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Analysis of statements made in favour of and against the adoption of competition law in developing and transition economies

Report[1] by

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Abstract

The paper is concerned with documenting and assessing statements made by policy-makers, opinion formers, and other stakeholders in favour and against the adoption of competition laws with particular reference to transition and developing countries which have not yet

enacted these kind of laws. For example, claims that competition enforcement might reduce the inflow of foreign direct investment, or that other policies are successfully used as substitutes for competition law, are assessed. In a first step, the method of generalized analysis structures the list of statements around core issues of common features to make them accessible to further interpretation and assessment. The paper shows that some claims are in fact country or region specific, and specific to the development level of the respective countries. In a second step, the core issues are assessed according to economic and legal criteria. Since the analysis focuses on transition and developing countries, the criteria for economic assessment are predominantly economic growth and development issues, but also include the economic coherency of a set of claims submitted by stakeholders in a given country. The criteria for legal assessment include whether claims are problematic in light of WTO-principles, or are even born out of a political objective which is incompatible with the spirit, if not the letter of WTO-rules.

Keywords: Development and transitions countries, competition law

JEL-classification: K20, K21, L40, L50, O20

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1 Introduction

In the more recent phases of globalisation, the adoption of competition laws has come to the fore. The political agenda in transition and developing countries as well as the development policy-agenda have shifted from state intervention toward a more market-oriented system of economic governance: "In the past, most developing countries were characterised by large state-owned sectors in highly concentrated industries and inefficient firms operating in domestic markets that were insulated by trade barriers. Since the early 1970s many of these countries have adopted new policies of trade liberalisation, de-regulation and privatisation." (Cuts 2003, p. 17). Also, with intensifying (regional) integration and globalisation, more emphasis has gradually been placed on the need for all countries in the world trade arena to enact competition law that would guarantee foreign trade to take place on a level playing field.

In particular since 1980, the number of countries enacting competition law has increased considerably (Palim 1998, Clarke and Evenett 2003). Especially "developing countries recognise the importance of implementing an effective competition policy and law, to achieve the maximum benefit from the process of liberalisation" (Cuts 2003, p. 17). In this respect, the enactment can be described as an evolutionary process, possibly starting with rules against the abuse of dominant position, rules about public procurement, rules governing state aid, sensible and effective rules about the structure and mandate of a competition authority, as well as legal remedies against decisions of the competition authorities. By contrast, rules against collusion of multiple firms (cartels) are often not required as urgently in developing and transition countries. Furthermore, these countries, at least during the earlier stages of competition supervision, may want to shy away from dealing with the more time consuming and resource-intensive issues of merger regulation.

In spite ever wider usage, a number of countries are not convinced that any form of competition law is necessary and/or beneficial for them. They may even perceive market based competition as dangerous to their prospects of economic development and hence have so far not enacted a competition law. Other countries are not even in a position to enact or enforce meaningful competition laws, for example because ongoing civil unrest or war forces them to fight market mechanisms or at least deprives them of the necessary resources for competition supervision. The Ivory Coast is a case on point, where the military coup of 24 December 1999 brought the progress of "competition law and building a competition culture to a halt" (OECD 2002, p. 3).

This report lists claims raised by policy-makers, opinion formers, and other stakeholders in favour and against the enactment of competition law. In particular, the report looks at developing and transition economies. It identifies structures amongst the claims by defining a taxonomy of statements (by use of the method of generalised analysis) and assesses each claim from economic and legal perspectives. As a precondition for economic assessment, the analysis has to assume well functioning markets. However, the legal assessment does not automatically assume that the respective countries have the necessary know-how for the enforcement of sensible competition rules. As experience has shown, for example in the transition countries of Central and Eastern Europe, it is one thing to write up and adopt the necessary legislation. In this respect, Western laws may be used as models and Western experts can help with local adaptation. However, the effective application of the new laws in everyday practice is quite a different challenge, in particular if they require a paradigmatic shift in approach and the development of an entirely different legal culture. The legal assessment, therefore, not only analyses whether claims for and against the adoption of competition laws may be problematic in light of higher legal obligations, in concreto those flowing from WTO-principles, or are even born out of political objectives which are incompatible with the spirit, if not the letter of WTO-rules. The legal assessment also reflects on the broader conditions that have to be met by a country's political and administrative structures and its legal culture before competition supervision will actually work in practice. Where those conditions are not met and cannot be established in the foreseeable future, otherwise unacceptable resistance against the adoption of competition law may have to be seen in a different light.

The assessment makes reference only to the rationale for and against a *national* competition law and does not consider international agreements on competition.

The starting point for this analysis are studies that deal with the issue of competition law in African, South American, South Asian and transition economies (see e.g. Boza 2000, Cuts 2003, and Kovacic 2001). As one main source of information, the report uses so far untapped material from the OECD where representatives of countries around the world have discussed the issue in four "Global Fora on Competition". Additionally, the report assesses the member countries' contributions to the APEC Competition Policy and Law Database, the submissions to the Intergovernmental Group of Experts on Competition Law and Policy at the Competition Law and Policy and Consumer Protection Branch of UNCTAD, and the submissions to the Working Group on the Interaction between Trade and Competition Policy at the WTO, as well as the academic literature available on the issue. The analysis provides new insights into the issue not only by compiling a systematic overview of a very comprehensive list of claims from the widest possible selection of countries, but also by reviewing the economic and legal contents of the claims and by assessing them critically.

The analysis is organized as follows: in the first section, the core principles of competition, competition policy, and competition law are briefly discussed. The second part of the report is concerned with the group of claims in favour of the enactment of competition laws. This is followed by the list of claims raised against enacting a competition law and their legal and economic assessment. The report closes with a brief conclusion for the case of transition and developing countries.

2 Competition principles, competition policy, and competition law

Competition is seen as one of the key features of market economies for the increase of economic welfare. There are two main reasons for this: First, competition has an impact on static efficiency of market outcome. Competition improves the allocation of resources and ensures that production of goods and provision of services are carried out at minimum costs, so that the welfare of a society at a given point in time is maximised. Second, competition improves dynamic efficiency of market outcome. Competition strengthens the entrepreneurial creativity of market participants and encourages producers to innovate and to improve their products, so that technical progress is enhanced over time.

In a more recent strand of literature it is suggested that dynamic efficiency of competition should be valued higher than static efficiency. For example, SINGH claims that in developing countries there is “need to emphasise dynamic rather than static efficiency” (Singh 2002, p. 22). This is not immediately obvious, however, since developing countries usually still struggle more with efficient allocation of resources while a multitude of pre-conditions for significant innovation are still missing. Audretsch et al., Baker, and Posner made the case, that the fast pace of innovation in several industries, as well as the nature of technologies, require a reconsideration of the weight which is given to static and dynamic efficiency (Audretsch, Baumol, and Burke 2001, Baker 1999, Posner 2001). Furthermore, Evenett made the point that “in many jurisdictions with active competition regimes the promotion of innovation or dynamic efficiency gains has become an important goal” (Evenett 2003c, p. 12). We suggest that there is a correlation between development on the one side and the relative importance of static and dynamic efficiency of competition on the other. As countries are progressing on the path of development, they are resolving more and more of the challenges of efficient allocation of resources in the existing production of goods and provision of services. Static efficiencies of competition become relatively less important. At the same time, continued welfare gains come to depend more and more on innovation, which in turn requires dynamic efficiencies of competition.

Competition is not only promoted and protected by a free market economy. Without the right legal framework, a free market economy could see the benefits of competition reduced by anticompetitive behaviour. Therefore many countries practice competition policy to protect competition. Competition policy in general includes measures that are concerned with private anti-competitive conduct and with state measures or instruments that affect the extent of competition in markets. State measures include, for example, trade policy, foreign direct investment policy, licensing policy, public procurement policy, state aid policy, as well as competition advocacy to promote or ensure a competitive environment (ibid., p. 13).

Among the measures that belong to competition policy, competition law is in many countries (one of) the most important instrument(s) to encourage competition in the markets (ibid., p. 14). Competition law could be regarded as an instrument which directly addresses strategic conduct of firms to reduce competition or to exploit market power. Competition law is defined by Audretsch et al. as the law which "lays down the rules for competitive rivalry. It comprises a set of directives that constrain the strategies available to firms" (Audretsch, Baumol, and Burke 2001). Another definition is given by Hoekman and Holmes. They define competition law "as the set of rules and disciplines maintained by governments relating either to agreements between firms that restrict competition or to the abuse of a dominant position (including attempts to create a dominant position through mergers)" (Hoekman and Holmes 1999, p. 877). In addition to that definition, UNCTAD and Evenett describe private sector conduct that is frequently regulated by competition laws. These lists include (and are not necessarily exhaustive): i) inter-firm agreements to restrict competition (cartels), as well as informal agreements between firms, including potentially pro-competitive cooperation in R&D activity, distribution, etc; ii) attempts to exploit market power, and other forms of unfair competition (e.g. predatory pricing); iii) mergers and acquisitions (UNCTAD 2002c, pp. 7-8, Evenett 2003c, p. 14-15).

Competition laws frequently do not only regulate private sector conduct. They may also deal with sub-optimal state intervention in the markets, in particular in the form of (discriminatory) state aid, and/or non-competitive public procurement. Furthermore, competition laws may contain exemptions and/or stipulate other (social) goals. For example, the competition law of South Africa mandates the promotion of employment, small and medium-sized enterprises, and the increase of "the ownership stakes of historically disadvantaged persons" (Evenett 2003c, pp. 12-13). Hence, a competition law could include more than a single objective. However, too many objectives may distort the effectiveness of a competition law.

3 Core issues in favour of the adoption of a competition law

3.1 Claims related to economic theory

Each economic system combines scarce resources to produce some value added, and the system that is able to produce the highest value added per resource utilised is the most developed one. Hence, economic development is a criterion of the efficiency of use of resources.

Because economies are differently endowed with resources and, in a dynamic view of the world, relative scarcity of resources changes over time, there is no one-size-fits-all technology that maximises value added in every country. Some economies are more advanced in finding their efficient combination of resources and are also more advanced in adapting to changes in the relative resource-scarcity (the more developed countries) than others (the less developed countries). Hence, a good mechanism is needed to allocate scarce resources efficiently, i.e. to achieve the highest possible value added given the respective endowment with resources.

Because of the diversity of products and technologies, and because of the dynamic nature of the modern world, this mechanism needs to simultaneously consider information about consumer preferences, about availability of resources, about technologies, and about how these might evolve in the future. The best mechanism we know today is the price mechanism in contestable markets: here, all available information is amalgamated into one category, the system of relative prices. Consumers can plan and execute their preferences to maximise their welfare. This includes the selection of products and services they want to acquire, given the price they find in the market, and the choice of most preferred supplier, according to price, quality, and service. The price mechanism coordinates demand and supply and clears the markets, thus eliminating excess demand or supply.

Producers use the information contained in prices to plan and execute the level of output in production that maximises their profits and to find the best allocation of resources to produce efficiently. In a static view, efficient resource-allocation produces the highest possible productivity, and in a dynamic view, the allocation-function of contestable markets produces the optimal amount of investment into future production and economic growth. Moreover, competition between producers gives rise to pro-competitive effects by which producers generate new technologies (process innovations), and generate new markets (product innovations), to improve their competitive position. Product and process innovations lift the country on higher levels of economic development.

All this obviously assumes perfect markets, i.e. the absence of externalities (spillover effects) or other forms of market failures such as information asymmetries or short-termism. Perfect market conditions, however, are rarely found, if ever, and certainly do not characterize the vast majority of economic activity. The real world may come close enough to perfect market conditions, if a number of precautions are put in place. Hence, from the point of view of economic theory, actively safeguarding contestable markets is an important or probably the most important tool in support of economic development. And in empirical terms, no alternative mechanism (e.g. economic planning, government intervention against the market) was so far able to produce efficiency and welfare to the same extent.

3.1.1 The efficient allocation of resources

The WTO lists a large number of countries that subscribe to the case that a competitive market environment promotes efficiency in the allocation of resources and hence the largest possible production.[5] In fact, the efficient allocation-claim specifically includes static and dynamic dimensions, where static efficiency is defined as to the optimal utilisation of existing resources (to achieve the maximum possible production: allocative efficiency, and at the lowest possible costs: productive efficiency), while dynamic efficiency refers to the optimal introduction of new products, production processes, and organisational structures (the maximum number of innovations that the markets want to accommodate with demand). The same countries are reported to have stated at the same time, however, that "the relationship between competition and innovation is complex, and that, in some instances, limited inter-firm collaboration in the form of joint ventures and strategic alliances can also play a role in achieving greater efficiency" (WTO 1998a, p. 4). The secretary to the second OECD forum on competition reports of an EBRD/ World Bank survey of 3,300 firms in 25 countries, in which "the authors found that the degree of competition perceived by enterprise managers has an important and positive effect on the growth of sales and of labour productivity, and also had a positive effect on firms' decisions to develop and improve their products" (OECD 2002, p. 6). More specific reference to the pro-competitive effect of competition-induced efficiency has been made by Romania ("innovation is supported", OECD 2004, p. 2), Korea ("encouraging innovative business activities", APEC 2005), and Canada ("strengthens the incentives for continual innovation", APEC 2005).

