

GOVERNMENT REGULATION IS GOVERNMENT MONOPOLY:

THE EXAMPLES OF BRITISH AGRICULTURE AND THE BRITISH STOCK EXCHANGE

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Pretty much everyone agrees that monopolies — government-run or government-backed, coercive controls over the production, distribution or purchase of particular categories of product or service — are bad for society, i.e. for pretty much everybody. One only has to remember the record of British Leyland — a government industrial monopoly that did considerably more damage to the British motor industry than the Luftwaffe — to see that monopolies are harmful.¹ The only exception to this generally agreed belief seems to run along the lines of “all monopolies are bad *except when I or my friends are in control*”, which helps to explain why monopolies are so popular with governments.

So this essay will not attempt to argue that monopolies are bad, any more than it will attempt to argue that the earth is round. The point I wish here to make is that monopolies, because they are so much more numerous, are accordingly causing *much more* harm, than is commonly thought.

I will focus on two examples, both of which show a monopoly in action and doing great harm, even though at first glance there doesn't appear to be any monopoly at all.

EVERY GOVERNMENT REGULATORY AGENCY IS A MONOPOLY

The first example is the long running saga of BSE. Bovine Spongiform Encephalopathy is a disease suffered by British beef cattle during the nineteen eighties and nineties, which is believed to be caused by unsatisfactory feeding practices — feeding bits of cows to other cows. Creutzfeldt-Jakob Disease (CJD), which is a similar and fatal disease suffered by a tiny handful — so far — of humans, is now believed to result from eating BSE infected meat. This circumstance lead to a European Union ban on all British beef exports, which at the time when this essay was written (January 1998), was still in place. Since December 1997 there has also been a British government ban on the sale within Britain of beef on the bone.

However you look at it, a great deal of evil has been caused here — possibly people exposed to a dangerous disease, certainly a major export industry blighted, many businesses bankrupted, consumers (that's you and me) denied the right to choose what we eat. And as usual it's a combination of small businesses and taxpayers (you and me again) who are going to pay for it all. But the evil is due to the disease, or to the greed of farmers, or their shocking lack of respect for the order of nature (feeding bits of cows to other cows), or else to the government failing to enforce hygiene standards. Isn't it?

After all, the beef industry consists of many different farmers selling to many different buyers (leaving aside EU interference). Not a monopoly in sight.

Wrong. The whole problem goes back to a monopoly fundamentally affecting the entire farming industry — the Ministry of Agriculture's Food Hygiene Service, which sets the standards of beef production hygiene, amongst a whole world of other things. It's important to realise that *every* government regulatory agency is a monopoly, in the definition given in the first paragraph of this article. It controls, in this case, aspects of the production and distribution of *all* beef in this country. It has the full backing of the law to do this. The result is that *all* farmers follow the procedures laid down by the standards monopoly. A monopoly by definition means that you put all your eggs in one basket, so when something goes wrong it goes wrong on a massive, massive scale.

If there were no government-backed standards monopoly, but instead different farms in a truly free market, there might still have been a BSE problem, caused by ignorance of the problems involved in recycling beef, until these became known. To that extent this evil was probably unpreventable. However, in a free market different farms would offer different standards of hygiene as part of their attempt to gain market share in a highly competitive industry, and would market and price their product accordingly, allowing you and me the right to make our own choice on the available information.

But with a standards monopoly the extent to which this will happen is severely limited. For here's another important point. The level of hygiene standards set by the monopoly, as with any other level it sets is not only the minimum, but also the maximum level. No farmer will waste money enforcing stricter standards on his farm, for remember, his customers have been told that his competitor down the road, doing the minimum amount necessary, is doing all that is necessary.

THE ORGANIC FARMERS ALSO SUFFERED

The farmer can't compete on hygiene quality, so other than to meet the minimum standard in the cheapest possible way, it's not a priority for him. As usually turns out to be the case with government monopolies, the result is the very opposite to what is intended.

