive forces by firms large enough to shape and dominate their markets;
- the power over public policy exercised by corporations whose contracts for public services deliver special relationships with government;
- the moral initiative grasped by enterprises that devise their own agendas of corporate social responsibility.

Democratic politics and the free market are both weakened by these processes, but they are largely inevitable and not always malign. Hope for the future, therefore, cannot lie in suppressing them in order to attain either an economy of pure markets or a socialist society. Rather, it lies in dragging the giant corporation fully into political controversy.

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Contents

important intermediate step. We have been operating with the model of pure markets derived from neoclassical economic theory. This model is unrealistic in several respects, and some developments in theory have tried to address these, in particular concerning the role of the giant corporation which dominates its markets. The ability of government action to cope with market failure will be considered in the light of this adjustment.

3

The Corporate Takeover of the Market

> It is a fact that within liberal society itself one of the key divisions of political identity . . . is between these two sides: the side that fears private power more, and in order to fight it is ready to give more room to the power of government; and the side that fears the expansion of government power more, and is therefore more prepared to tolerate private power.
>
> (Amato 1997: 4)

While a close involvement in government and politics by all kinds of firm can cause problems for a true liberal economy, particular problems appear in the case of what we shall call here 'giant' firms. A 'giant' firm is one that is sufficiently dominant within its markets to be able to influence the terms of those markets by its own actions, using its organizational capacity to develop market-dominating strategies. A giant firm for our purposes is also one that is active across more than one national jurisdiction. Both definitional criteria are needed. There are today many examples of moderately sized firms that have branches in a number of countries but which are relatively small within their markets. Unless they have monopoly positions in specialized markets, these are subject to the full weight of the laws of supply and demand, and are not covered by the present discussion. The two attributes

def: "giant" firm

intensify our general concern in this book with the political problem presented by such firms, as capacity for market-dominating strategy can include having a political strategy, and transnational corporations (TNCs) can sometimes play off national governments against each other.

neo-class theory of firm

In the perfectly competitive economy understood by neoclassical theory the firm is nothing other than a nexus of contracts, a point where resources in a number of markets come together and are traded off against each other. The firm's behaviour can be discovered from the signals that the market gives to its decision-makers about the most rational path that it should follow, given its taken-for-granted goal of profit maximization. Firms that do not maximize rationally in this way will be out-performed by those that do and will disappear from the market. The human beings inside the firm are little other than calculating machines for working out the appropriate logic of maximization in any given situation. Economic theory and, indeed, practical commercial law in the Anglo-American tradition treat firms as though they were individuals, because these schools of thought do not have a concept of an organization with internal complexities. But actually existing capitalist economies do not conform to the pure neoclassical model. As we have seen, in many markets there are barriers to entry that prevent more than a small number of corporations being present in the global market, let alone individual national economies. Sometimes vast investment is required for research and development; or extensive distribution networks have to be in place before a firm can establish itself.

mistaken treating firms as ind'ls

The fact that the firm, particularly the large one, is an organization and not just a nexus of contracts was first recognized in economic theory in the 1930s, in the theory of the firm developed by Robert Coase (1937). The central idea is most easily understood through the labour market. When a firm wants to make use of labour, it can do so by making a contract with some individuals that they will perform certain tasks in exchange for a set fee; if, when that task is completed, another one is needed, a new contract is made.

→ firms and labor mkts

This is common practice for tasks that the firm needs only sporadically, such as formulation of a new advertising strategy. When firms operate in this way, they can be understood fully by pure market analysis. However, when they want continuous and repeated performance of a set of tasks for an indefinite future, or want to bind people who work for them into a shared culture, they are likely to find it inefficient to keep making new contracts and introducing new workers to the firm. They therefore usually make general contracts, known as employment contracts, under which the supplier of labour services is guaranteed payment for a prolonged period in exchange for placing him- or herself under the general authority of the employer, carrying out such tasks as the employer may require. This is the idea of a 'job' with an organization with which most of us are familiar. The firm here becomes more than a nexus of contracts and is an organization with a hierarchy through which orders are transmitted to employees rather than contracts made with subcontractors.

