MONOPOLY AND THE JUST PRICE

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WHEN Parliament passed the Monopolies and Restrictive Practices Act in 1948, it acted on the belief that monopolies were capable of harming the public interest, although they did not necessarily do so. It provided for the establishment of a Commission which would, at the request of the Board of Trade, investigate the behaviour of particular monopolies,[1] and would report whether or not these monopolies were behaving in an anti-social manner. If they were acting contrary to the public interest the Government might make an Order requiring the monopoly to amend its behaviour, although in the majority of cases it has, in fact, chosen to rely upon reaching an informal agreement with the monopoly. The Monopolies Commission has completed eleven such investigations, and the Government has already acted upon most of the Commission's reports. About the middle of 1955 the Commission completed its first report on a 'general reference'.[2] In the case of such a reference the Commission was required to consider the general effect, over the whole of industry, of specified restrictive practices. The Act made no provision for Government action on such a report, which would therefore have no effect unless industry voluntarily amended its practices in the light of the Commission's judgments, or unless the Government made the report the basis of new legislation. The Government has now introduced a Bill to deal with the practices covered in this report.[3]

I do not propose in this article to discuss in detail either the findings of the Commission or the proposals of the Government. I want instead to pursue a line of thought suggested by the Commons debate on the report and a comment thereon by Fr Paul Crane, S.J. In the course of the debate, the President of the Board of Trade, Mr Peter Thorneycroft, suggested that, although these

1 The Act allows a reference to the commission where a single firm or cartel controls one-third of the supply of a commodity. It also applies to the export and processing of goods.

2 Monopolies and Restrictive Practices Commission, *Collective Discrimination* (H.M.S.O., 1955).

3 The Restrictive Trade Practices Bill also applies to practices not covered by the report on collective discrimination.

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discriminatory practices might be harmful, they were neither criminal nor morally repulsive.[4] Fr Crane, on the other hand, argued that these practices were part of the technique for acquiring a monopoly position in which it would be possible to increase profits by restricting output and raising price above the competitive level (competitive price being identified, at least approximately, with the just price).[5] In his statement, however, Fr Crane was forced through lack of space to accept a very simplified picture of monopoly behaviour. It is therefore necessary to look a little more carefully at this problem, especially at a time when moral considerations are all too rarely applied to economic questions.

The first step must be to set out the accepted teaching of the Catholic theologians on the subject of the just price.[6] There appears to be general agreement amongst them, from Albertus Magnus in the thirteenth century to Cardinal de Lugo in the seventeenth, that the just price is determined by the common estimation of intelligent people, and that this means, in the absence of price regulation by the civic authorities, the market price. The schoolmen did not, as some modern historians have suggested, put forward a labour theory of value, holding that the just price was determined solely by what was necessary for the proper maintenance of the producer. This was one factor entering into the determination of the just price, *through* the common estimate, but it was not the sole factor, nor the most important. Greater stress was laid upon the 'utility' of the article, that is, its power to satisfy human needs and desires. The identification of the market price with the just price, however, presupposed the absence of fraud and compulsion. The former requires no comment. Compulsion, it must be noted, included monopoly, where the buyer was compelled to purchase, if at all, from a particular seller, and on the conditions laid down by that seller.

Where competitive conditions exist in modern industry, the market price may safely be taken to be the just price. In a com-

4 Hansard, 15th July 1955, col. 1942. Whether these practices should be made criminal offences is, of course, a matter of expediency. Many acts which are immoral are not made criminal offences.

5 *Catholic Herald*, 29 July, 1955.

6 My treatment of this subject is based on the essay by Fr Lewis Watt, S.J., 'The Theory lying behind the Historical Conception of the Just Price', in *The Just Price*, edited by V. A. Demant (S.C.M. Press, 1930).

petitive market there are many buyers and many sellers.[7] If the buyers find that one seller is charging more than others they are free to take their custom elsewhere, and under such conditions price differences cannot persist. In the short run, price is determined by the buyers' common estimation of the article's worth. In the long run, if there are high profits resulting from high prices, new firms, which are free to enter the industry, will do so and the increase in supply will bring down the price of the article until the level of profits is such that there is no incentive for firms to enter the industry.[8] Thus, under competitive conditions the average level of profit is determined by what is acceptable to the generality of producers, and no firm is able to increase its profits by restricting output in order to raise price, though it may increase them by improving its efficiency. Price, therefore, is determined by the buyers' common estimate of the worth of the article, and by the producers' common estimate of what constitutes a fair rate of profit.

The monopolist, however, is in a different position. The price of the commodity is still determined by the buyers' common estimate of its worth, but with this difference. The monopolist can control the amount he puts on the market. If he restricts the supply there will be increased competition among buyers and the price will be raised. Orthodox economic theory is based on the assumption that the aim of the monopolist is to maximize his profits,[9] and it was monopoly behaviour of this kind that Fr Crane rightly castigated as unjust. The important question is how far profit maximization is the typical form of monopoly behaviour.

