Use and Abuse: The Myth of Divided Antitrust Economics

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Abstract

The new pattern of global antitrust regulation established by government authorities shows that, despite much being made about economists’ inability to agree on anything, convergence in antitrust economics is both recent and remarkable. Economists today near-unanimously believe that antitrust enforcement is beneficial to both consumers and economic growth and that it is a necessary component of any modern free-market economy. Despite this agreement, conflicting economic evidence presented by experts in competition disputes remains. While economists, lawyers, and triers of fact may interpret opposing positions as reflecting a misuse of economics, in the vast majority of instances, disagreement among experts reflects differing underlying beliefs about the interactions of firms and consumers, as well as differences in their understanding of what constitutes competition in the market at issue. This discussion explores a series of questions to consider—What do economists believe? What methods do economists rely on? Where do the differences lie?—to help focus on the root cause of common disagreements among economic experts in antitrust litigation. These questions are then considered in the context of litigation surrounding Best Buy in the matter of alleged cartel activity among thin-film-transistor liquid-crystal display (“TFT-LCD”) manufacturers.
I. Introduction

The new pattern of global antitrust regulation established by government authorities shows that, despite much being made about economists’ inability to agree on anything, convergence in antitrust economics is both recent and remarkable. Economists today near-unanimously believe that antitrust enforcement is beneficial to both consumers and economic growth and that it is a necessary component of any modern free-market economy. Testimony based on antitrust economics on topics including monopolization, horizontal agreements, and mergers reflect this uniform agreement among economists that competition is welfare enhancing.

The Act for the Prevention and Suppression of Combination formed in the Restraint of Trade, voted by the Canadian Parliament in May 1889, is widely seen as the first competition statute in the world. It was followed promptly by the well-known Sherman Act, approved by the US Congress on July 2, 1890, which still left more than 80 percent of the world economy devoid of antitrust regulation. It was only in 1957, with the signing of the Treaty of Rome, that more than 50 percent of world Gross Domestic Product (“GDP”) was brought under an antitrust statute. The former Soviet republics enacted their own antitrust laws in the early 1990s, bringing nearly 70 percent of world GDP under antitrust scrutiny. With the enactment by China of its Anti-Monopoly Law on August 1, 2008, more than 95 percent of world GDP is now under antitrust scrutiny.

However, economists have not always agreed with this now-accepted belief. For example, in his 1932 book Cartels, Concerns and Trusts, the well-known (at the time) German economist Robert Liefmann stated that: “The possibilities of a rise in price resulting from monopolistic organization—and in particular from a merely contractual organization such as is a cartel—are generally greatly over-estimated.\(^1\) The cartels are quite unable to influence the prices of consumers’ goods, especially of goods in general use, to such an extent as might be expected having regard to the great number of monopolistic organization.”\(^2\) On the issue of consumer welfare, he states that: “In particular, we called attention to the greater stability shown by the coal syndicate’s prices since 1900, and showed that this is generally more beneficial to the consumer than violent price fluctuations on the scale of earlier years.”\(^3\) Finally, on the role of the state, he explains that: “Once the value of cartels as a means of regulating economic life came to be realized, the State ceased merely to obstruct their development and to eliminate the resulting abuses; it frequently went so far as to encourage them” (emphasis in original).\(^4\)

Similarly, on the industry side, cartels were considered beneficial to stability and a standard mode of operation potentially superior to competition. In a 1935 article from the French periodical L’Illustration, the director of the Toa cement factory in Japan was quoted as saying:

> By common agreement, we have reduced our production by 57%. The quantity we are allowed to produce is fixed every three months by our industrial union created 11 years ago. During the first five years, the period anticipated by the agreement that all industrialists had signed at the time, everything was fine. But during the second period, a certain number of industrialists wanted

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1. Robert Liefmann, a German economist born in 1874, was an internationally recognized expert on “business associations and cartels,” the field in which he obtained his Doctorate. He had toured the United States extensively in 1907, 17 years after the Sherman Act was enacted. Deported to the Gurs concentration/internment camp in France in 1940 for being Jewish, he died in 1941.

2. Robert Liefmann, Cartels, Concerns and Trusts 108 (1932).

3. Id. at 141.

4. Id. at 215.
to get their freedom back and, because of the fall in price resulting from this renewed competition, we found ourselves in an inextricable situation. We then asked the government to intervene and force all the cement manufacturers to abide by the orders of the industrial union. The law voted in December 1934, therefore very recent, has finally reestablished this obligation.\(^5\)

Despite the near-uniform agreement on the merits of antitrust enforcement today, conflicting views on what constitutes competition and appropriate economic evidence in competition disputes remain. While economists, lawyers, and triers of fact may interpret opposing positions as reflecting a misuse of economics, in the vast majority of instances, disagreement among experts reflects differing underlying beliefs about the interactions of firms and consumers, as well as differences in their understanding of competition in the market at issue. These may result from differing information or underlying assumptions provided by counsel or other experts. These differences translate into subtle methodological differences, some of which may affect the expert’s conclusion dramatically. For counsel, judges, and jurors, appreciating where and how economists agree, as well as the roots of their remaining disagreement, is often difficult. In this discussion, we propose a series of questions to consider to help focus on the root cause of common disagreements among economic experts in antitrust litigation.