emp't contracts ≠ spot labor contracts

The main use that orthodox economics makes of the theory of the firm is in considering a trade-off that confronts companies. Use of the market enables frequent testing of prices and quality being offered in the external market, at the expense of possibly costly market searches and training to induct new employees and suppliers in the ways of the firm. Operation through hierarchy ensures continuity and reduced transaction costs at the expense of some inefficiency through neglect of market testing. Most large firms will reappraise the trade-offs in their use of markets and hierarchy from time to time in the operation of their businesses, adjusting the balance between them as seems more profitable. In several works Oliver Williamson (1975; 1985; Williamson and Masten 1995) has developed the original Coasian concepts, and in particular the idea of transaction costs, to explore a wide range of organizational issues affecting firms. As we saw in the previous chapter, a major transaction cost is information. Seen in simple neoclassical theory as something which rational actors necessarily possess,

usual Q: the tradeoff betw market + hierarchy

Walmart

information is in reality difficult to acquire. One reason firms have for developing and deploying organizational resources is to be able to acquire information. Large firms that have developed the ability to act as organizations, choosing when to go straight to market and when to use organizational resources, have acquired a capacity for strategy. They have not liberated themselves fully from the market; they remain subject to it in order to buy and sell successfully. But they also have some ability to act proactively, to use their organizational structure to shape markets and to determine how they will respond to them. For example, instead of responding passively to market signals that there is a demand for a certain product, they will mount marketing and advertising campaigns to create demand. This gives them advantages against smaller, market-driven firms, and also changes their relationship with consumers, where these latter are individuals rather than other corporations. The symmetry between buyer and seller that is fundamental to economic theory in general and to the idea of the sovereign consumer in particular becomes considerably distorted when the seller shapes the preferences of the buyer.

abil to shape mkts

These facts do not make giant corporations evil; which is fortunate, as it is difficult to imagine a prosperous life without them. But it does mean that they are not as fully subject to consumer sovereignty and market forces as neoliberal rhetoric claims. If we are increasingly told to welcome 'more market' in our lives, but 'more market' really means 'more giant firms', we need to know more about these and their political implications.

The Importance of Antitrust Law

The words quoted at the head of this chapter appear in a comparative study of US and European approaches to the problem of corporate power by Giuliano Amato, an Italian professor of law but also the past holder of several high political offices, including that of prime minister, in his country. In his book he deals with two of the central dilem-

how to think of

gov intervention needed to create comp mkts?

mas in market economies. First, are the virtues of the market better expressed in the maintenance of competition, and therefore with the existence of large numbers of competing firms, as in pure economic theory, or in the outcome of competition, which may often mean the survival of a few giant corporations and diminished consumer choice? Second, if the former is preferred, and given that it usually needs anti-monopoly legislation to maintain large numbers of firms in markets that are prone to concentration, how much government intervention is acceptable in order to preserve competition? Posing these dilemmas immediately throws into confusion the hackneyed opposition of 'state versus market'. The confusion is caused by the insertion of that third entity, the giant firm, into the equation. Most political debate glibly assumes that the firm is part and parcel of the market. But what about the state and the market united against the giant firm? Or the giant firm and the state together against the market? Both are possible and do occur. In the above quotation, Amato is mainly thinking of the relation between firm and state, and eventually this will be our concern too. But first we must see how it is that firm and market become separated.

Classic US antitrust law, developed in the first part of the twentieth century, aimed at breaking up major accumulations of corporate power, so that there was a limit to how far any one firm or group of firms could go in dominating a particular set of markets. One of the strongest examples of this was US banking law, which for many decades prevented US banks from having branches outside their home state. The core theory of US politics, pluralism, was able to reinforce itself in this intellectual environment. It was essential for economic and political democracy alike that there should not be concentrations of power so strong that they faced no effective competition; ordinary people should always confront a choice that put them on more or less even terms with the firms or politicians who might otherwise dominate them. Further, there should also be scope for easy entry by newcomers into both product markets and the political arena. To the extent that economic power could be a major source of political power too, antitrust policy protected democratic pluralism as much as it did market competition.

It proved impossible to maintain all markets with low entry barriers and full competition, as the efficiency advantages of giant corporations, often formed through mergers between firms rather than by growth consequent on the popularity of a firm's products, became ever stronger. In their desperation to maintain the image of small-firm, small-town America, government antitrust lawyers were forced into ever tougher definitions of offences against competition, and government found itself intervening in highly detailed ways in firms' conduct. This was an affront to the interests of very powerful corporations, and also confirmed the suspicion in some areas of US political opinion that government intervention, even if aimed at protecting small firms and local entrepreneurship, constituted communism. Economic and legal theorists, principally at the University of Chicago, and corporate lawyers defending antitrust suits for large corporations, developed a new set of principles that abandoned earlier insistence on the need for actual competition and large numbers of competitors if the liberal capitalist model was to work. A new theory of the economy emerged, which tended to favour large, market-dominant firms.