What comes as a surprise is that countries that appear to be favouring a policy of substituting competition by other tools (e.g. Hong Kong, China, and – until recently – Singapore, by use of the sectoral approach) also appear on the WTO list of proponents for the efficiency-claim. Equally astonishing is that Korea (also listed by the WTO as subscribing to the efficiency-claim), at an OECD Global Forum, stated that there was "a trade off between productive efficiency and allocate efficiency" (OECD 2003, p. 3), and that

5 Countries listed by the WTO subscribing to the efficiency-claim include Hong Kong, China, Singapore, New Zealand, ASEAN WTO Members, the United States, Turkey, Pakistan, Canada, the European Community and its Member States, Korea and Japan (*WTO* 1998a, p. 4). Additionally, the efficiency-claim was raised without any qualifications by Zambia (*OECD* 2001, p. 2), Mexico (*OECD* 2004, p. 2), and South Africa (*OECD* 2002, p. 2), although in South Africa, other aims were given greater importance.

if the country – considering itself as small – would not allow mergers, it "would lose productive efficiency if such mergers can achieve economies of scale" (ibid., p. 3). Moreover, Korea stated at the OECD that "strategic allocation of scarce resources and protection of selected industries by the government" (OECD 2002, p. 3) can produce "rapid economic expansion" (ibid., p. 3). Nevertheless, even Korea acknowledges that this may only be true for a limited time and that it may easily become fragile. What this demonstrates, however, are important inconsistencies in the statements of countries' representatives to different international fora.

Another example for the efficiency-claim is Indonesia: here, reference is made to "increasing efficiency" (OECD 2004, p. 4) at the most general level; no further explanations of mechanisms are provided. Kenya refers to "influencing resource allocation in constructive directions while helping to curb the abuses associated with unbridled private enterprise" (OECD 2001, p. 3). Interestingly, the concept of efficiency is not explicitly used here. It is, however, in the case of Romania, where the focus is on the notion that "Competition policy is protecting competition as most efficient resources allocation system of the society and it is not protecting competitors" (OECD 2004, p. 5). The representative of Ukraine to the OECD Global Fora reports of a particular problem related to the allocation of resources. Market mechanisms are distorted by 'institutional monopolies' which are characterised "for instance when specific economic players enjoy exclusive rights to an activity, a different tax regime, or easier access to financial resources and raw materials" ibid., p. 3). These are reported to be often backed or induced by the state and local governments. The representative claims that competition laws can curb this detrimental 'rule of the game' in Ukraine's society and have already done so on occasion (ibid., p. 3). For Cameroon, its representative to the OECD refers to the creative destruction-effect contained in the efficiency claim by stating that a national competitive environment is conducive to "Economic consolidation, through the elimination of inefficient businesses" (ibid., p. 5).

Other references to the efficiency-claim by Cameroon mention the effect of competition on the "development of the private initiative of nationals" (ibid., p. 5), and related to that, the claim that competition law has the objective "to expand the base of entrepreneurship" (OECD 2001, p. 2).

3.1.2 Competition law as a promoter of economic growth and development

On the basis of the expectation that contestable markets provide the best environment for efficient allocation of resources in a static view and help to generate innovation in a dynamic view, competition law can be seen as a promoter of economic growth and development. Another look at this claim shows that competition law will directly provide market-based incentives "that will channel private activity into areas of greatest benefit for all" (ibid., p. 4). This will be particularly relevant for transition and developing economies, as their political imperative is, of course, growth and development. This growth and development-claim can, therefore, help politicians in those countries to improve the acceptance of competition law amongst citizens.

Some countries report that their economies have in fact benefited in terms of growth and development from promoting competition. The Mexican representative to the OECD stated that "competition policy has registered substantial achievements in promoting economic development" (OECD 2004, p. 2). According to his Korean colleague, competition "paved the way for an upward level of economic growth" (OECD 2002, p. 3). The Bulgarian delegate declared that "protection of competition is expressly recognized as a pillar of the sound functioning of the market and the development of economy" (OECD 2003, p. 2). For the Romanian representative, "vigorous competition among companies has important influence on economic development by raising efficiency and expanding social welfare" (ibid., p. 3).

Some countries refer to this claim in a weaker form. Korea uses the concept of "balanced development of the national economy" (APEC 2005). The Ukraine specifies that competition "should facilitate fixing and strengthening such economic growth that is combined with the fulfilment of the basic tasks of social development [...] and socially-oriented market economy in Ukraine" (OECD 2002, p. 3). In later contributions, the Ukrainian representative stated that competition "can improve the development of utility companies" (OECD 2004, pp. 2-3), and "competition is the most crucial factor for strong economic development" (ibid., p. 2). In other countries, in this example Russia, it is explicitly the competition authority that "contributed to the high extent to successful economic development" (OECD 2002, p. 2, OECD 2003, p. 2 and p. 4, OECD 2004, p. 5). The "Competition Council was directly interested in participating to the building of a stable and functioning market economy as key condition of the Romanian economic development" (OECD 2002, p. 2, OECD 2004, p. 2), which, in turn, "would positively contribute to the development of the competitiveness and economic growth of Romania" (OECD 2002, p. 8). Even for a country like Japan, where allegedly industrial policy plays an important role, it was pointed out that "far-reaching structural de-concentration measures served as an important underpinning of the vigorous growth and development that took place in Japan in the post-World War II reconstruction period" (WTO 1998, p. 5).

In the expectation that competition law fosters economic development, the Indonesian Competition Law of 1999 was explicitly enacted to promote "growth and prosperity" (OECD 2004, p. 4). In China, the Antitrust Law stipulates the objective of "guaranteeing wholesome development of socialist market economy" (OECD 2003, p. 3). The Chinese version of the law makes it clear that competition first and foremost serves the development of the socialist market economy, rather than the most efficient allocation of resources and the widest measure of innovation. In China, therefore, competition, allocation-efficiency, and innovation, are not goals in and of themselves but means to a higher end: the promotion of the socialist market economy. In practice, however, it seems that China is nowadays as much concerned about growth and prosperity as other countries and the language of the law may suggest a distinction without much of a difference. Other countries, like Thailand, hope that "fair competition will bring about the development in production and economy as a whole" (OECD 2001, p. 6). In Poland, MP R. Jagieliński, in a parliamentary debate on the draft competition act of 1999, raised the expectation "that the development dynamics, in particular in the underdeveloped sectors, should improve significantly and we should be able to achieve sustainable development of the country" (Cylwik 2005, p. 24). Pakistan specifically added the dimension that "An effective competition policy/law […] can go a long way in poverty alleviation" (OECD 2004, p. 2).

As an example of reverse causality, the representative of Taiwan to the OECD forum on competition noted that "successful economic growth of the economy and changes in global trading environment of the last few decades initiated the call for transformation into a free market to sustain a further economic stability and prosperity" (OECD 2001, p. 2). Korea also makes this claim, albeit in stronger language: "a failure to introduce an effective competition policy at an appropriately early stage in the development process can necessitate costly industrial restructuring at a later stage" (WTO 1998a, p. 5).

3.1.3 Protecting, improving, and maximising consumer welfare

If competition assures efficiency in the allocation of resources and forces firms in a competitive environment to align their output to equate marginal costs and the price they cannot influence, then consumer welfare is maximised: consumers' demand is matched by supply. There is no shortage in supply, and the price is the lowest attainable with the available technology. In the words of the consumer lobby 'Consumer International': "Competition laws should help to make the operation of the market more transparent and efficient. The regulation of anti-competitive practices should facilitate a stronger application of consumer protection" (OECD 2002, p. 4). With a particular view on developing countries, the UNCTAD secretariat states that "competition laws and consumer protection shared the same goals, namely the defence of consumer interests" and that, in addition to competition law, complementary consumer protection rules were necessary: "While effective competition policy could benefit consumers indirectly, consumer protection rules were necessary in order to take care of consumers' immediate concerns. For example, consumers were easy targets for unscrupulous sellers cheating on weights and measures, quality standards, and so forth, as well as for misrepresentations and misleading advertising" (UNCTAD 2002a, p. 4, also in: UNCTAD 2001, p. 3).

Acknowledging that any transition in the system of economic governance, including transition to a competitive system, inflicts adjustment costs, Cooke and Elliott summarise the available empirical evidence as suggesting "that though the short-term social costs of transition to a more competitive economy can be highly significant, they will be insignificant when compared to the long-term costs to the economy of not being competitive" (Cooke and Elliott 1999, as quoted in OECD 2002). What remains open in this assessment is the distribution of short-term costs and long-term benefits amongst the different groups of society. This distribution of costs and benefits will favour those businesses and individuals that are able to adjust. It will punish – a t least in the short term – the owners and employees of inefficient businesses. If such a distribution is politically unwanted or unfeasible, transitory compensation schemes can be a useful tool. Related to this, the Pakistani representative to the OECD Forum on Competition holds that "When a reduction in the real income of a large proportion of the population combines with a perception that large profits are being made by a small number of recipients of state protection, resentment may grow, threatening democratic reform" (OECD 2004, p. 2).

A number of countries report from experience that competition increases consumer welfare (The WTO list the United States, Turkey, Canada, the European Community and its member States, India, and Singapore: WTO 1998a, p. 5). Further citations can be found for Cameroon, listing "Consumer welfare through an improved supply of goods and services" (OECD 2004, p. 5) amongst the benefits of competition law. Romania claims that competition law "expands social welfare" (OECD 2003, p. 3), and Thailand adds that competition is necessary "to eliminate unfair business practices and to protect [the] consumer" (OECD 2002, p. 2). In the Ivory Coast, the combined actions of the Competition Commission and the Department for Competition had a significant impact on consumer welfare, including "The fall in the price of major consumer goods" (OECD 2002, p. 3) and even "The birth of consumer movements" (ibid., p. 3). In Mexico, "competition policy has registered substantial achievements in promoting economic development and enhancing consumer welfare" (OECD 2004, p. 2).

Some countries report that the competition law was enacted and a competition authority was installed specifically with a view of improving consumer welfare. In Zambia, the aims and objectives of the competition law make explicit reference to the "protection of consumer welfare" (OECD 2001, p. 2). In Russia, the law refers to the "protection of the consumer rights" (OECD 2003, pp. 2-3), in Mexico to the "protection of the consumer" (OECD 2002, p. 2), in South Africa to "promoting consumer welfare" (ibid., p. 2), in Indonesia to "increase efficiency and people's welfare" (OECD 2004, p. 4), and in Korea to "maximising consumer welfare" (OECD 2003, p. 3), and to "protecting consumer rights and interests" (APEC 2005). Finally, in China, the law's objective is geared towards "protecting rights and interests of businesses and consumers and public interests" (OECD 2003, p. 3).

3.2 Experiences by particular countries in the economic sphere

3.2.1 Realisation of complementary effects of reform policies

Since the 1970s, and in particular with the demise of planned economies in most formerly socialist countries, state-governance of economies was increasingly replaced by a stronger adherence to markets and competition. Globalisation was as much a driver as a result of programmes of trade liberalisation, deregulation, and privatisation in most countries, both in the developed and the developing world. In this process, countries "recognise the importance of implementing an effective competition policy and law, to achieve the maximum benefit from the process of liberalisation" (Cuts 2003, p. 17). The WTO synthesis paper, for example, lists a number of countries (Mexico, Kenya, Turkey, Peru, Brazil, the European Community and its Member States) that support the claim that "competition law and policy have been implemented or strengthened not in isolation, but rather as one element of a package of interrelated reforms of policies aimed at promoting economic and social development" (WTO 1998a, p. 3).

Explicit reference to this claim can be found for Albania, referring to its own experience that "it is very important that market openness be accompanied with a complete regulatory reform, including an adequate legal framework and strong institutions to implement it" (OECD 2004, p. 3). Regulatory reform is specified earlier as "establishment of regulatory entities and competition authorities" (ibid., p. 3). Mexico is aiming to "reduce the temptation for protectionist intervention [by the government] and increase the potential for market-based discipline" (Wise 1998, p. 5). Taiwan says that "[f]ollowing the development of the economy and the transformation of economic structure, the awareness of competition culture and the enforcement of competition law become vital for realising benefits of market economy" (OECD 2001, p. 5). Jamaica also refers to this claim and provides the example "that possible price fixing activities of private firms would replace price controls" in the absence of supervisory legislation (the Fair Competition Act) (OECD 2003, pp. 2-3). The South African representative to the OECD Global Forum reports that "competition laws have been introduced in developing countries in response to the rapid penetration of markets that has inevitably followed the liberalisation of international trade and investment, and, particularly, through privatisation and deregulation, the liberalisation of domestic trade" (ibid., p. 3).