II. Question 1: Establishing Common Ground: What Do Economists Believe?

Economists tasked with evaluating market dynamics and firm behavior to assess allegations related to collusion and monopolization offer analysis to clarify whether collusive conduct or abusive monopolistic conduct best explains pricing and production decisions. They may provide expert insight into how a market would have evolved but-for particular behavior by a group of firms or a single dominant firm. While their conclusions may diverge, a first useful step is to establish what economists on opposing sides of a case agree on. As a general matter, the drivers of economic activity—human behavior, organizational activities, and market operations—are widely agreed upon by economists across the discipline. Indeed, the underlying principles that shape economic analysis seem as natural to the vast majority of economists as the laws of physics:

» We all agree that incentives matter.

» We agree that firms generally maximize their profits while consumers maximize their utility, although we may disagree on how profits and utility should be measured.

» We acknowledge, through our use of discount rates, the importance of immediacy (i.e., something today is better than something tomorrow).

» We recognize that opportunity costs are an important driver of economic behavior, in that every choice results in the loss of the alternative choice. This means that individuals and firms make decisions at the margin.

» We view trade, when entered into freely, as making both sides better off.

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III. Question 2: What Methods Do Economists Rely On?

Beyond our shared underlying understanding of economic reality, economists typically rely on very similar methods to identify anticompetitive behavior. They can be divided into two categories. First, we all rely on economic theory, which is nothing more than the mathematical or graphical expression of our underlying beliefs about economic interactions. Second, we generally rely on statistical analysis, which provides a powerful set of tools to analyze data and construct alternative (“but-for”) scenarios. There is general agreement on the use of these tools. For example, on the theory side, our models typically recognize that because individuals make decisions at the margins, the concept of marginal cost as a determinant of price under competitive conditions is a good starting point for economic analysis. Similarly, we view the use of statistics to draw inferences about populations from a sample of observations as a good starting point. Notwithstanding disagreement about the application of statistical averages and the correct level of aggregation in the context of class-wide analysis, our set of statistical tools is common across experts, who generally rely on similar distributional assumptions and count on appropriate parameterization to ensure accurate results. We all rely on theory and/or econometrics (the application of statistics to economic data) as tools in antitrust litigation to evaluate a coherent set of issues, including:

» Market dynamics and organizational behavior;

» The role of collusive or unilateral conduct on pricing and production decisions; and

» The nature of any number of “but-for” worlds absent the behavior at issue.

IV. Question 3: Where Do the Differences Lie?

Despite this remarkable agreement around behavioral assumptions and methodologies, attorneys, judges, and juries are often confronted by dueling economic opinions that can result in polar-opposite conclusions. This is only rarely related to the application of “unprofessional” economic arguments. More often, it is the result of different views of what constitutes competition or subtle differences in the application of generally shared economic theories and statistical tools, the choice of data, or the consideration of external factors.

That the outcomes of these analyses can vary so drastically is a source of significant dismay by triers of fact and is a direct manifestation of minor discrepancies in economists’ understanding of the basic building blocks of the economic world. These subtle differences of opinion about the nature of competition or the determinants of production or demand can have significant consequences because they result in differences in the interpretation of empirical facts or the specification of statistical modeling.
V. Case Example: TFT-LCD (Flat Panel) Antitrust Litigation

Consider the litigation surrounding Best Buy in the matter of alleged cartel activity among thin-film-transistor liquid-crystal display (“TFT-LCD”) manufacturers. This lawsuit stemmed from a long-running US investigation of a conspiracy to set artificially high prices for, and restrict the supply of, various sizes of TFT-LCD panels. The plaintiffs claimed that the defendants had engaged in price-fixing since 1998, resulting in overcharges to direct purchasers of TFT-LCD panels and to indirect purchasers of finished products containing those panels (such as televisions and computer monitors).

In this litigation, two top economic experts presented opposing models to measure the alleged overcharges. Both experts are affiliated with respected universities and are widely recognized as highly qualified in their fields, having published numerous articles on the subject in highly ranked scholarly journals and having received numerous awards. Yet, they reached remarkably different conclusions in their economic analyses, particularly with respect to how to measure input costs:

» The plaintiffs’ expert modeled TFT-LCD panel prices as a function of several variables, including the price of microprocessors, which was used as a proxy for input costs, to demonstrate an overcharge of roughly 20 percent.

» The defendants’ expert found that by altering the specification used by the plaintiffs’ expert in a very minor way, namely by replacing the price of microprocessors with any number of alternative input price indexes, the overcharge was close to zero.