Ironically, this approach, designed to keep government out of the economy, was thoroughly political throughout its development. The two academic lawyers, Robert Bork and Richard Posner, who played the main roles in reversing the bias of antitrust policy were appointed judges by President Ronald Reagan, and his neoliberal administration followed up these court appointments with various pieces of legislation favourable to the project.

We return to the first dilemma. Does economic competition denote a situation in which a large number of firms is present in the market, maintaining constant competitive pressure on each other and providing consumers with extensive choice? Or does it mean an economy in which competi-

back to this: defining competition

tion has been able to work to its logical end of weaker firms being destroyed by stronger ones, with a small number of survivors and reduced choice for consumers? The classic answer of US antitrust law and of the German *Ordoliberal* theorists had been the former. It is this that was reversed by the Chicago school. One consequence was that the idea of consumers' freedom of choice had to be dethroned from the principal role it played in promulgating the US vision of the world. The new approach has never sought much public prominence for this particular aspect of its argument; the more general Chicago approach to a free economy without government intervention was popularized by Milton and Rose Friedman's television series and subsequent book *Free to Choose* (1980). But the serious intellectual arguments tell a different story.

So, less cons. freedom of choice

The issue is not, argue Bork (1993[1978]) and Posner (2001), what consumers actually want to choose, but what gives them the biggest likelihood of having a choice. Logically, their scope for choice must be enlarged as wealth is increased in the economy as a whole. If there would be efficiency gains from a number of smaller firms being bought out by a larger one, then that would be the outcome that would maximize what they called consumer 'welfare', even if it led to reduced competition and left consumers with a reduced choice of goods. What should therefore be the concern of the law courts in deciding antitrust cases is what outcome would be most conducive to the maximization of consumer *welfare*, not *choice* as such.

consumer welfare not choice

While consumer choice is a democratic concept, leaving decisions to consumers themselves, consumer welfare is a technocratic one; judges and economists decide what is good for consumers. It is deeply paternalistic, the kind of idea that leads to the description of 'nanny state' when a government leans in that direction. If a group of consumers were to argue that they would prefer, say, to keep a group of local small shops rather than have these replaced by one supermarket, they would be told that they were irrational, as it cannot be in their interests to want a less efficient outcome. (In reality

who decides?

Consumer welfare/choice redefined

they are not asked, because in the market economy consumers do not have a voice as such, unless firms use them for their own private market research purposes; consumers indicate their preferences solely through price signals.) It is also a collectivist rather than an individual concept, despite the fact that the strong rhetorical stance of this entire strand of US economics thinking is individualist and anti-collectivist. Consumer welfare is to be understood in terms of a *general* gain in efficiency across the economic system. As we shall see below, the theory is not interested in how this gain is distributed among actual people. It is enough that there is net gain, somewhere in the collectivity.

This thinking favours the large corporation; at its core is the argument that mergers and amalgamations, leading to the emergence of giant corporations, will always lead to improved efficiency. The rationale for this view is that rational firms would launch takeover bids only if they were convinced that they could achieve efficiencies, and the prices offered for shares in the firm being taken over would reflect these expectations. Subsequent research has challenged these assumptions by showing that the improved profits made by takeovers might sometimes be associated with reduced efficiency. Particularly important are the network externalities and standard setting by large corporations discussed in the previous chapter. We saw there how a larger corporation can have superior means for distributing, publicizing or otherwise spreading its products, even if they are poorer products than those of smaller firms.

Firms + info

Giant firms also tend to possess considerably more information than their customers, except in those markets where the customers are other large enterprises. However, while this is very problematic to the idea of consumer choice, it is of no consequence to that of consumer welfare. Indeed, if having inadequate information makes customers more likely to purchase a product, there will be an increase in profits, therefore in overall wealth, and therefore in consumer welfare itself.

Against the advice of Chicago economists, consumer legislation frequently chases after these practices, as parlia-

ments legislate for common standards of information, or the European Commission insists that firms in these so-called 'network' industries allow competitors to connect to their platforms. But the very fact of this chase demonstrates how firms will behave if left to themselves, and how they do behave as they discover new fields in which to use standards, not as a form of consumer protection, but as a means of profit maximization against the felt interests of consumers – but not their 'welfare', as the definitional trick has it.