The countries that introduced a competition law to complement systemic reform include most prominently the former Warsaw-pact countries in Central Eastern Europe (the new EU Member States and those in accession negotiations introduced competition laws in the framework of the *acquis communautaire*), but also developing countries like Algeria in which "[t]he implementation of competition policy was accompanied by a radical change in the characteristics of the Algerian economy" (OECD 2004, pp. 2-3) including price liberalisation, liberalisation of external trade, privatisation, and regulating network sectors. The Ivory Coast decided "to go for a policy of open markets" (OECD 2002, pp. 5-6) in the 1960s, which led to the enactment of a competition law in 1978, and Kenya turned away from import substitution towards export orientation, supplemented and supported by a competition law (OECD 2001, p. 3). Bulgaria adopted a new competition law in 1998 as a reaction to the "changes in the Bulgarian economy (privatisation, deregulation, liberalisation) and experience from the enforcement of the previous competition law" (ibid., p. 2). As a result of the reform policies of the late 1980s in Pakistan (privatisation, deregulation and liberalisation, opening up of the economy for foreign investment) "the need to have strong regulatory framework was felt" (OECD 2004, p. 5).

Privatisation and deregulation

Of the reform measures listed above, privatisation is particularly important. It is claimed that privatisation has to be complemented by national competition laws: "competition policy can reinforce, and may even be essential to realizing, the benefits of privatization and deregulation programmes and initiatives" (WTO 1998a, p. 9, this includes Argentina, Canada, Dominican Republic, European Community and its member States, and the United States). In the case of Peru, it is reported with respect to competition policy as a complement to privatisation that "even after introducing competition the incumbent still has significant monopoly power, regulation of conducts is recommended. – Limits on profits or to rates of return generate distortions such as disincentives of inefficiency, cost-plus mentality and expensive enforcement, vulnerability to the capture of the regulatory commission by the regulated industry, and a tendency to limit competition among incumbents and to restrict new entry. – A better alternative is more reliance on competition policy: protecting existing and potential competitors against dominant incumbents" (APEC 2005). The representative of Ukraine to the OECD Global Fora stated that a competition law is necessary during privatisation, as the law "made the unlawful monopolisation in the course of privatisation [by one entity purchasing blocks of stocks of privatising enterprises] practically impossible" (OECD 2001, p. 6). The representative of Russia to the OECD Global Fora emphasised more generally the formation of a competitive environment "as a[n] essential element of economic reforms" (OECD 2002, p. 2), i.e. the process of privatisation, liberalisation and de-monopolisation of the economy. The representative of Bulgaria to the OECD Global Fora reported that the Committee for the Protection of Competition (CPC) "plays an important role in the process of deregulation and liberalisation" (OECD 2001, p. 7). Similarly, the representative of Zambia to the OECD Global Fora emphasised the need to assist the restructuring process of the economy by a law to regulate privatised enterprises: "It was evident that the removal of subsidies and price controls would put consumers at the mercy of the monopolies that dominated the market. In order to achieve price stability, the government needs measures to moderate inflation by checking the power of monopolies to apply higher prices and reduce output by virtue of their dominant market positions" (Cuts Country Report 2002, p. 34).

More specifically, the representative of South Africa to the OECD Global Fora added that not only could enterprises behave in anti-competitive ways *after* the privatisation process, but even the process of privatisation itself could be anti-competitive: "in truth the institutions and their managers are sufficiently powerful to blunt competition, and there are too many other major non-competition objectives linked to privatisation. Fiscal considerations – the desire to maximise the price of the asset – imparts an anti-competitive bias to privatisation. And the understandable temptation to use privatisation as an instrument of social engineering" (OECD 2003, p. 5).

Natural monopolies pose special problems in a wider process of privatisation of the economy. Although such sectors can be privatised, competition between several independent firms can hardly be introduced due to rapidly diminishing returns. However, even in those cases, several countries state that “[a]fter privatization, network monopolies (e.g. electricity grids, railway operations, or basic telecommunications operators) need to be guided by competition principles to ensure they do not abuse their dominant power with respect to end users” (UNCTAD 2002b, p. 11). Even the representatives of Russia and Ukraine state that competition laws and supervisory authorities can improve the operation of natural monopolies (for Russia: OECD 2002, p. 2, and for Ukraine: OECD 2002, p. 4).

Trade liberalisation

In relation to trade liberalisation “a large number of [WTO] Members have made the point that competition policy and trade liberalisation play complementary roles in promoting efficiency, consumer welfare, growth and development. Trade policy fosters these goals primarily through the reduction of government-imposed barriers to international commerce, while competition policy addresses principally anti-competitive practices of enterprises that impede access to, or the efficient functioning of, markets. Neither instrument is likely to be fully successful in the absence of the other” (WTO 1998a, p. 12).[6] While competition laws on the national level focus on competition in the domestic market between domestic firms, trade liberalization adds the important component of international competition. This is particularly significant for smaller economies and for sectors that are characterized by monopolistic or oligopolistic structures domestically. Even if a sector is not a natural monopoly and could see competition between a multitude of independent firms, this may not easily happen if know-how, capital and other production factors are concentrated in a few hands – usually hands that were connected to political power in one way or another prior to market reforms. Trade liberalization, therefore, is one of the fastest ways of challenging domestic dominance and forcing traditionally powerful firms to become competitive and to pass at least part of the benefits on to consumers. At the same time, trade liberalization can be undermined by anti-competitive behaviour of domestic firms, for example if retailers are pressured by dominant domestic suppliers into boycotting potential suppliers from abroad. Competition law and trade liberalization, therefore, are interdependent.

In a contribution to the WTO “Argentina has set out the results of 18 empirical case studies which, in its view, illustrate the importance of an effective national competition policy, even in the context of external market liberalization. The presumption underlying these studies is that, in general, when a country implements far-reaching trade liberalization, domestic prices will tend toward import parity levels. The competition agency

6 The point that trade liberalisation and competition policy are complementary tools are also made by several contributions at the OECD Global Fora: see e.g. Mexico: *OECD* 2004, p. 2, *OECD* 2004b, pp. 11-12, South Africa: *OECD* 2002, p. 2, Zambia: *OECD* 2001, p. 2.

of Argentina had, nonetheless, identified several situations where this response had not been forthcoming, due to the existence of anti-competitive practices of enterprises. Factors that tended to facilitate or underlie such anti-competitive practices included high market concentration levels, inelastic demand (reflecting a lack of substitutes), the prior existence of a cartel, and control by a dominant enterprise of scarce facilities that were necessary for imports to occur. Based on these findings, the representative of Argentina concluded that effective national competition policies are vital to ensure that the process of adjustment to external liberalization and resulting benefits for efficient economic development are not circumvented by anti-competitive practices" (WTO 1998a, p. 13).

One special claim in favour of a competition law related to foreign trade and state aid is raised by Ukraine. It is argued that "[t]he regulation of state aid will make it possible to ensure equal conditions of competition on external markets to national producers of goods, in particular it will make it possible to prevent their removal from those markets as a result of the application of antidumping [and countervailing duty] procedures by other countries" (OECD 2001, p. 7).

By contrast, it is quite a different question whether newly reforming economies, in particular if they are relatively small economies with limited consumer purchasing power, have to adopt their own anti-dumping regulations in parallel to the enactment of national competition laws and the liberalization of trade. This argument is often made. For example, "[i]n the case of Pakistan, an antidumping law was enacted in the 1990s as the fear of dumping increased with a decline in tariffs and removal of non-tariff barriers" (Cuts 2003, p. 25). Zambia reported that "the increase in import competition has led [...] to extensively use of anti-dumping measures in recent years" (Cuts 2002, p. 25). The *Kyiv declaration*, adopted by the representatives of the region comprising the Commonwealth of Independent States (CIS) and certain Countries of Central and Eastern Europe (CEECs) and addressed to the Fourth Review UNCTAD Conference, goes in a similar direction. It stresses the need for international cooperation and the "development of effective international instruments to protect competition during the further liberalisation of international trade" (OECD 2001, p. 8).

Various studies have shown that resort to anti-dumping legislation is reverse proportionate to the reduction of tariffs and non-tariff barriers (Miranda, Torres, and Ruiz 1998, pp. 5 and seq.). However, this does not necessarily mean that countries that liberalize their import regimes become targets of dumping. It may simply mean that domestic firms are seeking new ways of reducing competitive pressures from abroad, once the foreign competitors no longer have to pay high entrance fees (tariffs) to get to market and no longer have to deal with discriminatory and other non-tariff barriers. If imported goods are cheaper, it is always easy to claim that the foreign competitors are cheating, i.e. dumping. In reality, they may just be more efficient. Therefore, countries should be required not only to examine the prices of imported goods. They should be required to also demonstrate that the respective markets meet certain pre-conditions that would make predatory dumping feasible or at least conceivable (Mickus, 2002). These elaborations, however, will be for another study.

3.2.2 Competition law as a remedy against anti-competitive practices (including international mergers and cartels)

One typical claim in favour of the adoption of competition law is that it is a means against anti-competitive behaviour practiced by domestic as well as foreign enterprises. In the case of Korea, a general remark in this direction has been made at the OECD Global Forum, namely that national competition law is used as a tool against the "abuse of market-dominant position" (OECD 2003, p. 2). More specifically, the country's contribution list the two most pressing problems to be resolved by competition law: it "prevents excessive concentration of economic power and regulates cartels and unfair business practices" (ibid., p. 2).[7] In respect to the historical concentration of industries, the national competition law is used to control price determination by monopolies and oligopolies: the MRFTA prohibits undue pricing by monopolies and parallel price increases by oligopolies (Wise 1999, p. 6). In another contribution to the OECD, the country reports a related problem with the concentration of industries: the Korean Free Trade Commission "designed its own guidelines that is to eliminate anti-competitive regulations such as entrance barriers" (OECD 2001, p. 4). As another example, Zambia pointed out its concern that the removal of subsidies and price controls, might enable domestic monopolies and parastatal companies to enact monopolistic price rises (leading to inflation), and would put consumers at the mercy of the monopolies (both in terms of prices and reduced output). To solve these problems, it is reported that measures are needed "checking the power of monopolies" (Cuts 2002, p. 36) and to "ensure the existence of competition" (OECD 2002, p. 6).

In a vertical view of the claim that competition law is needed to prevent anti-competitive practices, the WTO assesses that "a clear majority of cases (80 per cent plus) of anti-competitive practices in a developing country setting involve the supply of intermediate products purchased by other businesses, rather than goods purchased by final consumers. This is another important reason why competition policy is more likely to assist than to harm firms in developing country markets in enhancing their international competitiveness" (WTO 1998a, p. 14). One example where the problem of vertical restraints proved to be a problem is that of Thailand's chicken industry, where "concerted action between the nation's largest producer and supplier to determine quantities" (OECD 2001, p. 5) was terminated with the help of the country's competition law.

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7 In this respect Romania e.g. "highlighted the area of anti-competitive agreements among firms (i.e., cartels) as a key focus of enforcement activity for competition agencies in developing and transition economies" (*WTO* 1998a, p. 17). Latvia, Pakistan, Russia, and South Africa e.g. pointed out amongst other things the need to restrict or break up (excessive) market concentration (Latvia: *OECD* 2001, p. 2, Pakistan: *Cuts* 2003, pp. 31-32, Russia: *OECD* 2004, p. 2, South Africa: *OECD* 2003, p. 2).

Another issue in this respect is related to the fear that M&A activity could later lead to anti-competitive practices due to increased market power (ibid., p. 2). In the particular case of Jamaica, mergers and acquisitions are not seen as inherently bad (due to scale economies). The national competition law would only intervene in case of use – or rather abuse – of a dominant position (OECD 2003, pp. 3-4). Even in Egypt, the claim is raised that because the country does not have a national competition law, mergers and acquisitions have so far been undertaken without proper control (OECD 2002, pp. 2, 7). Romania additionally made the claim, that "merger control ensures a diversity of mass-market consumer goods and low prices for the final consumer" (ibid., p. 5).

Natural monopolies might also practise anti-competitive behaviour. Being natural, they cannot be broken up into smaller units and need a regulator to control them (for example in the case of Estonia, a sectoral regulator exists in energy, railway transport, and communications: ibid., pp. 2-3). However, as the representative of Ukraine to the OECD Global Fora rightly stated, competition law can still serve as a remedy against anti-competitive practices, because it "can improve the regulation of activities of natural monopolies" (ibid., p. 4). In Russia, economic competition is governed by the Ministry for the Antimonopoly Policy and Support of Entrepreneurship (MAP) which "plays nowadays a significant role in the processes of deregulation and restructuring of natural monopolies" (ibid., p. 2). Whilst the national competition law was elaborated with the assistance of the OECD, the competition authority is a ministry and hence not independent from state interests – a problem of particular relevance for the efficient regulation of natural monopolies.

Interestingly, the Peruvian commission is in charge since April 2001 "to evaluate the legality and the subsidiary nature of the companies kept by the Peruvian State. Up until now [April 2001], the Commission expressed its opinion about State-owned companies in different sectors, such as: commercial airlines, post, naval construction and reparation, editorial, real estate and coca leaf trading (ibid., p. 3).