After a six-week trial and a day of deliberation, a California federal jury found the defendant Toshiba Corporation not liable for conspiracy to fix the prices of TFT-LCD panels. Defendant HannStar Display Corporation had previously acknowledged its participation in a conspiracy to fix the prices of certain TFT-LCD panels; however, the same jury awarded only $7.4 million in direct damages, based on figures calculated and presented by the testifying expert. The Best Buy plaintiffs had asked for $770 million in damages based on their economic experts’ analysis and overcharge estimate.

VI. Assessing Opposing Economic Arguments in the TFT-LCD Case

Given the complexity and sophistication of the economic analyses on both sides, what is counsel—or a jury—to do in circumstances such as this? A typical response has been to raise the Daubert standard: Is the analysis scientifically rigorous? For economic experts, the standard is sometimes thought of as a determination of whether the work done meets academic levels of rigor. While this strategy sometimes works, I purposely selected an example where the statistical analyses were standard and differed only in subtle ways between the two parties. It has also become increasingly apparent that economic analyses published in scholarly journals without the submission of data and without the testing of alternative

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6 In re TFT-LCD (Flat Panel) Antitrust Litigation, MDL No. 1827 (N.D. Cal. 2012).
specifications by referees cannot be as thoroughly examined as similar analyses presented in a litigation context where the opposing side has complete access to the underlying data and programs.7

Absent gross errors or the exclusion of one of the experts through a Daubert motion, what is the trier of fact to do? The TFT-LCD matter provides a concrete example of how to assess opposing economic arguments. Both experts proposed a statistical analysis to explain the price of TFT-LCD panels in order to isolate the effect of the conspiracy. Both agreed that various measures of costs and demand would be important determinants of prices with or without a conspiracy. In fact, they seemed to disagree principally on only one issue. Namely, they disagreed on whether the Producer Price Index (“PPI”) for microprocessors is an appropriate proxy for costs.8 The plaintiffs’ expert included the PPI for microprocessors in his analysis and found an overcharge resulting in damages of more than $700 million for all purchases and more than $230 million for direct purchases alone. The defendants’ expert took the identical model but replaced the PPI for microprocessors with any number of other PPIs for TFT-LCD panel inputs and showed that the overcharge became indistinguishable from zero, thereby suggesting de minimis damages. What is the jury to do in a situation like this? Ultimately, the right answer is a matter of belief rather than statistical modeling or theoretical equations.

“Is the PPI for microprocessors a good proxy for the cost of building TFT-LCD panels?”9 This is a perfect example of a fundamental disagreement between economists that does not involve the use or misuse of the tools of economics but rather a matter of disagreement in underlying beliefs. The question may be relatively easy to grasp for the trier of fact. Jurors may agree with the plaintiffs’ expert that the PPI for microprocessors is a necessary component of any good analysis of the determinants of TFT-LCD panel prices because, for example, they heard testimony that microprocessors represent a significant cost factor. Alternatively, they may believe that if substituting any number of alternative PPI into the analysis makes the overcharge go away, then the results are not robust and ultimately suspect since they may be the result of a fishing expedition. This, of course, would reflect a failure of methods as much as a disagreement between the experts.

Uncovering the fundamental disagreements in beliefs that underlie econometric or theoretical analyses are likely to be much more effective than trying to explain the relative merits of one statistical specification over another. Statistics and theory are only as good as the underlying assumptions, data, and phenomena that they translate. An alternative approach is to call in a third expert who can stress test the opinion of the two disagreeing experts based, for example, on the nature of the industry, the workings of the cartel, and the likelihood that it would result in successful price-fixing. Notably, a jury in Washington state reached a different conclusion regarding the same analyses when presented with a separate but similar litigation by the retailer Costco; that jury “split the difference” between the experts’ opinions and awarded higher damages.

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7 Based on recent instances of lapses in scholarly review, the academic standards that have served as a rubric in Daubert hearings may themselves become insufficient benchmarks of quality.

8 The defendants’ expert analysis was completed in the context of the broader observation that the modelling of TFT-LCD panel prices more generally was much more difficult and likely to result in error than the plaintiffs’ expert believed.

9 Although the issue is not relevant to this discussion, the plaintiffs’ expert argued that the PPI for microprocessors was appropriate because it was a good proxy for demand, since monitors and computers are complements.
VII. Conclusion

Over the last few decades, economists have reached a degree of consensus in antitrust unprecedented in recent history. Nevertheless, economic experts working in good faith can and do reach vastly different conclusions when applying similar economic theory and econometrics to the same set of facts and data. In practice, this means that strongly conflicting opinions do not automatically indicate that economic evidence is being misused. Instead, it reflects more subtle tensions in economists’ beliefs about human behavior, organizational activities, firm characteristics, and market dynamics, which all influence their development of models that describe their economic reality and that help define but-for worlds. Counsel play an important role by uncovering these underlying beliefs, understanding how they are translated into the economist’s theoretical or empirical construct, and assisting the trier of fact in evaluating the relative merits of the two positions.