Both classic US and European antitrust thinking had in mind a number of interests that have to be served by the structure of the economic order: shareholders, certainly, but also consumers as such, and the desirability of maintaining a class of small and medium-sized entrepreneurs. This need to serve a number of interests created dilemmas for competition law. Whose interests should be protected? Those of shareholders in seeking mergers sufficiently large to enable a firm to impose standards on a market, or those of smaller firms using networks or standards in order to enter the market, or consumers wanting to be able to maximize their choices? Anglo-American law, as developed under neoliberal influence, has simplified this dilemma considerably: shareholders alone constitute the interest that must be served by an enterprise. We shall encounter a number of problems with this argument below and in later chapters, but for the present we must concentrate on the aspect that is relevant to the Chicago amendment to antitrust theory and its approach to consumers.

once plural interests

Now, only shareholder interest counts

The argument in favour of shareholder interests works well, all other things being equal, if perfect competition can be assumed. In a pure market, shareholders can maximize their interests only if consumers are being well served, otherwise these will defect to competitors. However, once there is a movement to the restricted competition characteristic of the modern economy, the situation changes. There are important asymmetries of information between large corporations and all others on the market. It is in the space opened by these asymmetries that there is scope for behaviour that

info asymmetries

Apply both cons interests + shareholder info maximizes shareholder interests but not those of consumers. It cannot therefore be assumed that consumer interests can be safely entrusted to the maximization of shareholder interests.

We can take this further if we are able to demonstrate the possibility of a decline in concern for customers by firms that are making high levels of distributed profits. We should assume that firms will do as much as they can to conceal any such actions, by maintaining front-line activities and cutting back on less obvious aspects of customer service – just as governments making cuts in public spending try to spare highly visible front-line staff in schools and hospitals. Reductions will be most evident where firms reduce their level of something called 'redundant capacity'. This is a concept that we derive from engineering, but it has many social uses. When engineers design a machine, they have to envisage stresses and strains to which it might be subject on exceptional occasions. Let us take the example of a bridge. If the engineers design a bridge so that it will take the strains of its expected everyday traffic only, there could be a disaster if ever an unusually heavy lorry tries to cross during already heavy traffic. They will therefore design for considerably larger stresses than normally experienced. However, this does not mean they can design the bridge so that no weight of traffic would ever be too heavy for it, for that would make it far too costly, drawing resources away from other projects with more urgent needs. A decision of calculated risk has to be made, and part of the skill of engineers lies in making these calculations. The extra capacity that the engineers design into the bridge, running from expected everyday traffic to the maximum possible load for which they decide they must design, is called redundant capacity. Most of the time, possibly for all its life, that extra load-bearing capacity of the bridge will not be needed; it will be redundant. Above that level is the risk that the engineers have calculated that they must take if the project is to be commercially viable. Exactly where to set the level remains a matter of judgement and cannot be delegated to a technical formula.

A vast real-life example of this issue occurred with the British Petroleum oil-rig disaster off the coast of the southern USA in 2010. All drilling for oil, but especially that from under the sea, entails considerable risks of accident and of potentially extensive pollution – major examples of what was discussed in the previous chapter as 'negative externalities'. Oil firms have to design into their equipment and drilling platforms expensive protection against a series of possible disasters that are unlikely to happen, but which if they do happen will cause major problems. They have to design for a high level of redundant capacity. This is obviously a highly expensive business, and the question has to be faced of just how unlikely a risk has to be before a firm can decide to ignore it and save some money. BP and its US subcontractors, including Halliburton, a major contractor of the US government in Iraq, made a series of such decisions; the disaster did happen; and the damage has been far greater than the cost of providing protection against it.

In the years preceding the disaster, BP and its subcontractors, in common with many other corporations, had reduced the role of engineers in their decision-making structures in favour of finance specialists. Engineers and financial experts take different approaches to risk. Did this change lead to a reduction in the degree of redundant capacity that BP and its US partners considered necessary? There was very considerable anger in the USA that such a disaster could occur on the US coastline, and the fact that BP is a 'foreign' firm loomed large in that anger. In general political discussion, US public opinion is usually scornful of the apparently higher sensitivity to risk shown by European publics as evidence of a lack of entrepreneurialism. It will be interesting to see if this attitude is revised as a result of this case.

An example of the use of the idea of redundant capacity outside the scope of engineering itself would be the funding of basic scientific research by governments. If government funds only that level of research that is necessary for easily perceived current needs, there will be no new discoveries, the potential value of which is not known at the time. Basic research, in contrast, generates knowledge that is 'redundant', as it cannot immediately be used; but one day it might become useful. Governments cannot be expected to fund all possible kinds of research on the grounds that one day it might be useful, as it would be too costly. They have to make a judgement somewhere between catering only for easily predictable needs and doing everything possible.