Anti-competitive practices are not only a problem within the domestic economy if it lacks a competition law, but also on an international level. Again, national competition law can help safeguard the contestability of markets (this has been stressed for example by Argentina and Taiwan: WTO 1998a, p. 13, and OECD 2004, p. 2, respectively).

Various countries have raised concerns that foreign international (transnational) enterprises and cartels can hurt domestic enterprises and national consumers by way of anti-competitive practices. Vietnam states that "like […] other transitional economies, [it] may face the situation that foreign enterprises can abuse the advantage of market liberalization to impose their restraints such as price fixing agreement, predatory pricing and other abusive behaviours to distort fair and equitable competition environment" (OECD 2002, p. 2-3, this has also been stated by Egypt: OECD 2002, pp. 2, 8). Thailand stated that "rigorous competition law and policy is therefore indispensable to control and maintain competition" (ibid., p. 2). More specifically, Pakistan concluded that "competition laws can be used as effective instruments to alleviate the problem of international anticompetitive practices in at least two ways: (i) deter; (ii) prosecute (alone or in cooperation with other countries)" (OECD 2004, p. 2). Russia explicitly includes the control of multinational mergers into the Antimonopoly Law: "the same rules are applied to all companies both national and foreign based on the principle of national treatment" (ibid., p. 3). Although he did not question the need for national competition law, G. K. Lipimile from the Zambian Competition Commission raised doubts whether a developing country was in fact in the position to challenge international cartels. Hence, he welcomed that "[t]he establishment of institutions like the Global Competition Forum and the International Competition Network offers an opportunity for developing countries to develop a mechanism where their concerns shall be addressed in international enforcement of antitrust laws" (OECD 2002, p. 4). Similarly, the Latvian competition surveillance authority sees "prospects for multilateral competition surveillance instruments" (ibid., p. 3).

3.2.3 Enhancing the attractiveness to foreign direct investors

With regard to foreign direct investment, opinions vary as to the impact of competition law. Some countries share the view that competition law could negatively affect the inflow of foreign direct investment (see chapter 4.1.5), whilst others argue that competition law could enhance the attractiveness of countries to foreign direct investment. In a meeting at the WTO "representatives of a number of countries, including the European Community and its [M]ember States, Japan, Turkey, Norway, Brazil, Korea, Morocco, India, Tunisia, Argentina and the United States, said that competition and competition policy could play an important or, in the view of some of these countries, even a central role in facilitating development. Among other benefits, competition policy could […] enhance the attractiveness of an economy to foreign investment, by providing a transparent and market-oriented framework for the resolution of disputes involving multinational enterprises, which would reduce uncertainty and transaction costs" (WTO 1998b, pp. 5-6). Similarly, Egypt stated that competition policy could be seen "as a prerequisite for the entry into the developing host countries by some multinationals" (OECD 2002, p. 8). Furthermore, Russia claimed that "[p]enalties are much lower in Russia than in developed countries. The lower penalties in Russia are an obstacle to effective application of antimonopoly regulations, which in turn discourages the inflow of foreign investment and hampers the development of competition in Russia's goods markets" (OECD 2004, p. 5).

3.2.4 Promoting international competitiveness of domestic enterprises

A claim raised in favour of the adoption of competition law is that effective domestic competition is the best way to build internationally competitive enterprises. This claim was raised by Pakistan ("Businesses cannot be competitive on international markets if they are not exposed to competition in national markets", ibid., p. 3) and by several members of the WTO ("robust competition in the home market contributes positively to the international competitiveness of firms", Canada, Hong Kong, United States: WTO 1998a, p. 14). For Poland, the case was made that competition law can help to improve the efficiency of domestic enterprises, "increasing the competitiveness of the Polish industry" (this has been referred to for example by the Polish MP E. Freyberg in a parliamentary debate in 1999 on the reform of the national competition law: Cylwik 2005, p. 23). More specifically, a competition law that regulates the granting of state aid, e.g. for technological development, regional policy, and environmental protection, can teach domestic firms to use state aid efficiently whilst pursuing international competitiveness (see e.g. MP I. Niewiarowski , and MP Z. Zarębski: ibid., pp. 22-23. Moreover, a competition law can help to reallocate previously inefficiently disbursed funds to promising enterprises: MP R. Jagieliński: ibid., p. 24.). The point is, that competition within a country is necessary for the development of a competitive industry. Only competition, forces firms to use their resources most efficiently and to adopt and to develop the most efficient production technologies. Furthermore, experience with doing business in a competitive environment is generated, which helps these firms to compete successfully internationally, when the market opens to foreign competitors (see also chapter 4.1.2).

3.2.5 Competition law as an instrument of competition advocacy

As a result of central planning, transition economies have accumulated little experience with competition. What is lacking is a competition culture. A culture of competition, however, is one of the central elements for the creation of a competitive environment. Competition advocacy is therefore seen by many countries as an important instrument to promote competition (WTO 1998a, p. 11, Romania stated in this respect that "the building of a competition culture is the most important step to be followed by politicians from all countries that committed to promote a more market based economy": OECD 2002, p. 2). As pointed out by Anderson and Jenny, activities in competition advocacy "may include public education activities, studies and research undertaken to document the need for market-opening measures, formal appearances before legislative committees or other government bodies in public proceedings, or 'behind-the-scenes' lobbying within government. These, it has been suggested in the Working Group, may be among the most useful and high payoff activities undertaken by agency staff" (Anderson and Jenny 2002, p. 7, as found in Evenett 2003c, p. 14). In this respect, many countries stated at the OECD Global Fora that their competition agency promotes a competition culture through competition advocacy activities (see for example Peru: OECD 2002, p. 2, Venezuela: ibid., p. 4, Romania: ibid., p. 6, and Russia: ibid., p. 2.). An interesting example is Algeria, where the assessment of "competition during the period 1995 to 2002" (OECD 2004, p. 3) shows that there is still a long way to go "until a genuine culture of competition emerges, not only among firms but as a 'way of life', that includes consumer behaviour, too" (ibid., p. 3). To correct this shortcoming of existing competition law in Algeria, a new Act was passed, which specifically addresses the need to build up a competition culture (ibid., p. 4).

However, not only competition advocacy (through competition authorities) is necessary to improve the competition culture within a country, but also the active enforcement of the competition laws. In the WTO, the point has been made by several countries that "the existence of a competition law coupled with a vigorous enforcement policy greatly facilitates effective competition advocacy work (Argentina, Brazil, Canada: WTO 1998a, p. 11). This is confirmed by the example of South Africa, where "[m]erger hearings are held in public – with due regard to the need to protect confidential information – and interested parties are, in addition to the Commission and the merging parties, entitled to make submissions to the Tribunal. […] Representatives of the media regularly attend and report on merger hearings and the outcomes of these decisions – all of which are fully reasoned and publicly available – are widely publicised and debated" (OECD 2004, p. 3).

To sum up, the experiences made by several countries show that a competition law, its effective enforcement, as well as a sensible structured and functional competition authority can help to build up a competition culture. Therefore, a current lack of competition culture should not be used as a justification for the absence of competition laws, but rather as a reason to enact these laws as soon as possible.

3.3 Experiences by particular countries in the political sphere

3.3.1 Remedy against corruption

Corruption and ties between politicians and the private sector is a serious problem, in particular in many developing and transition countries (CPI 2004). It directly affects the competitive environment of the economy. Government bodies in developing and transition countries have manifold possibilities to affect competition, for example by discriminatory licensing, selective subsidies, preferential procurement, etc. The incentives for favouring some enterprises over others, regardless of economic efficiencies and rules of fair play, might be strong due to the low pay of many officials (Kovacic 2001, p. 296). As pointed out by KOVACIC, competition law might help to "undermine corrupt agreements between government officials and business managers" (ibid., p. 296). Some countries explicitly mentioned that they enacted competition law as means against corruption or that competition law can act as a tool against unhealthy favouritism. In Indonesia, the competition law was enacted, inter alia, "to address public concerns regarding monopolistic practices and closely related concerns about corruption, collusion, and nepotism" (OECD 2001, p. 2). In China, when discussing the scope of a proposed antimonopoly law, the point was raised that "emphasis shall be laid on standardizing administrative monopoly" (ibid., p. 6) to eliminate corruption and to create an environment of fair competition. With particular reference to state aid, a member of the Polish Parliament argued that competition law was beneficial for the efficiency of the Polish economy: "In Poland, the nature of state aid does not enforce favourable changes for the economy. It is the particularly unprofitable sectors that extort state aid, increasing the ineffectiveness of the economy. State aid is not transparent, has a discretionary, unpredictable character, thus being negatively perceived by the investors" (MP E. Freyberg: Cylwik 2005, p. 23).

3.3.2 Social objectives (racial inclusion, etc.)

The first democratic government in South Africa "inherited an economic structure characterised by high levels of market concentration and ownership centralisation" (OECD 2004, p. 2). "Thus, South Africa's competition law incorporates specific objectives of social and other public policies into its own objectives." [...] "These objectives reflect, to an extent, the differing pressures on policy-makers, and their prioritisation depends on the development of precedents from cases" (Cuts 2003, pp. 31-32). And "[t]is particular background to the competition law also accounts for a statute that incorporates a multiplicity of objectives, a mix of 'traditional' competition objectives and a range of social objectives, such as employment creation and retention, black economic empowerment and the promotion of SMEs. It's generally thought that this is a feature of developing countries and I'm happy to acknowledge that specific features of our country account for the particularly strong emphasis on 'non-competition' objectives in our law" (OECD 2002, p. 3).

3.3.3 The role of international organizations and regional agreements

International organizations, like the IMF and UNCTAD, and also regional institutions, like the EU, play an important role in the implementation process of competition laws in developing and transition countries. On the one hand, they support countries who want to enact competition laws. On the other hand, they try to convince or force countries to implement competition law. With respect to the latter, a representative of South Africa stated that, as a matter of fact, many developing countries enacted competition laws to react to rapid changes in the economy (e.g. deregulation, privatisation, and foreign trade liberalisation), but also "there are some countries whose competition laws have been introduced at the insistence of the IMF" (OECD 2003, p. 2). A recent example for pressure from the IMF combined with a new domestic understanding of the need for competition law is the case of Indonesia. "While Law Number 5's passage in 1999 came about in part to satisfy conditions of a Letter of Intent entered into between the Indonesian government and the International Monetary Fund in July 1998, the law's passage also drew much support from politicians, the government, the public, and the press as a means to address growing concerns about monopolistic practices and unfair business practices" (OECD 2001, p. 3). Another example is reported by the representative of Russia. In this case a trade agreement between the EU and Russia in steel goods included obligations on competition (OECD 2002, p. 4). For the Ivory Coast, it was openly stated that the most important argument for the adoption of a competition law was "pressure from donors" (ibid., p. 2). The question whether outside pressure, in particular if not combined with strong domestic forces, can achieve effective supervision of competition, will be analyzed in some detail below. Unfortunately, experience shows that it is easier to adopt a new competition law than to apply it in practice. If having a law on the books is what it takes for a country to obtain or maintain access to IMF money, compliance *de iure* can certainly be bought. *De facto*, things may not change much or not at all. And since there are many possible reasons for ineffective or inexistent enforcement, the IMF and other international development agencies can rarely blame a country for lack of good intentions. In the end, the laws are adopted but not enforced, the IMF has achieved nothing, and the developing country has learned another lesson in how to avoid the birth pains of actual development (in this respect, it is worth noting that due to the political instability of the country, enforcement activities in the Ivory Coast came soon to a halt: OECD 2002, p. 2).

The requirements imposed by the EU on candidate countries prior to admission are a particularly good example of outside pressure for the adoption of competition laws. These requirements include the implementation *de iure* and the application *de facto* of national competition laws in line with those of the EU, which form part of the *acquis communautaire*.[8] Although it has been argued that the implementation of national laws along these lines made perfect (economic) sense for the candidate countries regardless of their accession to the EU (see e.g. Carlin 2001, Dutz and Vagliasindi 1999, Emmert 2004, Fox 1997), it is not clear whether all of them would have adopted these particular rules in this kind of a framework. Be that as it may, whether out of their own conviction or because of the pressure applied by the EU, all candidate countries duly enacted or amended competition laws to fulfil this precondition for membership in the EU (see e.g. Hölscher and Stephan 2004, Bulgaria and Romania, which could join the EU as early as 2007, share the view that competition law is an important element in the preparation for EU membership. For Romania: OECD 2003, p. 2, Bulgaria: OECD 2001, p. 2).

