Let’s Play Monopoly

Read the article and answer the questions that follow.

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By Robert J. Barro

It’s almost the end of summer and time for the first annual contest to choose the best operating monopoly in America. The contestants, selected by a panel of Harvard economists, are as follows:

1. The U.S. Postal Service
2. OPEC
3. Almost any cable-TV company
4. The Ivy League universities (for administering financial aid to students)
5. The NCAA (for administering payments to student-athletes)

Some other worthy candidates, which just missed the cut, are the National Football League, the American Medical Association and the U.S. Departments of Agriculture and Defense.

Each contestant exhibits fine monopolistic characteristics and is worthy of serious consideration for the award. The U.S. Postal Service claims to be the longest-running monopoly in America and has the distinction of having its control over first-class mail prescribed (perhaps) by the Constitution. The monopoly has preserved large flows of revenues and high wage rates despite studies showing that private companies could carry the mail more efficiently at much lower cost.

On the other hand, the position of the Postal Service has been eroded: first, by successful competition on package delivery; second, by the recent entry of express-delivery services and third, and potentially most damaging, by the introduction of the fax machine. Since faxes are bound to supplant a substantial fraction of first-class letters, the failure to get Congress to classify a fax as first-class mail and, hence, the exclusive domain of the Post Office shows a remarkable loss of political muscle. Thus, despite past glories, it is hard to be sanguine about the long-term prospects of the Post Office as a flourishing monopoly.

Good Guys and Bad Guys

OPEC was impressive in generating billions of dollars for its members from 1973 to the early 1980s. To understand the functioning of this cartel, it is important to sort out the good guys from the bad guys. The good guys, like Saudi Arabia and Kuwait, are the ones who have typically held oil production below capacity and thereby kept prices above the competitive level. The bad guys, like Libya and Iraq (when Iraq was allowed to produce oil), are the ones who have produced as much as they could and thereby kept prices low.

The good guys were responsible for the vast expansion of oil revenues during the blissful period after 1973. (Hence, they were responsible for the considerable difficulties endured by oil consumers.)
But, unfortunately, these countries could not keep the other OPEC members in line and were also unable to exclude new producers or prevent conservation by consumers. Thus, oil prices plummeted in 1986 and only the start of the Persian Gulf crisis . . . [in 1991] could get prices temporarily back to a respectable level.

In any event, it is unclear that OPEC qualifies for the contest: It is not really American, and its members would probably be arrested for price-fixing if they ever held an official meeting in America.

Most cable-TV companies have government-issued licenses that keep competitors out. Thus, this business supports the hypothesis (offered, I think, by George Stigler) that private monopolies are not sustainable for long unless they have the weight of government behind them.

**Fear About the Future**

The rapid escalation of prices and the limitations on services seem, however, to be getting customers and their congressional representatives progressively more annoyed. Thus, it would not be surprising if legislative action leads soon to a deterioration of the cable companies’ monopoly power. It may even happen that consumers will be able to choose among cable companies in the same way that they choose currently among long-distance telephone carriers; how could the struggling providers maintain a respectable cartel in that environment? This fear about the future diminishes the claim of this otherwise worthy contestant for the first annual prize.

Officials of Ivy League universities have been able to meet in semipublic forums to set rules that determine prices of admission (tuition less financial aid) as a function of applicant characteristics, especially financial resources. In some cases, the schools pooled information to agree in advance on the right price to charge a specific customer. Airlines and other industries that wish to price discriminate can only dream about this kind of setup.

Moreover, the universities have more or less successfully applied a high moral tone to the process: Rich applicants — especially smart rich applicants — are charged more than the competitive price for schooling in order to subsidize the smart poor, but it is unclear why this subsidy should come from the smart rich rather than from taxpayers in general.

In any event, the universities’ enviable cartel position has been damaged by the unenlightened Justice Department, which argued that the price-setting meetings were a violation of antitrust laws. Since most of the universities involved have agreed to stop these practices, it may be that future prices for private higher education will come closer to being competitively determined. It seems that this prospect has already motivated some distinguished universities to declare themselves as being in financial difficulty.

**Remarkably Successful**

The final contestant, the NCAA, has been remarkably successful in holding down “salaries” paid to college athletes. It would be one thing merely to collude to determine price ceilings (for example, to restrict payments so that they not exceed tuition plus room and board and some minor additional amounts), but the NCAA has also managed to monopolize all the moral arguments.
Consider a poor ghetto resident who can play basketball well, but not well enough to make it to the NBA. If there were no NCAA, this player might be able legitimately to accumulate a significant amount of cash during a four-year career. But the NCAA ensures that the player will remain poor after four years and, moreover, has convinced most observers that it would be morally wrong for the college to pay the player a competitively determined wage for his or her services.

For many economists, this interference with competition — in a setting that has no obvious reasons for market failure — is itself morally repugnant. But the outrage is compounded here because the transfer is clearly from poor ghetto residents to rich colleges. Compare the situation of contestant number 4, the Ivy League universities, in which the transfer from rich to poor students can readily be supported on Robin Hood grounds.

The NCAA has the much more difficult task of defending a policy that prevents many poor individuals from earning money. Incredibly, this defense has been so successful that it has even allowed the organization to maintain the moral high ground. When the NCAA maintains its cartel by punishing schools that violate the rules (by paying too much), almost no one doubts that the evil entities are the schools or people who paid the athletes, rather than the cartel enforcers who prevented the athletes from getting paid. Given this extraordinary balancing act, the decision of the panelists was straightforward, and the NCAA is the clear and deserving winner of the first annual prize for best monopoly in America.

The panel of economists also considered briefly an award for the least-efficient monopoly in America. This choice was, however, too easy. It goes to the American Economic Association, which has been a dismal failure at establishing licensing requirements or other restrictions on entry into the economics profession. It is a sad state of affairs when almost anyone can assume the title of economist.
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1. Do you agree or disagree with the final contestants for the monopoly award? Explain.

2. How might e-mail change the market for first-class mail?

3. What prevents a cartel, particularly OPEC, from maintaining a long-run monopoly? What would help to make it more successful?

4. What are the standard arguments against monopolies? What example is provided in the reading that emphasizes these arguments?

5. What is price discrimination and under what conditions is it successful?
6. Why doesn’t the NCAA have competition in providing a forum for young athletes to play sports?

7. How does leaving college early to go pro or going pro directly from high school affect the NCAA monopoly?

8. Why are monopolies considered to be bad? Be sure to discuss price, output and efficiency in your answer.