Redundant capacity is one of the areas in which firms can make decisions that will be immediately relevant to shareholders' interests, but only of clear relevance to customers' (and therefore long-term shareholders') interests in a longer run. A decision to reduce redundant capacity will immediately boost profits. In the longer run it might result in disastrous service failures, but if the firm fails to meet the share market's profit expectations there will be no long term, at least not for current management. Judgement is required, and the firm must choose between favouring shareholders or consumers; the more the firm concerned is protected from competition by near-monopoly status, the more it will lean towards the former.

The Chicago approach has three ripostes to these objections. These are arguments concerning the effectiveness of limited competition, distributive effects and government intervention.

First, it points out that there can be aggressive competition between a small number of giant firms. Once actual consumer choice and the market weakness of consumers is devalued in importance, all that matters for competition to exist is that a small number of producers are trying to take each other's market share. The Chicago school has reached the view that three firms will be enough to ensure this. If there are just two firms, and certainly if there is only one, the school would accept a case in favour of breaking up the firms concerned as in the normal antitrust solution. Critics argue that this ignores the scope for tacit collaboration among such a small number of firms. Assume, for example, that the banks in a particular country would find it more profitable for their shareholders to reduce the number of

branches and reduce the training given to their counter staff, reducing overall the quality of service offered to small retail customers. In a strongly competitive market, with large numbers of banks, the first banks to try this would be likely to lose customers to more customer-friendly rivals, with consequent loss of profits; shareholders' interests are made equivalent to those of customers through the market. The banks cannot solve the problem by making an agreement to reduce the service offered, for such an agreement would break competition law, while with a large number of banks it would not be possible to maintain a purely informal 'nods and winks' agreement against opportunistic defection.

Now assume that the national banking system is dominated by four large banks. Their numbers are small enough to operate through informal, virtually undetectable signals to each other that they will all reduce services to customers and increase their profits. The capacity for strategy that a large player in a market possesses also extends to a small group of players being able to give subtle signals that cannot be detected by competition authorities. The Chicago writers are very dismissive of the possibilities for firms to give signals of this kind, which has led to them being criticized in turn for naivety in underestimating firms' capacities in this regard. Their argument is not based on naivety, however, but on the weight they place on a different factor altogether. What they actually say is that, while it is possible that firms engage in such practices, it is better to give them the benefit of doubt; otherwise one provides government with an excuse for intervening in the market, which the Chicago writers regard as the worst possible outcome.

Before considering this last fundamental point in detail, we must examine the remaining issue, distributive effects, as this also has implications for government intervention. The Chicago school sees consumer welfare as maximized when the overall level of wealth is raised in an economy, on the grounds that consumers' welfare cannot be increased by reducing the quantity of resources. They are explicitly uninterested in the distribution of this wealth, in who actually holds it. To take an extreme case, imagine a set of mergers that increases efficiency in an industry but which reduces competition to the point where prices to consumers rise, or services to customers deteriorate as suggested above in the example of declining redundant capacity. Provided the quantity of wealth produced for shareholders by the efficiency gains is greater than that lost to consumers through the increased prices, Chicago followers would argue that the price rise is consistent with an increase in consumers' welfare, as the economy overall is richer. If pressed on whether it matters if the actual wealth is held by shareholders or spread among consumers, they would probably say that much of it is bound to 'trickle down' to everyone else; but more importantly they would certainly argue that this is merely a distributive question and of no concern to economic theory. They might acknowledge that we may have reasons for caring about distribution, but would then say that this is a matter for political action, not for economics.

The Paradox of Government in Neoliberal Thinking

However, while Chicago economists suggest political action as the only remedy for distributive problems and, indeed, any other goals that cannot be achieved by the maximization of shareholder interests, they generally regard it as the worst possible eventuality, even worse than restrictive, anti-consumer behaviour.