Fortunately, international organizations and regional agreements not only compel certain countries to adopt competition laws. They frequently render valuable support for the enactment and the enforcement of a competition law, as well as the building of a competition culture in developing and transition countries. For example, Peru highlighted the assistance offered by the OECD in “personnel training of the technical department” (OECD 2002, p. 3). Russia emphasized the technical assistance from UNCTAD to Russia and other CIS (Commonwealth of Independent States) countries to build a competition culture (ibid., p. 5), and the assistance provided by the OECD for the elaboration and modernisation of competition law (ibid., p. 2). Algeria pointed out that its competition law “is very largely inspired by European legislation and jurisprudence” (OECD 2004, p. 4). Tanzania mentioned the support from international organizations as well as foreign national institutions: “We have so far got support in various forms from the UK/DFID, sida/Sweden and WB/FIAS/IFC” (ibid., p. 5).

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8 The requirement is that the candidate countries have to be “willing and able” to apply the *acquis communautaire*, including the EU competition rules.

4 Core issues discussed against the adoption of competition law

The discussion of the virtues and dangers of a competitive framework based on market governance, also includes a number of claims against the enactment of competition law. Either the validity of the concept of welfare-maximisation or the pro-competitive effect of competition supervision are questioned and rejected, or doubts are raised against particular parts of a competition law. In other cases, alternatives to competition policy are discussed that supposedly suit the particular conditions in transition and developing countries better. As one example, the South African Competition Tribunal stated at an OECD Global Forum on competition:

"In the last decade the dawning awareness that globalisation and liberalisation have not realised their earlier promises has also swung the pendulum back towards industrial policy. Though there is still no respectable voice for turning the clock back to the development strategies of the 'fifties and 'sixties', the respect for industrial policy remains strong. [...] In summary then, developing countries will insist on seeking a balance between competition law and policy, on the one hand, and industrial policy, on the other. They will insist, in other words, on attempting to meet both sets of objectives" (OECD 2003, p. 3).

4.1 Development strategies

4.1.1 The development model of the East Asian Tigers

The success of the Asian tigers is frequently used in support of alternative development models. The case is made that "critically it was the state, not competition, that provided the key disciplines and, hence, little is heard about competition policy or law in the endless accounts of the triumph of the Asian tigers. [...] It is still widely held that a select band of countries had developed successfully and that industrial policy could claim some significant role in this all too rare achievement. [...]" (see e.g. The South African Competition tribunal in, ibid., p. 3). Malaysia, for example, on the basis of past experience, believes that industrial policy (in the case of Korea, these include: primary industry, including agriculture, mining, fishery, and forestry (with the exception of the briquet manufacturing industry, APEC 2005) is an important and integral part of a successful development strategy. Therefore, coherence between industrial policy and competition policy should be pursued (OECD 2002, p. 3). This also concerns "coordination of investment decision which in turn requires close co-operation between government and business" (ibid., p. 3). Korea adopted a Government-driven growth strategy but also established anti-competition regulations (Nam Kee Lee in OECD 2001, p. 5); the government stated that "conflicts and tensions with industrial policy inevitably arise in the process of introducing and implementing competition policy" (Joseph Seon Hur in OECD 2002, p. 3). Cameroon raised the point that "[d]iscussions of the interaction between competition policy and industrial policy often centre on primacy between the two policies. Examples from developed countries (e.g., EU, USA, Canada) show that although competition policy has existed there for a very long time, its implementation has been very recent; as a result, the initial emphasis was on an industrial policy that promoted stable growth and fostered rapid development. This is further illustrated by the economic history of Japan, whose faster growth has been attributed to the fact that for a long time industrial policy took precedence over competition policy" (OECD 2004, p. 4). Representatives of Brazil suggested that "countries should first industrialise their economies through government targeting of industries, and implement competition policy later" (WTO 1998a, p. 16).

To assess whether the interventionist policy measures of South-East Asian states are promoting economic development or not, it is useful to look at the relationship between industrial policy and competition in the national development process of a number of these South-East Asian states. Japan, the Republic of Korea, as well as Taiwan have implemented a lot of policy measures to foster economic development, such as control of market entry, mergers, cartels, firm cooperations, market-sharing, trade protection, subsidies, export promotion, and investment managing (UNCTAD 1998, p. 14). In general, these measures had a higher priority than undistorted competition (Singh and Dhumale 2001). However, while the Korean government in general followed the Japanese economic development strategy (ibid., p. 135), state intervention activity in Taiwan was less strongly pronounced and free-market elements played a larger role (Evenett 2003c, p. 37). The role of state intervention in Japan's development process is well examined, for example in the comprehensive study by Porter et al. (Porter; Sakakibara and Takeuchi 2000). Evenett, who reviewed the existing literature concludes, with particular reference to the study by Porter et al., that in the successful Japanese industries direct state intervention policies played a marginal role. Direct state intervention to the detriment of competition was more likely to explain the failure of industries than their success. It was more the indirect state intervention policies, like stimulating demand for new products, standard setting and education policy, which could explain the success of industries (Evenett 2003c, pp. 32-35). In the case of Korea, the government especially promoted the creation of large cooperations (chaebol) which supposedly would be able to compete on international markets. In this strategy, competition between different chaebol plays an important role. They compete for market share, which determines the investment allocation by government, as well as for government support, which is provided according to export performance. They also compete in product and technology development (Singh, Dhumale, Arestis, Baddeley and McCombie 2001, p. 135). Whilst successful in creating large cooperations, Evenett highlighted that even Korea today sees the disadvantages of such a policy, as it has created large economic and political power in the hands of a few cooperations. This tends now to be used to raise entry barriers, to raise prices, and to reduce competition. He concluded that the Korean experiences suggest that states wanting to build up internationally competitive firms or national champions need a competition law to attenuate the harmful effects of such a policy (Evenett 2003c, pp. 35-37).

As pointed out above, the policy by Taiwan was less interventionist than in Japan and Korea. Moreover, as in Japan, it was not the restriction of competition that stimulated economic development. Rather, the benefits came from governmental measures which supported the industry's own efforts (ibid., pp. 37-38). In this sense, a report by UNCTAD stated, that "[a] key role in industrial success was played by strong competition among Japanese firms and among firms from Taiwan Province of China on domestic and international markets; the most successful Japanese industries have been those where domestic rivalry was strong […]" (UNCTAD 1998, p. 14).

In summary, first there is no single model of development policy in South-East Asian states which could explain the success of these states. Second, experience suggest that in the above mentioned cases competition between firms played an essential role in the development process. Furthermore, even where states wanted to improve international competitiveness of domestic firms, competition within the country proved necessary to attenuate harmful effects from such a policy (see also chapter 4.1.2).

4.1.2 Import substitution policy and infant industry strategy

In the process of industrialisation, transition and developing countries may strive to change the structure and composition of imports in an attempt to develop specialised industries at home. In the economic development literature, this approach is known as import substitution policy. An infant industry strategy could be regarded as one rationale for an import substitution policy. While support for import substitution policies has been fading in the last decades, Malaysia still makes a case for its heavy-industry import substitution policy, which is credited, for example, with today's successful national car project (OECD 2003, p. 2). To extend this success into other sectors, Malaysia argues that several other domestic industries should be exempted from competition laws until they are internationally competitive (OECD 2002, p. 3). Similarly, in a statement to an UNCTAD session on competition, representatives of various least developed countries called for more Western appreciation of their perceived need to support domestic industries "[until] these acquire the capacity to compete with powerful MNCs" (e.g. for Bangladesh: Chowdhury 2002, p. 3). Kenya adopted an import substitution policy in combination with export licensing (OECD 2001, p. 2), and in Peru, import substitution was done before 1990 and supplemented with export subsidies (César Guzman-Barron Sobrevilla, Président Comision de Libre Competencia Peru: OECD 2002, p. 2). Countries seeking to emulate some of the more successful experiences with this particular development strategy would, however, find it difficult to harmonise competition laws with policies where the state has a regulating and managing role as owner and where the state also implements a protection policy for the benefit of the local industry.

The economic rationale behind an import substitution policy is to protect the domestic industry from foreign competition, and in this way to foster industrialisation as a motor of economic growth. In this context, it is argued that firms in less developed countries are not able to produce as efficiently as established firms in developed countries. They do not use the same production technology and their workers and management do not possess the necessary knowledge and experience. Protection from foreign competition would give these firms the possibility to gain production and management experience and to increase their efficiency over time to eventually find themselves in the position to compete successfully with firms in developed countries. Experience with import substitution policy in the past shows, however, that this development strategy failed in almost all of its applications. The main reason for this could be seen in the fact that import substitution in the past generated an environment which is not beneficial to the creation of knowledge (compare Bruton 1998, p. 903).

Nevertheless, recent studies indicate that import substitution policies cannot be refuted in every single case. Specifically, protectionist measures which foster endogenous learning may be reasonable for a developing country (ibid., pp. 930-931). However, whether certain types of import substitution may sometimes yield beneficial results or not, these limited exceptions to the more general rule do not negate the need for competition within a country. Competition is necessary in the process of building up a competitive industry, as it forces firms to use their resources most efficiently and to adopt and to develop the most efficient production technology. Furthermore, experience with doing business in a competitive environment is acquired, which may help the firms to compete successfully internationally, when the market opens for imports and exports. In this way competition within a country can be useful to compensate for import substitution policy's main weakness in generating knowledge. In summary, if countries choose to build up industries through import substitution, the best way to do so is to ensure competition within the country and only ease competition from abroad by use of trade policy measures strictly limited in time (and in agreement with WTO rules).

4.1.3 Export oriented policy and small country-claims, economies of scale

Reasons, why foreign trade can be beneficial for a country are manifold and include welfare effects for consumers gaining access to a wider variety of products, efficiency improvements on the production-side due to intensifying competition (specialisation on comparative advantages), due to technology transfer, economies of scale by access to larger markets, etc. In addition, current account surpluses are the only vehicle for a country to repay external debts. Moreover, surpluses give rise to currency revaluation expectations on the foreign exchange markets, which is an important instrument for countries attempting to stabilise their monetary and financial systems. While these benefits are particularly interesting for heavily indebted and economically unstable developing countries, the realisation of positive benefits hinge on the country achieving current account surpluses or at least a balance of trade in goods and services. Hence, many developing countries attempt to assist their exporting companies with a development strategy promoting export orientation. This strategy includes a variety of interventions, some providing assistance to targeted exporters, some to specific exporting industries, and some to any company attempting to export.[9] Sometimes import tariffs are levied in the misguided hope that the country can generate export surpluses this way. With not all companies actually exporting, most policies in support of exporters (including those of horizontal design) contradict the notion of a level playing field. That is why many developing countries fear that the introduction of national competition laws might force them to discontinue export promotion strategies. However, while export promotion may be problematic from the point of view of efficiency in resource allocation and while it may be problematic in light of WTO requirements, there is no immediate reason why a country could not have competition laws with explicit or implicit permissions for export promotion.

Of the many states that have (had) such policies, Taiwan reports that the national Fair Trade Law exempts concerted actions from the law if they "boost international trade" (OECD 2001, p. 2). Indonesia excluded international agreements and export agreements from competition law activities (ibid., p. 3). That country has long used some measures for export orientation and trade administration to get more positive market effects (OECD 2004, pp. 2-3).

Many theoretical analyses, in particular the new trade theory and the new economic geography (most prominently Krugman, Venables, Helpman, Grossman, Feenstra, etc.), have reviewed the hypothesis that trade liberalisation alone is sufficient to increase welfare of all participating countries. Although the premise of various studies has been that developing countries may not benefit significantly or at all from trade liberalisation, they have in general not been able to challenge the free trade paradigm other than in very special circumstances. Still, the empirical fact remains that foreign trade is often very unequal and remains unbalanced even over a longer period of time (with deficits burdening a country over an extended period that cannot be treated as irrelevant). In terms of national competition law and its objective to guard a level playing field within the economy, the promotion of exports can be best achieved first by way of increasing the intensity of competition on the domestic market in order to make firms fit to compete internationally. Second, a mercantilist policy (even if undesirable from a supra-national perspective) can be neutral in terms of distortions on the national arena and therefore need not contradict a national competition law.

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9 The latter occurs even in the case of developed economies, albeit motivated by use of the market imperfections-case. E.g. German exporters can apply for a so-called Hermes credit scheme, where the exporter can claim his expected export revenue from the German government. This is a helpful instrument where the foreign client might be less reliable, or the revenue might need considerable time to be credited to the exporter.

One particularly persistent claim regarding export-promotion strategies pertains to the so-called small-country effect. Companies in transition and developing countries suffer from the particular problem that their home markets often cannot generate a sufficiently large demand to allow the companies to reach their optimal size in terms of scale economies.[10] It is therefore claimed that some concentration and cooperation in the smaller domestic markets should be allowed, since this would be welfare and efficiency improving when benchmarked against the efficiency of larger companies from larger countries or integration areas (the 'relevant market'). Additionally, small and medium-sized companies (as measured against the benchmark-sizes of foreign firms) are claimed to be in need of some form or other of affirmative action. Furthermore, it has been argued that (the application of) national competition law needs to be relaxed with respect to selected companies, in order to develop so-called 'national champions' of a sufficient size to be competitive on world markets (see chapter 4.1.4). Since these kind of policies are at variance with the letter and spirit of typical competition laws, the enactment of such competition laws is perceived as a danger to international competitiveness, domestic industrial growth (reviewed in Evenett 2003d, p. 6, and Cooke and Elliott 1999), and welfare more broadly. In short, benefits from scale economies are claimed to exceed benefits derived from a higher intensity of competition (Langhammer 2000).

