



# Competition and regulation

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## Overview

- Competition and regulation: conceptions and principles
- Common issues and situations



## Competition and performance

- Competition
  - Disciplines exchange in markets
  - Facilitates response to change in economies
- Better performance follows stronger competition.
  - Not just in economic theory about perfect competition
  - But in practical experience: policies to promote competition promote growth and employment.



## “Competition” means “markets”

- “Competition” is characteristic of a sound, open enterprise economy.
- Pro-competitive regulatory policies respect market exchange as the principal means of allocating resources.
- The quality of framework laws and institutions supporting markets is highly important.



## Competing concepts in “competition”

- Rivalry
  - opportunity for producers
  - choice for consumers
- Efficiency
  - productive: lower costs
  - allocative: better use of resources
  - dynamic: innovation, flexibility, resilience
- Fairness



## OECD research

- Improving regulation about private governance and opening up access to markets where competition is economically viable would:
  - Increase investment by 2-3 percentage points;
  - Increase foreign direct investment by 20% overall, and up to 80% in some countries; and
  - Reduce the (multi-factor) productivity gap with high-productivity countries by 4-10%.
- Regulation and Economic Performance: Product Market Reforms and Productivity in the OECD (Nicoletti and Scarpetta, 2005)



## OECD research II

- Reforms related to trade liberalisation – tariffs, constraints on foreign investment and regulation affecting inward trade – would raise productivity and GDP per capita by up to 4.5%.
  - The benefits of liberalising product markets and reducing barriers to international trade and investment in the OECD (OECD, 2005)



## Long term trends

- Above-average growth, 1980s and 1990s:
  - Australia, Ireland, Korea, United States
  - Each was reducing barriers to entry and competition or strengthening competition policy and enforcement in this period.
- Below-average growth, 1980s and 1990s:
  - Belgium, Denmark, France, Germany, Greece, Italy, Switzerland
  - Competition-based reforms here were less ambitious.



## Reform programs and results

- Australia
- Ireland
- Korea
- Netherlands
- New Zealand
- United Kingdom
- United States



## Links between regulation and competition law

- Competition “policy” and competition “law”
  - Competition law: Rules about conduct of enterprises
  - Competition policy: Principles about rules and decisions of authorities
  - Common goal: Support market competition – entry and choice – in order to improve welfare
- Competition “law” problems reveal regulations that need reform
  - Frustration of opportunities due to exclusion
  - Inefficiency of outcomes due to collusion and monopoly



## Conflict of law and regulation

- Between competition law and other laws
- Between competition law enforcers and other regulators and agencies
- Between national competition law and rules or actions at other levels of government
- Between competition law and policies that create market power



## OECD Guiding Principles

- 1: Reform programs
- 2: Systematic review
- 3: Transparent process
- 4: Strong competition policy
- 5: Pro-competitive economic regulation
- 6: Market openness
- 7: Policy linkages



## 4. Strong competition policy

- *Review and strengthen where necessary the scope, effectiveness and enforcement of competition policy.*
  - Eliminate gaps and co-ordinate with regulators
  - Enforce vigorously and impose sanctions that deter
  - Empower competition authorities to advocate reform



## 5. Pro-competitive economic regulation

- *Design economic regulations in all sectors to stimulate competition and efficiency, and eliminate them except where clear evidence demonstrates that they are the best way to serve broad public interests.*
  - Review regulations to remove constraints
    - On entry, access, exit, pricing, output, normal commercial practices and forms of organisation
  - Ensure that benefits outweigh costs, and that
  - Alternatives cannot meet objectives with less effect on competition



## 5. Pro-competitive economic regulation II

- Promote efficiency in economic regulation of market power through
  - Separation of competitive elements
  - Access to essential facilities
  - Interconnection of contiguous networks
  - Price controls that encourage efficiency
- Promote consumer choice
- Review state involvement
- Review universal service programs



## 6. Market openness

- *Eliminate unnecessary regulatory barriers to trade and investment through continued liberalisation and enhance the consideration and better integration of market openness throughout the regulatory process, **thus strengthening economic efficiency and competitiveness.***



## Consistency of competition with regulation

- Is regulatory policy **consistent** with the conception and purpose of competition policy?
- Regulation can ...