To understand the depth of this antipathy we need to understand the traditional US hostility to most government action, apart from military, and its most recent intellectual manifestation in the political science school associated with the University of Virginia (see, for a key text, Buchanan and Tullock 1962). This has been the home of the public choice school of politico-economic theory. This presents nearly all state activity as the self-seeking and self-aggrandizement of political figures and officials. For this school, a proposal to develop a public service should not be seen as having anything to do with the substance of the service in question, but

as politicians and officials expanding their scope for patronage. From this they drew similar conclusions to their friends at Chicago: keep as much as possible in the market, away from the public sector. Important issues are raised here, and we shall confront them in later chapters. For the moment we need only to register the dilemma in which the combined Chicago/Virginia approach leaves us in relation to issues like distribution, pollution and environmental damage. We are told that these are not matters for firms, as their duty is to maximize shareholders' profits; if we want action on them, we will have to turn to politics. But when we arrive at the door of politics we find Chicago/Virginia people waiting there to warn us never to turn to politics for anything, as governments are at best incompetent and at worst corruptly self-seeking. We are therefore left with no capacity to criticize whatever firms do, provided they do not conspire together in obvious collective groups, no matter what damage they do to any interests or values that do not serve shareholders' interests. While this is presented to us as a matter of individual choice in the market, we also know that the Chicago school of neoliberalism has redefined this so that it often means, de facto, the preferences of large corporations.

There might seem to be a further paradox in that, while the Chicago school is deeply suspicious of government, it makes major use of law. Its advocates would distinguish sharply between law and government. It is, in theory, possible to do this within the common law systems of the Anglophone countries, where the law is (partly) developed through changing judicial interpretations designed to facilitate agreements between parties, without recourse to government. The partial triumph of the Chicago approach within the US, and eventually European, courts was achieved through judges taking a different view of antitrust cases, without government action – apart from such small matters as President Reagan appointing Bork and Posner to the bench in the first place.

The Chicago school argues that, often, even recourse to the courts is unnecessary, and that parties to most disputes over property rights can resolve their differences by taking an economics approach. The willingness of one side to buy off the other will provide a sure indication of where the balance of material interests, and therefore overall efficiency, lies. It is notable that most of the examples on which this approach to competition law has cut its teeth have been taken from traditional manufacturing and even agriculture and not from characteristically late twentieth- and twenty-first-century sectors. The key text, an article in 1960 by Robert Coase entitled 'The Problem of Social Cost' (oddly, the same Robert Coase who gave us a highly modern theory of the firm in the 1930s), is based on the hypothetical case of a cattle rancher and a farmer. The former permits his cows to damage the farmer's crops. This was normally seen as a need for the law to protect the latter's crops from damage. Not so, argued Coase. If the farmer is to gain from the rancher restraining his cows, it is in his interests to pay the rancher to do so. If the amount he is willing to pay is enough to deter the rancher, then that is the efficient outcome. But if the rancher finds the amount offered less than he can gain from continuing to allow his cattle to roam free, then it is more efficient for the cows to continue to damage the crops. There is no need for an abstract debate over entitlements and rights: the amount that people are willing to pay to settle a case, rather than abstract ideas like justice, should determine legal outcomes, as this ensures efficient use of resources.

There is room for ethical debate here: does it matter if a legal system gives up all idea of justice? But we shall concentrate on a different problem. The Chicago approach calls for a limited number of identifiable individuals (persons or firms) who can be engaged in making a deal. It is far more difficult to make such solutions work where gains or harms from externalities accrue to very large numbers of individuals, as is typical of many contemporary environmental damage cases, especially where those affected cannot be defined as a specific class for the purpose of a class action and who have difficulty overcoming the problem of collective action.

Chicago writers are aware of issues that might occur through corporations combining together formally as anti-competitive cartels or lobbying politicians. Although the Chicago approach has done much to legitimate the economic power of big business against customers and smaller firms, it would join the already heterogeneous consensus of social democrats and neoclassical economists in opposing the translation of economic into political power – though Bork (1993) in particular insists that small firms conspire together to lobby politicians as much as large ones. Indeed, he departs from the usual position of the US of support for local levels of jurisdiction against more central ones, on the grounds that local legislatures are more vulnerable than central ones to lobbying pressure.

Against Bork one can argue that small firms, with the important exception of those that have local monopolies, are more likely than large ones to be in pure markets, with profit margins pressed down below the point where they can afford the costs of lobbying in the US political system. They are also vulnerable to the general problem known as the logic of collective action. Assume a mass of individuals (human beings or firms) who each have an interest in working for a goal, the achievement of which will benefit all concerned, irrespective of whether they joined in working for it. It is not in the interests of a rational actor to take part in action to achieve that goal, especially where that actor is a firm in a highly competitive market. To take part in an action while competitors do not is to incur costs that the competitors will not bear, even though they will benefit from successful action. If some 'mugs' do participate in the action, those who do not join them save on costs but get the benefits.