In this respect, countries like Indonesia, Taiwan, and Romania report that they exclude to some extent small-scale enterprises from the application of competition law (Indonesia: OECD 2001, p. 3, for Chinese Taipei: ibid., p. 2, and Yang-Ching of the Fiar Trade Commission: APEC 2005, for Romania: OECD 2003, p. 4). In fact, most developed countries, whether small or large, grant small and medium-sized enterprises (SMEs) some preferential treatment, and even the USA excludes some scale-intensive sectors from its competition law (in the USA, these are e.g. cooperatives in agriculture and fishing, shipping, rail, etc.: APEC 2005). The Philippine government remains uncertain about how to treat SMEs under a competition law regime vis-à-vis large enterprises (ibid.).

With respect to concentration control, a number of developing countries hold that in small countries with small-scale companies, there is a particular need to allow firms to achieve economies of scale by mergers and acquisitions. Being a small country is claimed to have particular implications for merger policy (For Peru: WTO 1998a, p. 14, or Estonia: OECD, Third Global Forum on Competition, for Estonia: OECD 2003, p. 2, for Jamaica: OECD 2003, p. 3, for Pakistan: OECD 2004, p. 4, for Latvia: OECD 2002, p. 2). Malaysia states that an example of this claim is "the recent government-induced mergers in the banking system to enable these institutions to compete with international banks" (OECD 2003, pp. 3-4). In Zambia, it was the private sector that raised this claim

10 Related to this is the Linder-Hypothesis, according to which companies need a close proximity to the market to develop products that can be competitive on international markets. This hypothesis, however, mainly applies to the development of differentiated goods and hence trade between more developed countries (see *Changkyu Choi* 2002, pp. 601-605).

(OECD 2002, p. 7). The South African Competition Tribunal postulates: "… the operation of scale economies in small markets dictates a permissive approach to mergers in developing countries" (OECD 2002, p. 3, for Jamaica; OECD 2003, pp. 2-3). Peru argues that "concentrations taking place in the context of economic liberalization are less likely to be linked to anti-competitive practices, but rather to the adaptation of the domestic economy to the changes resulting from the new economic environment" (WTO 1998c, p. 14, found as comments by the representative of Peru, reported in M/4, para 64, and the written contribution on Peru on this matter (document W/59). Similarly, Malaysia feels that an "optimal combination of competition and co-operation between firms" is necessary to achieve fast long term growth (OECD 2002, p. 3).

A further reasoning focuses on investment. Pakistan claims that developing countries – due to their small size – produce less investment than required to achieve economies of scale (OECD 2004, p. 4, for Korea: Wise 1999, p. 4). The framers of the first competition law of Canada in 1879 "believed that Canada as a whole would benefit from large aggregations of capital (such was the means to a higher standard of living for the nation)..." (APEC 2005). By the 1960s, the claim read: "To reap the benefits of economies of scale and scope, companies require massive investments and a large market to underwrite such investments. These structural characteristics would require a balance between competition and efficiency, with greater concentration being a necessary means of achieving greater efficiency" (ibid.). Along a similar line, Kenya argues that the "large-scale formal sector firms" have better access to credit in terms of price. Here, in the absence of government intervention in favour of smaller firms, there is no level playing field in the domestic economy. In South Africa, the historically rooted phenomenon of intense cross-ownership (cross-holding) between large financial corporations and large conglomerates today constitutes a systemic disadvantage for SMEs (Cuts 2003, p. 27).

With respect to the general nurturing of small-scale companies, this may seem to be well-founded e.g. where SMEs suffer from a less lobbying-influence on politics or industry-wide wage negotiations, compared to larger companies or state-owned companies. These disadvantages, however, emerge due to shortcomings in the competitive environment and are hence best removed by a more comprehensive application or design of competition law, rather than by affirmative action. With regard to the claim that small-scale firms suffer from a competitive disadvantage over larger firms in terms of access to finance, in particular in the absence of developed venture capital markets for investment, for example in R&D, empirical evidence typically shows that small companies do spend less resources in formal R&D and still are more innovative. Therefore, competitive disadvantages, where they exist, are not tied to the fact that the home country is small. In general, an analysis of OECD material and a review of the literature on SMEs reveals that their role in innovation, employment growth and the adoption of new forms of work organisation is often over-emphasised (Parker 1999, pp. 63-89).

The contention related to the size-disadvantage of domestic firms in small countries with small markets rests on the assumption that the small country's firms have access only to the domestic market. The relevant market, however, includes the whole integration area and spans exactly the same size as the markets of the competitors from larger home countries. This not only pertains to the market for goods and services but also to financial and capital markets (with a view to the alleged disadvantage of small countries in terms of investment). In terms of mergers and acquisitions, a well designed national competition law considers the market share of any given firm in the relevant, not the national market. In a more dynamic perspective, even the contention of a first-mover advantage of firms that have been able to 'mature' on the domestic market before going abroad has to be relativised because products constantly change with innovations and changing product specifications generate new markets and opportunities. Therefore, small firms from small countries can grow bigger when operating in an integrated market and compete better with firms from larger countries. By contrast, if small firms from small countries are not competitive, this is rooted in inefficiencies or the choice of technology, because the shape of economies of scale is not firm- or country-specific but rather is industry- or product-specific. In terms of economic theory of the firm, the existence of increasing economies of scale in a competitive setting is difficult to uphold. The "Choice of optimal proportions of inputs (with free disposal and no indivisibilities) will always assure at least constant returns [to scale]" (Eatwell). Where indivisibilities exist, they are typically incremental, and several solutions for optimal firm-sizes are available.

4.1.4 National champions

National champions are individual companies picked by industrial policy to be supported or nurtured to successfully compete on world markets. They are sometimes viewed as focal points of economic development or the core of a development strategy. National champions exist in many countries, in particular in developing countries[11], but also in countries from the developed world (a classic example are the national airlines; a regional or supra-national version would be Airbus Industries). It is claimed that it is necessary (or at least preferential to swift economic development) to build up national champions by way of selective industrial policy, as those champions are the only domestic companies actually able to compete successfully on international markets. In an application of this claim, Malaysia maintains that competition law has to "take into account existing industrial policies including those promoting 'national champions'" (OECD 2003, p. 4). The South African government and the private sector in that country often argue in merger cases that "developing countries should take a benign, even facilitative, position on 'national champions'" (OECD 2002, p. 3).

11 For example Pakistan holds that "in most developing countries, competition is restrained by industrial policy […] especially by subsidising the so-called 'national champions'" (*OECD* 2004, p. 3).

The empirical evidence about national champions is, however, rather mixed at best. Even the Korean development of the automotive industry in the so-called ‘chaebols’ is nowadays being reviewed rather negatively. “The recent history of the Korean auto industry thus appears to be a simple story: the transition from an industry created by a developmental state following a strategy of techno-nationalism to an industry incorporated into global production networks and substantially foreign owned. With the financial crisis, technoglobalism supplanted technonationalism. [...] A strategy of promoting technological autonomy no longer appeared viable where access to the latest technologies, access to markets, and to economies of scale and scope had become defining characteristics of viable competitors in a globalized industry” (Ravenhill 2001, p. 5).

In more general terms, we would conclude that first, the specific support of particular industries or firms has distorting effects on competition, so that prices, determined by market-mechanisms, cannot confer the correct information to investors and scarce resources are allocated in an inefficient way. Moreover, globalisation makes the idea of national champions superfluous. Large-scale companies, in particular, have to embrace a multinational strategy of sourcing in global supply chains, of global production, and of global selling, a genuine global presence in all aspects of their business. This and the unresolved problem of picking the right candidate to perform as a national champion (German Monopoly Commission Report 2002/2003, pp. 1-12) led the more developed countries to switch from the promotion of national champions to the promotion of small and medium-sized enterprises (Parker 1999)[12]. The larger companies themselves switched their strategies from national to multinational (Sleuwaegen et al. 2001). To the extent there is any specific support of particular industries and firms in developed countries today, it is for SMEs, although the benign role of SMEs is increasingly being challenged empirically (see above under ‘scale economies’). Hence, national champions should be those that thrive in fair and open competition in the domestic market and consequently emerge as competitive in the world market. In this respect, the concept of ‘hidden champions’, emerging from a competitive environment without selective policy nurturing and typically of a rather small size yet particularly successful in world markets, appears to be rather more successful.

4.1.5 Foreign direct investment

The claims raised against a national competition policy with respect to foreign direct investment (FDI) are twofold. First, where FDI is considered an important source of economic development, and of technological progress – in particular in developing countries (OECD 2002, p. 2) – it is feared that introduction of competition laws may negatively affect the inflow or structure of foreign direct investment (reported e.g. by Dr. Nguyen Minh Chi: OECD 2002, p. 3, however, he does not support this statement. Also

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12 Although even in the EU, some “national paradigm” is still prevalent (*Klein* 2004).

in: Cooke and Ellitott 1999). In these countries, preferential treatment of FDI is often used in an attempt to attract foreign investors and compliance with competition rules would seem to forbid continuation of this kind of practice. On a related issue, allegations were made in Poland, that "new provisions requiring the consent of the Anti-Monopoly Office for capital mergers would have negative impact on new direct foreign investments" (Szałamacha 1995, Gronowski 1995). Hence, some developing countries are seeking to draft a competition law that "balances competition and continuance of FDI" (OECD 2002, p. 2). Because of a real or alleged impact on FDI, some countries, in effect, treat competition law as a lower priority than FDI (this was reported by the Zambian representative: ibid., p. 10).

The second kind of claim is related to the fear that multi-national companies (MNCs) from more developed countries are more powerful and, when allowed to compete on a level playing field with small and, therefore, weaker domestic firms, could dominate the host economy. The winners of such an 'unequal' competition would be the multinationals and welfare losses would accrue. In this respect, the UNCTAD secretariat reports many reservations on behalf of developing countries to liberalise foreign trade and to open borders, allowing import competition and FDI to flow into their markets. Also, it has been claimed that "[f]oreign firms often took advantage of the liberalization of trade and foreign direct investment to dump substandard products with hazardous consequences for consumers" into developing country markets (UNCTAD 2002a, p. 4).

FDI is driven by the expectation of a profitable investment in the economic framework of the host economy. However, if the profitability of an investment depends on preferential treatment – in terms of tax holidays, competition-reducing import restrictions, etc. – then it becomes questionable whether this investment is in fact desirable for the host economy or whether it rather constitutes an inefficient allocation of resources. This pertains mainly to preferences for investors in particular sectors. Often countries attempt to invite foreign investment into particular sectors to speed up a sectoral and technological development that would otherwise not happen or would only happen at a much lower speed. The objective here is to alter path-dependent development patterns.

From a theoretical point of view, however, investment that does not correspond to the host country's pattern of comparative advantages is in reality a wasteful use of resources. Only investment that corresponds to comparative advantages truly generates higher welfare levels. In terms of empirical evidence, it is difficult to prove this theoretical argument, mainly because many factors influence the success or failure of an investment. However, some case-studies from well-researched regions can be cited in support of our point. Most Central and Eastern European Countries at some point attempted to attract foreign direct investments in technology-intensive industries (e.g. the automotive sector) by way of incentives. The countries had an abundance of labour and, therefore, comparatively low wages and wage costs, and were hoping to create broad and sustainable employment at higher wages. However, the investment that was attracted in these sectors was typically rather capital-intensive with a bias towards labour-saving technologies. In the end, little employment was generated in relation to capital cost, forgone taxes or host country subsidies, and the special tariff agreements resulted in higher costs for consumers in the host countries (i.e. opportunity costs). Arguably, investment into infrastructure could have generated a higher level of employment and economic growth. A review of the literature on the effects of incentives to attract foreign direct investment in the Central and East European automotive sector concludes that preferential treatment did not play a large role in the decisions of multinational investors, and re-investment did take place as planned, even where the preferential treatment had to be discontinued due to EU competition laws (Kämpfe 1996).

For other parts of the world, a review of empirical studies concludes that more competition is probably associated with rather more FDI inflow than the other way round, i.e. that there is a positive correlation between competition supervision and FDI. FDI inflows and inter-firm agreements in Japan are not correlated; a higher intensity of competition in the perception of business people was associated with greater inflows of FDI. The report concludes that only in case of mandatory pre-notification merger review laws, a dampening effect on FDI inflow could be empirically verified (Evenett 2003d, p. 9). In this respect, we would argue that it would seem odd to assume that mergers that would probably not be allowed under reasonable competition laws – and these are the only ones that would be discouraged by pre-notification procedures – could be welfare enhancing for the host economy overall. Hence, a country need not fear that the application of sensible competition laws would scare away genuinely desirable FDI, because FDI inflows are not welfare enhancing per se, or – to say it differently – not every investment is a good investment. Rather, the most preferential structure of FDI-inflows can be expected to emerge by adherence to market mechanisms supported by a competitive framework. Again, to say it differently, market mechanisms with sensible competition supervision are probably the most successful mechanisms for the selection of good FDI over bad FDI.