The exception to the rule serves to prove it — the so-called “organic” farmers, who have long preferred more “natural” methods of feeding their animals to the ultra-cost-conscious practices of the farming majority. The organic farmers *did* market their product at least partly on the grounds of hygiene quality, but only at the extreme upper end of the market at much greater cost than “normal” beef. This meant that organic beef farmers, having ignored the standards monopoly by in effect setting themselves up as a separate industry of *organic* rather than *normal* farmers, were producing entirely safe beef. But it didn't help them. Enter the monopoly again, who ordered the destruction of *all* beef cattle over a certain age, *including organically reared cattle that everyone agreed were safe*. It was as clear an abuse of monopoly power as anyone could want.

THE CLAIM TO MONOPOLISE RELIABLE INFORMATION

Central to this last twist in the saga is another important aspect of monopolies, both a source of and an aspect of their power: monopoly of information. This is reinforced by the hygiene standards



Economic Notes No. 79

ISSN 0267-7164 ISBN 1 85637 401 7

An occasional publication of the Libertarian Alliance,
25 Chapter Chambers, Esterbrooke Street, London SW1P 4NN
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The views expressed in this publication are those of its author, and not
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monopoly's claim to disinterestedness: the standards monopoly neither benefits nor suffers financially from the level of hygiene it sets, therefore it will set the right one.

But the BSE story was very different. First, any problems were covered up. Then, many would argue, these problems were blown totally out of proportion. So far we have tacitly assumed that there is a BSE problem. Yet nothing that I, as an interested member of the public, have been able to find out tells me that there is any significant risk to eating beef on the bone, even if I deliberately chose to eat super-discount beef from BSE infected cattle. Which-ever side the truth lies on, the standards monopoly's claim to monopolise the reliable information has made it harder for consumers to make their own decisions. And in any case, the monopoly has made our decisions irrelevant. Whatever I think, I can't eat that beef, and that's that. Because of the monopoly.

The BSE case is illuminating because it demonstrates that anywhere there is a government regulatory agency — and how many are there? — there is a monopoly. And I'm willing to bet large sums that that monopoly will either be (a) expensive but powerless, or (b) a source of evil in the world. Despite the generally acknowledged badness of monopolies, government regulatory monopolies, because they are not usually recognised as such, proliferate. They are usually marketed as the solution to a problem which they then make worse. Monopolies are attractive because of the *control* they appear to offer, yet by its very nature this control destroys market signalling and sensitivity. Monopolies act as a sort of black hole of information — any information on the industry they control doesn't come back out except in a distorted form. And this is the case even if the people running the monopolies are total altruists without any prejudices whatsoever.

THE STOCK EXCHANGE MONOPOLY

The second example I shall offer not only reinforces the points made above, but will show that much of the evil in this country can actually be traced back to one monopoly alone, perhaps the most insidious of them all.

There was much tabloid complaint about the vast fortunes paid to the directors of newly privatised monopolies. Yet there are plenty of examples in non-monopolistic industries of abuse by senior managers.

Consider the very existence of golden parachutes. I run a company. The company does badly. The shareholders lose a fortune. It is decided to get rid of me — so I'm given a hundred thousand pound handout, in addition to my pay, as a leaving present. Given this kind of abuse, socialism starts to look attractive, especially if the company is simultaneously firing many of its mere workers. Few people object to Richard Branson making his money, but this sort of thing sticks in the throat of even the most committed free-marketeer. And quite rightly so, for it has nothing to do with free markets.

Most such abuses can be traced back to two things. First, most of the big executives sit on each other's boards. They hire each other, and so vote each other nice little deals. And the second factor is the nicest deal of them all — the three year rolling contract. This means that a company director is hired not for three years at a time, but for three years into the future, continuously updated. The company is legally obligated to keep him, at his present rate of pay (and often even taking into account projected pay increases and bonuses) until three years from the date of giving him notice. So if he does prove to be incompetent, the only way to get rid of him is to pay him enough to compensate for the loss of three years projected (usually quite high) earnings. In fact it's worse than that, because unless you want a person you've just fired running your company for the next three years you'd better pay him more to agree to leave.² No non-executive company employee can come up with such a heads-I-win-tails-you-lose employment contract, not even in the heyday of the unions. How on earth, in a supposedly free market, is this possible?