Giant firms, with their tacit agreements to limit competition and capacity to check what competitors are doing, are differently situated. They are not small players in a mass action; their contribution can make a difference, and they may stand a good chance of limiting benefits to themselves. Paradoxically, the danger of mixing economic and political power through lobbying politicians to take action favourable to a firm or sector is considerably greater in a 'Chicago' economy than one with perfect markets. But the school has its own answer to this. The more that government becomes involved in the economy, the greater the range of issues where corporate power can be politically deployed. Therefore, they argue, reduce the economic role of government, and the problem will be reduced. Once again we see Chicago economists recommending that we turn to political action to resolve problems of distribution and goals outside the scope of profit-making, only then to assert that government should not in fact become involved at all.

The firms that benefit from a permissive approach to oligopoly are not themselves required to abide by the strict principles of the neoliberal doctrines from which they benefit. There is absolutely no evidence that the corporate giants of the USA consider that they should not lobby government in case this amounts to an undesirable mixing of polity and economy. Amato, in the study quoted above, points out that US administrations became particularly susceptible to Chicago reasoning and its tolerance of oligopolies at precisely the moment in the 1970s when German and Japanese imports were beginning to hurt US manufacturing, and corporate lobbyists were arguing that greater corporate size would help confront this competition.

Robert Reich, a noted US economic commentator and former Secretary for Labor in the Clinton Administration, has described the US corporate lobbying system in his book *Supercapitalism* (2008). He attributes growing inequality, increased job insecurity and corporate corruption as negative features of modern American life that can be traced back to successful lobbying. One example involved the scandals in the US economy at the end of the 1990s affecting Enron, WorldCom and some other firms. These cases did not concern a murky hinterland of the capitalist economy, but its very heart. Enron, a Texan oil-producing corporation, had become the seventh largest firm in the USA, and donated millions of dollars to the election campaigns of US President George W. Bush. It owed $64 billion at the time of its collapse in

2001 – an all-time record that lasted only until the following year, when the WorldCom crash exceeded it. Both corporations had their accounts audited by Arthur Andersen, one of the five largest auditing firms in the world, until it too collapsed as a result of its involvement in the cases. (For an interesting analysis of the case, see Froud et al. 2004.)

Corporate lobbying provided the background to these scandals. In the name of the free market, lobbyists had persuaded Congress to pass legislation allowing a firm employed by a corporation to audit the accounts of that corporation and also to sell it other accountancy and consultancy services. This had previously been illegal because of the incentive it might give audit firms to keep quiet about irregularities they found in corporate accounts, so that they would not lose lucrative contracts. This is precisely what happened, and quite soon after the legislation was passed: Enron had major irregularities in its accounts; Arthur Andersen audited them, and its staff found the irregularities, but senior management hushed them up because of the important consultancy contracts they had with Enron. It is to the credit of US pluralism that the scandal could not be kept secret; the matter went to the courts and several senior executives found themselves in prison.

A more recent example is the extraordinary lobbying campaign unleashed by the US health industry against the Obama administration's healthcare reform policy. It was reported (by the UK's *Guardian* newspaper on 1 October 2009) that US health insurance firms, hospitals and pharmaceutical corporations deployed six lobbyists for each member of Congress and spent $380 million campaigning against the policy. 'Campaigning' primarily means contributing to the re-election funds of sitting congress-persons. Although the legislation was eventually passed, it was diluted in many important ways. One – which raises issues to which we shall return in the next chapter – was to replace the originally planned national health insurance fund of the kind familiar in most European countries with an obligation on citizens to buy private health insurance, government subsidizing the contributions of those on low incomes. This provides compulsory, partly subsidized customers for private corporations.

Similar sums are being spent by the financial services industry to emasculate the Obama administration's attempts to re-regulate that industry following the global crisis brought about by its unregulated behaviour.

In 2010 the International Monetary Fund (IMF) claimed that during the previous four-year electoral cycle, US firms spent $4.2 billion on political activities, particularly prominent among them being firms in the high-risk end of the financial sector (IMF 2010). A former chief economist of the IMF, Simon Johnson, has claimed (2009) that the financial sector has now captured control of US government in a manner normally associated with developing countries.

The USA is not uniquely vulnerable to corporate lobbying. In July 2010 the European Parliament decided between two approaches to food labelling, designed to give consumers information on the health risks associated with certain ingredients. One was a prominent colour-coded graphic of ingredients, the other a small-print black-and-white list. Despite their clear preference for coloured graphics to present their own logos and publicity information, 11 leading food and drinks manufacturers lobbied heavily in favour of the small-print black-and-white lists. A representative of a consumers' organization, which was lobbying for colour-coding, told the *Independent* newspaper (7 July 2010) that corporate lobbyists out-numbered those of consumer associations by a hundred to one. The Parliament voted as the corporate lobbyists wanted.