With respect to the alleged problem that there is an unequal distribution of power between large foreign and smaller domestic companies, an economic assessment would suggest that it is in fact a competitive environment that best promotes the ability of domestic firms to compete against foreign investors. The abuse of a power-advantage by foreign investors, for example in the form of predatory pricing for the elimination of the local competitor, can best be prevented by efficient application of domestic competition laws. Also, it is by no means typically the case that larger companies are more competitive in contestable markets. When state-owned companies are privatized, foreign investors often command more financial power, enabling them to win in competitive bidding over domestic firms. However, it would seem odd to assume that the price paid for a company exceeds its future value; hence domestic firms should be able to procure the price on the financial and capital markets. Moreover, the welfare losses of having the national economy dominated by foreign investors is confined to profit repatriation, as these are the only resources leaving the country and hence reducing domestic demand. This loss is normally smaller than the welfare loss incurred in a biased privatization, i.e. when domestic firms win the privatisation race only because they have been granted special treatment.

4.1.6 High investment intensity

Fast economic growth and swift economic development crucially depend on a high intensity of investment. This has led many countries to support investment projects at the firm level (in the case of Korea by way of subsidies: Wise 1999, pp. 4-5). Where investment, however, is selective, i.e. targeted at particular companies and not potentially available for all companies (in a horizontal design), this policy obviously contradicts competition law. Hence, some transition and developing countries share the concern that competition laws could have a negative impact on investment activity (e.g. Jamaica: OECD 2003, p. 3). The claim is that strong competition reduces profits of enterprises, which in turn reduces their possibilities to spend money on R&D, new technologies, new products, etc (Evenett 2003d, p. 6). Moreover, in developing and transition economies, companies often do not have the financial resources, collateral, or even sufficiently large profits to match the investment-power of companies from more developed countries. Hence, some transition and developing countries hold that some monopolistic power or oligopolistic power is acceptable in special (and not further specified) "circumstances" (for Hong-Kong: APEC 2005).

In theory, investment activity can be welfare enhancing. From a neoclassical point of view, capital accumulation fosters economic growth p.c. until the steady state is reached (Solow 1956). Furthermore, the endogenous growth theory points out that investment could foster long term growth through 'learning by investing' (Romer 1986). Therefore, especially in developing and transition countries where the capital stock is relatively smaller compared to developed countries, higher intensity of investment could be taken to be welfare enhancing. However, this is not correct for each case. In macroeconomic terms, every investment is associated with opportunity costs in form of reduced actual consumption. Only where profits generated from an investment project overcompensate the associated consumption-reduction effect in the long term, is the investment welfare enhancing. In general, economic theory indicates that a free market with competition is the best mechanism to identify welfare enhancing investment. Competition is necessary to force the firms to invest their capital in the best possible way. Prices, determined by the market mechanism, contain the information the investor needs. Furthermore, without competition, a firm has no incentives to invest at all. However, SINGH points out that in the real world of developing countries with incomplete and missing markets, unfettered competition may have ruinous tendencies and could be detrimental for investment activity. He suggests that developing countries need "an optimal degree of competition which would entail sufficient rivalry to reduce inefficiency […], but not so much competition that it would deter the propensity to invest" (Singh and Dhumale 2001). Empirically, there is little evidence about the interrelation between competition intensity and investment activity. To the best of our knowledge, there exists only one study by Evenett on this issue (Evenett 2003d). This study indicates that competition enforcement is beneficial for state investment activities as it helps to avoid bid rigging and cartel activities of private firms which could be detrimental for state investment decisions. With respect to private incentives for investment, the study identifies cases where competition enforcement reduces investment activity as well as cases where investment activity is increased (ibid., pp. 11-12). In summary, competition law may not maximise investment activity but rather optimises investment activity.

4.1.7 Research and development, innovation, intellectual property rights

Some countries argue that the introduction of competiton law can reduce the intensity of R&D at the firm level. This is based on the idea that certain kinds of non-market conditions or transactions are necessary or beneficial for R&D or that some state assistance leads to more or better R&D. For example, Egypt argued that "[c]ompetition policy may also limit cooperative efforts in the field of R&D" (Mahmoud Mohielding: OECD 2002, p. 12). Consequently, in order to maximise R&D, some cooperative behaviour should be allowed. This claim prompted Taiwan (specifically, the country excludes concerted actions that "promote joint research and development": OECD 2001, p. 2) and Indonesia (here, the carve-out refers especially to joint ventures in R&D and intellectual property rights: ibid., p. 3) to exclude some provisions from their competition law that pertain to inter-firm R&D efforts. However, with competition law in place that exempts cooperative behaviour (for R&D), Egypt warned that this "can be used as a façade for anticompetitive practices" (Mahmoud Mohielding: OECD 2002, p. 12). In a related way, one might argue that even problematic behaviour by a dominant firm might not be considered abusive, if it promotes technical progress (OECD 2003, p. 3). Moreover, monopoly profits can "act as a spur to innovation and the creation of new products and processes" (Evenett 2003d, p. 6). Yet another claim refers to the virtues of state aid for the stimulation of R&D (e.g. state aid for R&D is allowed in Romania: ibid., p. 4). In fact, even the developed countries implement various forms of research policy by providing finance for basic and applied research in universities and research institutions, and the EU Commission, on the supranational level, has its Framework Programmes.[13]

Economic theory suggests that a dominant position or a monopoly of one firm is not necessarily an undesirable market outcome. As Schumpeter recognized, firms are permanently engaged in creating new products or improving their efficiency to achieve or maintain a competitive advantage over their competitors. The most successful of these firms will achieve a dominant or even a monopolistic position after some time and may

13 Such research, however, is typically competitively allocated and usually horizontal in its design, hence produce rather little distortions.

reap super-competitive profits for a while until they are overtaken by another firm (Schumpeter 1942, pp. 81-106). The very possibility of making monopolistic profits is, therefore, the main incentive for firms to innovate and to vigorously compete in the first place. If this possibility is reduced by state action trying to preserve contestable markets, firms may lose (some of) their incentive to innovate and may reduce their R&D activities (Motta 2004, p. 55). Hence innovation-related monopoly profits, if transitory and proportionate to the efforts invested to generate the innovation, are welfare-enhancing. In such a situation, contestability of the market is still guaranteed. If innovation-related monopoly profits exceed the costs of generating the innovation, a new firm can enter the market and soak up the excess rent. Only where the innovation-monopolist erects entry-barriers, competition law has to intervene. However, this intervention is not welfare-reducing.

In fact, management theories and empirical studies suggest that a competitive environment contains the largest potential for generating innovation (the so-called pro-competitive effect), because firms are constantly forced to invest in R&D with a view towards adopting and generating new technologies, and thus to defend their position in the market (see for a more detailed description: ibid., pp. 39-64). In the absence of competition, firms tend to become complacent and profits are not used to innovate and create new products and processes. This was most clearly illustrated by the failed socialist experiment.

With respect to cooperative efforts between firms for the purpose of R&D, we find several reasons why allowing such cooperation can be welfare-enhancing. Rather than completely exempting cooperation (allegedly) dealing with R&D from competition law, this behaviour should be governed by sensible rules within national competition law. The first reason is the existence of technology spillovers between firms. Technology spillovers may result if firms are unable to contain the full benefits of their R&D activities, i.e. when they cannot avoid that other firms also benefit from these activities (incomplete internalisation, externalities, and market failures). This may reduce the incentives of firms to innovate. Furthermore, it is sometimes beneficial for R&D activity, when firms put their knowledge together to avoid re-creating knowledge which already exists and which is needed for the innovation process (ibid., pp. 203-204). An example would be a situation where different firms hold patent rights on different products or processes which are needed to develop a single new product. BAUMOL (Baumol 2001) as well as Leahy and Neary (Leahy and Neary 1997) elaborate in more detail how R&D cooperation can be beneficial and welfare improving. Moreover the results of Leahy and Neary indicate that cooperation is to be preferred over alternative R&D policies, like subsidies. These authors further claim that R&D cooperation between firms is beneficial on its own and needs no government incentives.

However, cooperative efforts are not always beneficial for R&D activities. First, this may be the case if spillovers do not exist to a sufficient extent. Second, R&D cooperation is not beneficial, if the combined market share of the participating firms is too high, and the incumbents gain the power to prevent competition (Motta 2004, pp. 204-205). Furthermore, cooperative efforts in R&D could be anti-competitive, if the cooperation does not only comprise R&D activities but also includes cooperation in production and marketing.

The implications for optimal competition law are the following. First, competition law should not concentrate on transitory and limited monopoly profits and should rather focus on fostering competition through the reduction of entry barriers, making it easier for new firms to enter the market (compare also Evenett 2003c, p. 25). Second, cooperative efforts in R&D might be favourable (this is also the case in US and EU, where R&D joint ventures are particularly treated: Motta 2004, p. 205), if spillovers exist and competition, especially on the product market, is ensured. Specifically, this means that competition law should ensure that the R&D cooperation does not reach too far into the product market (ibid., p. 204) and that entry barriers into the market are low (enough). Moreover, an independent competition authority would be the appropriate institution to decide on a case-by-case basis which cooperation to allow and which not to, because it is sufficiently far away from business and government not to fall prey to vested interests.

4.1.8 State owned enterprises

Some countries hold that state-owned enterprises are an important factor for economic development and industrialisation. This argument has been raised, in particular, by Thailand, Indonesia, Malaysia, the Philippines, and Singapore.[14] The representative to the OECD for Pakistan stated that "until [the] late seventies, […] state-owned enterprises were found to be the major borrowers in domestic and world credit markets; and commanded a sizeable share in the budget" (OECD 2004, p. 3). Since state-owned enterprises are governed by powers other than markets (in terms of objectives as well as management), and since they typically enjoy some form or other of state guarantee and soft budget constraints, i.e. they cannot fail and have no strict obligation to allocate resources efficiently, a market involving state-owned enterprises cannot provide a level playing field for private firms. Competition law would have to force governments to discontinue preferential treatment. State-owned enterprises would then, for the first time, be exposed to open competition, and would have to decline to fulfil the non-market objectives previously imposed by the government. Hence, enacting competition law and applying it to all enterprises would contradict the socio-economic and other non-market objectives of a country that used to pursue these by heavily relying on state-owned enterprises in its economy.

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14 "Parastatal institutions and conglomerates, or in some cases even monopolies, in addition to special regulatory regimes for the exploitation of natural resources, can play an important role in the development process". Comments by the representative of Thailand, speaking on behalf of ASEAN WTO Members, in *WTO* 1998a, pp. 13-14.

Mexico raised another concern against the adoption of competition laws and their application to state-owned enterprises: in case of a crisis, it might become necessary to re-nationalise important industries of national interest, e.g. utilities (OECD 2004b, p. 29).

“Indeed some of the questioning has gone even further with many orthodox development economists beginning to recognise again that there are a range of key goods and services [e.g. natural monopolies, utilities] that cannot yet be provided through markets alone” (OECD 2003, p. 3).

In terms of economic rationale, and as argued in our section on ‘development models’ (see chapter 4.1.1), industrial policy is an inefficient development strategy. Competition between firms played an essential role in the development process of even the South East Asian tigers during their successful catching-up process. State-owned enterprises are not per se less efficient, however, and can fulfil an important role in a competitively organised economy (including in the case of a crisis), but only if submitted to hard budget constraints and only if they operate on a level playing field with private enterprises. Again, a national competition law controlling governmental influence, as well as the market power of state-owned companies and their behaviour, is still the optimal policy for economic development.

4.1.9 Control over tax base

In the context of the alleged virtues of state-owned enterprises, it is sometimes argued that increased competition and privatisation of state-owned enterprises, can erode the tax base (Langhammer 2000, OECD 2002, this was also raised by Cameroon in the more general framework of “sovereign control over their countries economic mechanisms: OECD 2004, p. 3). In the particular case of China, this argument was raised by local governments. In China, the tax base depends on local companies, and competition with companies in other regions can be a peril to the tax revenue of a local government (Xue Zheng Wang (state administration for industry and commerce): OECD 2004).

This claim, however, seems to be rather odd: maximising tax revenue from enterprises would require the taxed entities – here state-owned enterprises – to achieve maximum profits. This, in turn, would necessitate that the taxed entities operate efficiently. As argued above, state-owned enterprises can in fact be efficient if they operate under competitive market-governance without interference by the state. Control over tax revenue is an issue for the system of taxation. Differentiated tax-treatment of economic entities will distort investment decisions. This will cause inefficient allocation of resources and is sub-optimal compared to situations where taxes are assessed objectively on the basis of performance. With respect to competition between companies of different regions in China, a local government can in fact see its tax base erode if its own state-owned enterprises fail to compete against enterprises in other regions. This, however, is a question of the competitiveness of companies in the region and the pattern of specialisation between regions – if private companies in the weaker region are unable to compete, why should state-owned enterprises do any better? Rather, open competition between regions would eventually provide the most efficient patterns of specialisation (allocation of resources), maximising welfare across the whole country. Regional cohesion is best targeted by policies of redistribution rather than by the control of state-owned enterprises.