We must not lose sight of the fact that today many monopolies are inevitable. It is no longer a case of the merchant buying all the grain coming to market in order to exploit the buyers. Many industries can now only be efficiently organized on a large scale, and where demand is limited monopoly is inevitable. The fact that such monopolies are not contrived to exploit the consumer does not alter the fact that they have the power to do so.

7 It is assumed, of course, that there is no agreement among sellers to fix prices.

8 Similarly, if profits are unduly low, firms will leave the industry.

9 This he does by restricting output to the point where the additional cost incurred by increasing output is just equal to the additional revenue earned by the sale of the increased output. The additional revenue is the price received for the additional output, less the amount by which price is reduced (in order to sell the greater output) on the previous output.

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Not all monopolies will exploit the public, and few will do so to the fullest extent of their powers. The monopolist is not entirely unresponsive to public opinion, and does not wish to attract unwelcome publicity by making too great a use of his power, though usually it will be safe for him to exploit the public to a limited extent. Another restraining factor is the difficulty of maximizing profits. The economic theorist assumes that the monopolist has full knowledge of his costs of production and of the demand for his product. In fact he is likely to have but an incomplete idea of the way in which his costs vary with output, and certainly only a rudimentary idea of how demand varies with price. In the absence of such knowledge, profit maximization can only be a hit-and-miss affair, and it may be doubted whether many monopolists would consider an attempt at profit maximization worthwhile.

Empirical data also suggests that not all monopolists exploit the public. In its *Report on the Supply of Insulin* the Monopolies Commission had nothing but praise for the manufacturers, though these were in as strong a monopoly position as could be imagined. In its other investigations the Commission rarely found unduly high levels of profit. The most striking case of high profits it encountered was in the dental goods industry, and these high profits were earned on the supply of certain new plastic products, the demand for which was expanding rapidly.[10]

There can be no doubt that it is wrong for the monopolist to restrict output and raise price in time of prosperity in order to earn greater profits. Is it equally wrong for him to use similar methods in time of depression in order to maintain a normal rate of profit? There is a widely held view that in time of depression monopolistic measures are justified, and in the past such measures have even been initiated by the Government. In general such a policy is mistaken. It does nothing to promote general recovery from the depression, and improves the position of one industry at the expense of others. In exceptional circumstances, where an industry is particularly vulnerable to depression, and where fierce competition may drive prices well below the cost of production,

10. It is probable that the high rates of profits were mainly due to the rapid increase in the demand for the new product. High profits would normally be expected in such conditions in a competitive industry, for it may be difficult to increase productive capacity as rapidly as demand, and shortages will force up the price.

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it may be justifiable to afford it monopolistic protection.[11] This problem becomes particularly serious where an industry is hit not by general depression but by a permanent decline in the demand for its products.[12] Continued losses mean that firms are unable to maintain their capital intact, and cannot afford to replace obsolete machinery; thus, after a time, even the reduced demand cannot be met efficiently.

Economic theory has always tended to assume that abnormally low profits would rapidly lead to the exodus of firms from the industry, so that competition would become less intense, and prices would rise, and the remaining firms would be covering their costs.

In practice, firms are reluctant to give up the ghost. Their specialized plant has only a small scrap value, and they are likely to continue producing so long as they are earning more than enough to cover their prime costs. So long as all firms adopt this line, prices will remain below the level at which firms can afford to replace their worn-out and obsolete equipment; and it may be a long time before sufficient firms go out of business, as their plant finally becomes unusable, for the level of prices to rise again. While it is certain that in such conditions competition is not advantageous, it is doubtful whether the type of monopolistic measures usually adopted are entirely satisfactory, since these involve buying out the weaker firms, and so imposing additional charges upon the firms that remain in the industry.[13]

11 To operate a large plant for a small output is wasteful. Firms are anxious to keep their plant running to capacity and reduce prices in order to obtain orders. They continue to reduce prices so long as these cover prime costs, i.e. such items as raw materials and wages of direct labour. If these costs are not covered it is more profitable to cease production altogether. When a firm reduces prices it may attract custom from other firms, but this is lost when others follow suit. In many industries, where total demand is unresponsive to price reductions, this means that all firms have slashed prices to attract custom from each other, since there is no significant increase in total demand, and none are better off as a result of the price cuts.

12 For example, the problems of the Lancashire textile industry arise from the loss of export business accompanying the development of the textile industries of Japan and India.