Amato set out as the central dilemma of antitrust policy the choice between private and public power: do we risk enhancing the state's reach in order to tame private economic power, or do we tolerate the latter in order to avoid giving government more power? The Chicago approach seems to belong squarely with the latter; but in fact it does something quite different. By assisting in the growth of truly giant corporations, it connives at a mighty combination of private economic power and state power. The latter is not used in a totalitarian way, as with the fascist or communist state, but it is used further to assist and protect the interests of those corporations.

Much of the original extremism of Chicago antitrust doctrine has failed to stand the test of time (Cucinotta et al. 2002). In particular, its neglect of network externalities in fast-moving, high-tech economies, and its acceptance of the ways in which small groups of dominant firms can act anti-competitively without leaving any paper or email trail of complicity, have led to considerable revision in US law, and limited the extent to which European law has imitated earlier US developments. In 2002, Richard Schmalensee, an academic who had helped Microsoft Corporation fight its legal battles against US antitrust authorities, was complaining, just as Bork had 20 years before, that antitrust law prevented leading firms from pressing home their advantage, forcing them to allow competitors to survive with a resulting overall loss of efficiency. He attributed Microsoft's legal problems to the fact that it had not devoted enough attention to political lobbying – a situation which it has subsequently remedied.

It is a testimony to the strength of public institutions and a sense of public interest on both sides of the Atlantic that antitrust suits continue to be brought to the courts, and that corporations are required to relinquish a monopoly position or provide access to their platforms for smaller competitors. However, three major points remain. First, the paternalistic test of consumer welfare rather than actual consumer choice, and the essentially collectivist doctrine that, provided wealth has been created somewhere in the system, it does not matter who enjoys it, have remained central to how mergers and acquisitions are viewed in competition law. These concepts have become part of the heritage of neoliberalism, however true its rhetoric remains to the ideal of freedom of choice.

Second, whatever the defects of Chicago theory as a set of economic principles when compared with the theory of pure markets, it came into being partly as an attempt to counter the sheer lack of reality of the previous orthodoxy. By the 1970s US antitrust law, in its attempt to prevent market domination by giant enterprises, had started imposing impossible and impractical restrictions on mergers and acquisitions. Whether one sees this attempt to safeguard small firms and consumer choice as nostalgia for an increasingly unrealistic image of small-town America or (as Bork believed) as an attempt to impose a socialist state, it was certainly Quixotic. The same applies to the similar aspirations of the *Ordoliberalen*. The positive achievement here of the Chicago approach to antitrust was to make the courts, as well as legal and economic analysts, think seriously about the opportunity costs of trying to preserve the neoclassical ideal of an economy dominated by masses of small and medium-sized enterprises. Trying to maintain this ideal would be costly in terms of both economic efficiency losses and increased government intervention. But they could have made these points solely within the framework of that well-trusted economics concept: opportunity cost. Redefining the matter as the contorted notion of 'consumer welfare' was a piece of populist rhetoric which betrays the political rather than purely economic and jurisprudential motivation of the authors of that concept.

Finally, the Chicago innovations did nothing to resolve the central issue: economic and political power translate into each other. This is why it is so difficult in practice to maintain the separateness alongside interdependence required by liberal capitalism. An economy dominated by giant firms makes this worse, as it generates very high concentrations of wealth. Not only can firms convert this wealth into political influence, but they can use the capacity for strategy given to them by their size and organizational hierarchies to pursue political purposes and to become political actors. Seeing the firm as an organization and not just as a nexus of contracts enables us to perceive the implications of this for political theory.

4

Private Firms and Public Business

The previous chapter considered a distinction between the market and large enterprises, and a tendency in neoliberal thought to give the latter attributes of the former that they do not really share. We encounter this distinction again when considering the very important processes that have taken place in recent years as governments, under the influence of neoliberal ideas, have sought to move their own activities closer to those of the private sector or even to move them fully into that sector. The process is always seen as being about adapting government to the market. Often it has instead adapted it to the corporation. This has in turn further helped to develop the politicized giant firm – which is in its turn the opposite of what liberal political economy intended.

Much conventional debate over the relative virtues of the market and the state relates to the market failures discussed in Chapter 2, and the approaches with which governments have historically sought to remedy them. These approaches then became themselves the objects of neoliberal criticism from the 1970s onwards as the sources of 'government failure'. We are now ready to examine these, disabused by the discussion in Chapter 3 from believing that it is a simple matter of state versus market.