... contradict competition policy,

- Regulations may have encouraged, or even required, conduct or conditions that would otherwise be in violation of the competition law.
- For example, regulations may have permitted price co-ordination, prevented advertising or other avenues of competition, or required territorial market division.



... replace competition policy,

- Regulation may try to control market power directly, by setting prices and controlling entry and access.
- Changes in technology and other institutions may change the premise, that competition law would be inadequate to the task of preventing monopoly and the exercise of market power.



... reproduce competition policy,

- Regulators may have tried to prevent coordination or abuse in an industry, just as competition policy does.
- For example, regulations may set standards of fair competition or tendering rules to ensure competitive bidding.
- Different regulators may apply different standards, though, and policies which look similar may lead to different outcomes.



... use competition policy methods.

- Instruments to achieve regulatory objectives can be designed to take advantage of market incentives and competitive dynamics.
- Co-ordination may be necessary, to ensure that these instruments work as intended in the context of generally applicable competition law.



Common issues and settings

- Market “failures”
- Public policies
- Public services



## Market “failures”

- “Natural” monopoly
- Information
- Externality
- “Public good”



## Public policies

- Trade
- Privatisation
- Public ownership
- Industrial policy
- Culture



## Public services

- Health care
- Education
- Social welfare



## “Natural monopoly” principles

- Regulate the monopoly
  - Identify it correctly
  - Control price and (maybe) entry
- Stimulate competition elsewhere
- Structural separation
  - But: efficiencies of vertical combination
- Access to “essential facility”
  - And setting the price of access
- Incentive to invest sunk costs in the monopoly



## Public service considerations

- Universal service
  - Scope
  - Subsidy
  - Cost
- Sunk cost recovery
  - Pricing



## Information principles

- Disclosure requirements
- Standards and certification rules



## Public policy principles

- Ownership
  - Distorts market responses
  - Preferential treatment
    - Incentive: to preserve public resources
    - Opportunity: to use power to disadvantage of competitors
  - Implicit unfair advantages
    - Soft budget constraint
    - Expectation of preferential treatment



## “Competition Toolkit” for assessing regulation

- Process:
  - “Competition checklist” initial screening
  - Full assessment if necessary



## Competition Checklist

- Does the law or regulation:
  - Limit the **number or range** of suppliers?
  - Limit their **ability** to compete?
  - Reduce their **incentive** to compete vigorously?



## Limit suppliers?

- Grants exclusive rights
- Requires a license, permit or authorisation
- Limits the ability of some types of suppliers
- Significantly raises cost of entry or exit
- Creates a geographical barrier to supply or investment



## Limit ability to compete?

- Controls or substantially influences prices
- Limits freedom to advertise or market
- Sets standards for product quality that give an advantage to some suppliers, or that are higher than well-informed customers would choose
- Significantly raises costs for some suppliers, especially by treating incumbents differently from new entrants



## Reduce incentive to compete?

- Creates a self-regulatory or co-regulatory regime
- Requires or encourages publication of information on outputs, prices, sales or costs
- Exempts an industry or group from the competition law
- Reduces mobility of customers by increasing the costs of changing suppliers



## Results of Initial Review

- A positive answer to any of the items in the Competition Checklist:
  - signals a potentially significant competition concern
  - warrants a detailed, full competition assessment



## Competition Assessment

- Evaluate whether the regulation would
  - Impose barriers to entry
  - Force firms to exit
  - Increase prices
  - Reduce product variety
  - Increase concentration significantly
  - Reduce innovation
  - Affect related markets