13 It is a common plan for the firms that remain in the industry to buy out their weaker brethren. The industry remains monopolistically organized, and the remaining firms are able to exploit the consumer by restricting output and raising prices, though no abnormally high profits will appear to be earned since the remaining firms will include in their capital sums paid to buy out the firms that have ceased production. The ideal arrangement would be to eliminate the weaker firms swiftly, and then allow competition to be resumed. A levy on firms in the industry to provide the funds to buy up the excess capacity would not be objectionable, but the firms that remained would not have the power to exploit the consumer, by forming a price ring. The levy would be an outright loss to the firms remaining in the industry. There is no moral objection to

The case against monopoly is not only that by restricting output and raising prices it offends against commutative justice. Fr Crane pointed to the effect of monopoly on the right to work and on economic efficiency, and suggested that in these two respects monopoly offended against social justice. It is doubtful whether monopoly restricts the number of jobs open to the worker. Jobs in one industry may be limited in number as a result of monopolistic restrictions on output, but the existence of monopolies is not incompatible with full employment.[14] A more serious result of monopoly is the general lowering of the wage level. Monopoly will, in the first place, reduce the demand of the monopolised industry for labour, and displaced workers can only be absorbed by other industries at lower wages.[15]

Monopoly also restricts the freedom of individuals to enter an industry and to invest their capital in it. This is seen clearly from the reports of the Monopolies Commission, particularly those dealing with collective monopolies. In a collective monopoly a number of firms, usually organized in a trade association, decide to limit competition by fixing common prices. (Usually such schemes for common prices will be accompanied by quota arrangements, which fix firms' share of the total demand.) In so far as such arrangements raise price above the competitive level there is a presumption that they are immoral. The case against such policies is even stronger when they are supported by other practices which deny the public the services of firms willing to accept lower prices. The most commonly used device for this purpose is exclusive dealing. Associated manufacturers may sell only through distributors who agree not to handle the products of independent competitors, and may stop supplies to distributors who do not abide by such agreements.[16] Where the associated

this. Profits are supposed to be the reward of enterprise and risk-taking. If firms wish to justify the profits they receive in this way they must be willing to meet losses when things go against them. They cannot expect to be allowed profits in good times as a reward for risk-bearing and then ask to be cushioned by monopoly against losses in bad times.

14 The immediate effect of the introduction of monopolistic restrictions is, of course, to create some unemployment. This may be particularly serious for skilled men who cannot find comparable work in other industries.

15 Output in these other industries will be increased. The greater output will be sold at a lower price, and wages will therefore have to fall. (This tendency may be strengthened by a fall in productivity as more men are employed.) Thus the burden of monopoly does not fall entirely on the consumer but is partially shifted on to the worker in the form of lower wages.

16 An alternative method is to offer a financial inducement to exclusive dealing.

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manufacturers control the greater part of the output of an industry, distributors are not likely to sacrifice trade with them in order to stock the goods of the independent firms, and these firms are therefore unable to place their goods before the public.[17]

It is commonly alleged that monopoly breeds economic stagnation. The empirical evidence on this subject is conflicting. Some monopolies, like the cotton-spinning machinery industry, have been shown on investigation to be inefficient, to some extent at least, whereas others, like the weaving machinery industry, have been found fully efficient. Deductive reasoning, however, confirms the belief that certain forms of monopolistic practice reduce the level of efficiency in an industry. In several of its reports the Monopolies Commission has argued that quota systems, which determine the pattern of output over a long period, reduce efficiency by preventing the relative expansion of the more efficient firms.

In his note in the *Catholic Herald* Fr Crane rightly rejected nationalization as a solution for the problems of monopoly. Instead he suggested the restoration of healthy competition in industry. This is undoubtedly the best remedy where practicable. Most of the cases investigated by the Monopolies Commission have been ones of monopoly power exercised by trade associations, with arrangements for price fixing supported by such devices as exclusive dealing. It would be possible to restore some measure of competition to these industries by outlawing devices that handicap independent producers, even if members of associations were left free to agree among themselves upon minimum prices. The report of the Commission on collectively administered schemes for discrimination called for the outlawing of these practices (with provision for granting exemptions in a small number of special cases). The Bill now introduced provides for the registration of a wide variety of restrictive practies, including the fixing of common prices and level tendering, as well as the devices to handicap competitors that were considered in the report on collective dis-

17 Associations operating such schemes have suggested that the distributor who fails to honour such an agreement to deal exclusively in their goods is not deserving of sympathy if his supplies are stopped. In the ordinary course of events it is certainly dishonourable, if no more, to break one's word. In cases of this kind, however, it can well be argued that the agreements are made under duress and are not, therefore, morally binding.

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crimination.[18] Each agreement will be liable to investigation by a newly established court, which will decide whether or not the practice is justified and should be allowed to continue. It has been made clear, however, that the firms wishing to continue to operate their agreement will have the onus of proving that it is in the public interest. If the new Bill proves to have real teeth, then there may well be a considerable increase in the degree of competition in many industries. The work of the Monopolies Commission will be much reduced, but it will continue to deal with cases of single firm monopolies, which do not come within the scope of the new Bill.[19]

18 The collective enforcement of resale price maintenance (the process whereby a manufacturer fixes the price at which retailers and others may sell his product) is made illegal. If an association stops supplies to a retailer who has cut the price of goods supplied by any member of the association, the retailer will have a remedy in the civil courts. On the other hand, the power of the individual manufacturer to enforce resale prices will be increased if the clause is passed giving him the right to take legal action against a retailer with whom he has no contract but who has been given notice of the conditions of price maintenance.

19 The Commission will also deal with agreements relating solely to the export trade.