It isn't. The market is fundamentally unfree, because there's a government instituted monopoly at the very centre of it. Ultimately the owners of the vast majority of shares, whether directly or through pension and asset funds working on our behalf, are you and me. So when this kind of thing happens, why on earth can't we just phone

up and say "do that and I'll sell my shares"? Because we can't own shares directly.³ I have to hire someone else to buy and sell them for me — a government law, a government monopoly. This one is called the Stock Exchange. It works by licensing, and thus strictly limiting the people allowed to deal in shares. A company with listed shares can only trade them on the Stock Exchange through stock brokers, and they will be subject to the rules of the Stock Exchange. It's not a free market.

Furthermore it costs a minimum of half a million pounds to get a Main Board listing, followed by regular and expensive compliance requirements every year — such as a monopoly set price you pay to have your shares listed in newspapers.

This monopoly was, as usual, set up with the best of intentions, to prevent charlatans selling to us poor, naive members of the public worthless shares in bogus companies. (Since when, of course, such an abuse has never occurred again. And the Titanic never sank.) And, as usual, the result was the opposite. Us poor, naive members of the public were denied the right to make our own decisions using whatever information we could get access to — unless we can afford the cost of paying a Stock Broker every time we wish to buy and sell shares. It's as if you were legally compelled to pay someone else every time you wanted to buy something in a supermarket.

Anyone who's bought a house may recognise these problems. Or anyone who's ever hired a lawyer. The rights to practise in law and real estate are controlled by government licensed agencies. So it doesn't matter how many lawyers or real estate agents there are, they all offer the same service in the knowledge that they aren't about to face cut-price competition.

A GOVERNMENT-BACKED MONOPOLY AT THE HEART OF CAPITALISM

The end result of the Stock Exchange monopoly is to reduce competitiveness in every industry in the country that is dominated by publicly listed companies. (For example, around 10% of money raised by a company on the Stock Market will go on the cost of raising it, through regulatory fees). Thus it reduces national economic growth, increases unemployment, and reduces the level of service to you and me. The socialists were right about there being grave abuses in the capitalist system (loony though their "solutions" may have been) but it was the lack of a free market, the imposition of a government-backed monopoly at the heart of capitalism, that caused them.

So, next time you hear a report on the news and you think to yourself "that's ridiculous/outrageous/just bloody stupid", look carefully. It may be well hidden; we may take it for granted because we've simply grown used to it; but I'll bet you the reward for bankrupting Barings that there's a monopoly at the root of it.

NOTES

1. Or for a more recent example, ask the Canadians. As Eastern Canada experienced its worst winter for 77 years, Canadians froze because the giant state utility Hydro-Quebec was able to supply power only to keep ablaze the giant illuminated Q at the top of its own headquarters. Yet just over the border the many small private utility companies of Vermont and New Hampshire kept their customers warm. The irony is that part of the rationale for creating the Canadian monster was to produce a national champion to stand up to the Americans across the border (*Daily Telegraph*, 27th January 1998).
2. Here's a recent example, from the city pages of the *Daily Telegraph* on the day I wrote this article, 30th January 1998. Two directors of Frederick Cooper, an architectural hardware company, were paid £1.1m between them, when they resigned following a collapse in the company share price caused by continual poor performance. As the men were respectively the company's chief executive and its finance director it's reasonable to assume they were largely responsible. But they were both on three-year rolling contracts. The comment of Frederick Cooper's chairman and acting chief executive says it all: "What can you do when you're given advice that this contract has to be honoured?"
3. Well, you *can* arrange to buy the shares of a Public Limited company privately direct from their current owner. But the company doesn't have to recognise the sale unless it's been registered by the company registrar, who can charge you for doing so. And whenever you sell shares you pay stamp duty, a percentage of the value of the shares. So the more your shares increase in value, the more it's going to cost you to realise that increase in value. The same applies to houses, with similarly distorting effects on the housing market.