4.1.10 Imperfect capital and financial markets

The problem that investment activity is insufficient in transition and developing countries is aggravated by the fact that in some such countries, capital and financial markets are still rather immature or underdeveloped. "[I]mperfections in the capital market create differential entry barriers for different types of local entrants (small vs. large, established vs. new) and between domestic and foreign players" (Cuts 2003, p. 27). For example, in Central and East European transition countries, underdeveloped financial markets forced many companies to borrow from abroad – in the case of domestic firms as soon as convertibility was granted, and in the case of foreign investment subsidiaries directly via the headquarters. References to this problem were made in a parliamentary debate on the reform of competition law in Poland, and in the case of Hungary, the underdevelopment of the financial sector led to current account and exchange rate pressure, inflation, and even first signs of capital flight associated to the non-acceptance of the domestic currency (for Poland: Cylwik 2005, p. 19).[15] The alleviation of higher barriers for small and/or new enterprises or for domestic enterprises vis-à-vis their foreign competitors by way of policy intervention is, however, seen as potentially in contradiction to the rules of national competition law. Moreover, higher interest rates also typically result in lower levels of investment and/or investment projects involving higher risks of default (adverse selection and credit rationing (for a theoretical explanation of this, see Stiglitz and Weiss 1981). Whilst the described effects of incomplete financial markets are in fact visible in some countries, remedies should not be in conflict with national competition laws. First, putting domestic companies in the position to procure credit on international financial markets might involve a slight risk-surplus on international credit rates. Second, the most important remedy should target the problem itself, i.e. the development of the domestic financial sector (including capital and financial markets, and the banking system with an independent and credible central bank at its core). Again, the experience of Central and Eastern Europe after the demise of the planned-economy system is a case on point. Granting access to foreign financial markets for domestic enterprises, as well as the development of the domestic financial sector, proved to be successful remedies without involving any anti-competitive practices like nationalisation of companies (e.g. by way of debt-equity swaps), crediting by the state, (implicit or explicit) state guarantees for commercial credits, and the like.

15 In the case of Hungary, those effects forced the government to turn around with respect to introducing currency convertibility (see *Stephan* 1999, p. 151).

The proposed granting of access to international financial markets for domestic investors necessitates, however, some degree of convertibility of the national currency, i.e. the removal of foreign exchange restrictions, of the control over capital and current accounts (convertibility), of controls of exchange and interest rates. Some countries report that such reforms added to the difficulties already experienced with financial and currency stability and brought about a painful increase in domestic interest rates, as well as generally higher interest rates in comparison to other countries (e.g. reported for Zambia, Sri Lanka, India, and Pakistan: Cuts 2003, pp. 25-26). This produced a non-level playing field, because foreign firms now had access to cheaper capital compared to domestic firms and were able to outperform them even more. Tanzania's banking sector reforms did not lead to the expected fall in interest rate spreads, again giving foreign firms an advantage (ibid., pp. 25-26). This could make it necessary for those countries to support domestic enterprises and new entrants, which, in turn, could impede their willingness to enact competition laws. In the case of Korea, the government supported the chaebols as a substitute for developed capital markets ("absence of developed factor markets" (Wise 1999, p. 5, and Josef Seon Hur: OECD 2002, p. 3).

Whilst the reported detrimental effects of financial liberalisation remain undisputed, the reasons do not lie in the act of liberalisation, but rather in the state of underdevelopment and imperfectness of the domestic financial markets. Any policy attempting to fight the symptoms rather than the roots of the problem remains suboptimal. A competitive environment remains the best tool to develop financial and capital markets and to overcome the imperfections in the financial sector.

4.2 Substitutes for competition law

Several countries, including Thailand, Indonesia, Malaysia, the Philippines, and Singapore, have argued that "competition policy actually comprises the full range of government measures that impact on market structure and conduct, including trade liberalization measures. Thus, a commitment to competition policy need not entail the adoption of a traditional competition law" (WTO 1998a, pp. 13-14). This raises the question whether there is actually a "need for a comprehensive competition law for delivery of competition policy" (ibid., p. 16).[16] In this respect, the WTO working group for competition policy reports that "some other delegations have expressed the view that, while it may indeed be possible for a country to have a competition policy without having a competition law, having such a law provides important benefits. These include ensuring greater consistency in enforcement approaches across industries; giving the policy statu-

16 Argued by e.g. Thailand, Singapore, and Hong Kong, China. (*WTO* 1998a) Pakistan extends the list of substitutes by FDI policy and regulatory policy: "These policy tools comprise of rules and regulations that serve purposes other than maintaining competition, with a view to fostering efficiency." (*OECD* 2004, p. 2).

tory character, enforceability and stability; enhanced ease of adaptation of new analytical techniques applicable across sectors and a reduced danger of institutional ‘capture’ of a comprehensive competition authority as compared to the situation of regulators that focus on particular economic sectors” (WTO 1998a, p. 16).

4.2.1 Sectoral approach

Sometimes it is argued that there is no need for comprehensive competition laws, since increasing competition is only necessary in particular sectors, and that some sector, for example public utilities, operate better under regulation than under competition law. For example, Hong Kong, China, and Singapore (Singapore finally accepted the advantage of enacting a competition law, the law has been passed in October 2004) describe their competition policies to be implemented through sectoral regulatory policies, codes of conduct, and other appropriate means, rather than by adopting a comprehensive competition law (WTO 1998a, p. 16).[17]

Hong-Kong and China also declared that their competition policy framework is defined through policy statements on competition, rather than in the form of law. Policies to be pursued include “prudential supervision, service reliability, social service commitments, safety, etc.” (APEC 2005). They reinforce and implement the policy statements with sector-specific measures which are explicitly not limited to laws (ibid.).

A sectoral approach as a substitute for comprehensive competition law is likely to be insufficient, however. While a sectoral approach may effectively address competition issues in some specific sectors, competition issues in all other sectors remain neglected. In those other sectors, anti-competitive practices remain unchallenged, with all negative effects on economic development and welfare, like increased prices, market entry barriers, or lower innovation activity (see chapters 4.1.7 and 4.2.4). From an economic perspective, there are further drawbacks to a sectoral approach. First, sectoral regulations distort the efficient allocation of resources, where some sectors are regulated and others are not. In such an environment, private agents not only have to observe price signals to determine the rates of return on investment, but also institutional barriers and regulatory decrees. This might even be the case where all sectors are regulated, if rules and regulations are different in different sectors or interpreted differently by regulatory agencies (Chen and Lin 2002, pp. 156-157). Second, an independent competition agency can be expected to control industries more independently, being free from particular interests, compared to a sectoral regulator. The latter is potentially more involved in vested inter-

17 In the particular case of Singapore, the regulated sectors include broadcasting, power and gas, local transport (including train, bus and taxi services), Singapore port and harbour, telecommunication are regulated: “Under the WTO negotiations for telecommunication services, Singapore has made broad pro-competitive commitments in the areas of interconnection, competitive safeguards, transparency in regulations and independence of regulators” (*APEC*).

ests within the regulated industry (ibid., pp. 157-159). LIN exemplifies this with a case study about an acquisition made in Hong Kong, China. In this case, a Hong Kong telecom firm was allowed to acquire a competitor equipped with a mobile licence, after having been unsuccessful in the bidding process for a limited number of licences. After that, the regulatory agency had problems to explain why it compromised the regulatory environment by allowing the loser to acquire a licence through the back door. Furthermore, this acquisition seemed not to be independent of particular interests, as it could be regarded as a compensation deal for the prior termination of the monopoly status of the Hong Kong telecom firm. LIN claims that this is not a specific case[18], rather that it reflects problems of the sectoral approach that emerged "from the presence of asymmetric information, and will likely also arise in other sectors" (Lin 2004, pp. 19-20). However, this does not mean that there is no need for sectoral regulation. In some fields, there are good reasons for specific and different sectoral regulation, in particular in network industries or industries which have features of a natural monopoly (see e.g. Borissova 2002). The main reasons are high sunk costs, which raise entry barriers by requiring potential new entrants to make high investments (e.g. railway systems, power systems, fixed line telephone services), or increasing economies of scale, or network advantages.[19] In those particular industries, it may be efficient to have all business handled by a single firm. In fact, regulation for parts of these sectors is even done in countries of the developed world. To sum up, sectoral regulatory measures do not contradict the need for comprehensive competition laws. Rather, sectoral regulations should supplement competition law in particular fields. They cannot produce an efficient outcome as stand-alone measures.

4.2.2 Foreign trade

It is sometimes argued that transition and developing countries merely have to liberalise foreign trade to increase competition on domestic markets via imports (Cuts 2003, p. 17, and Cooke and Elliott 1999, pp. 2-3)[20], because foreign trade can promote competition far better than the adoption of a competition law (Kovacic 2001, p. 287, in particular for Singapore and Hong Kong, China: APEC 2005, for Indonesia: OECD 2004, pp. 2-3, and

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18 An interesting case on point is the recent merger in the German energy sector (E.ON and Ruhrgas). In this case the merger was forbidden by the German competition authority. However, the German Minister of Economic Affairs at the time, who was responsible for the recently liberalised energy sector, allowed the merger by ministerial decree. Today this minister is a senior manager in the merged firm. Furthermore, it became known that the minister was on the payroll of one of the merged firms at the time of the merger.

19 For example, in the energy sector, the coverage of the whole area with power distribution systems is relatively expensive, whereas the costs for connecting customers to the power grid in already serviced agglomerations are relatively low.

20 In particular for Singapore and Hong Kong, China: *APEC*, for Indonesia: *OECD* 2004, pp. 2-3, and for Jamaica: *OECD* 2003, p. 3.

for Jamaica: OECD 2003, p. 3). Taiwan's version of the claim refers to the early stage of economic liberalisation of a country, is restricted to small businesses (APEC 2005), and includes the trinity of trade liberalisation, de-regulation, and privatisation (OECD 2004, p. 2, the latter was also mentioned by Zambia: OECD 2002, p. 7). The representative of Peru even holds that merger control can prevent benign rationalisation processes in an environment of a high degree of openness, where merged companies are controlled by foreign competitors (WTO 1998a, p. 17). Not questioning explicitly the necessity of competition law, the Estonian government reports that "[i]n the case of Estonia the number of markets solely or even partly supplied by the domestic goods is very limited. Even the markets that are supplied by our most prominent industries, like the furniture industry, face very strong competition from abroad" (OECD 2003, p. 3). The representative of Singapore to a working group meeting at the WTO in 1997 held that "the 'import-discipline hypothesis' had ceased to be a hypothesis and had become a fact" (WTO 1998b, p. 12).

From a pragmatic point of view, one could argue that for countries with weak administrative capabilities and rudimentary institution building, "enforcing trade liberalisation may still be the most straightforward strategy to help competition to increase" (Langhammer 2000). While this is all well, it does not solve the question whether trade liberalisation can, on a long term basis, act as a perfect substitute for competition laws. One might be tempted to assume that import-competition from abroad is a sufficient condition for the contestability of markets, because firms in an integrated economic area do not think nationally but in terms of the integrated market. A domestic monopoly cannot abuse its dominant position by restricting output below the market-efficient optimum or by reaping monopoly-profits as long as competition or even potential competition from abroad exists. However, this assessment falls short of reality in some respects (WTO 1998a, p. 12). First, not all products or services are tradable, and for those that are not, competition from abroad cannot exist, whether this is due to transportation costs or the locality of services. Foreign trade liberalisation can be supplemented by the opening up of domestic markets to foreign investors (including in the non-tradable sectors), but a national competition law still remains necessary to prevent investors from dominating the domestic market. Moreover, a monopolist in the domestic non-tradable sector could harm the competitiveness of a firm in the tradable sector if it served as a supplier. Second, anti-competitive practices can also be agreed upon between domestic and foreign firms. In the absence of regional agreements with respect to competition, national competition legislation remains indispensable to guarantee contestability. Third, import restricting entry-barriers can be erected either by government measures including e.g. regulations, standards, licensing requirements, but also by the private sector, for example via outright vertical market restraints as a device for deterring imports (Kemani and Dutz 1995, of course, where non-tariff barriers exist, the claim that liberalised foreign trade acts as a substitute for competition laws is flawed in itself). In fact, even in the case of the EU as a highly integrated economic area, individual states found it important to have their own national competition laws (if only to coordinate competition policy between domestic and European jurisdictions). All in all, liberalisation of foreign trade is not a perfect substitute for national competition law, and can rather serve as a complementary policy measure.

4.2.3 Privatisation, corporatisation, and economic deregulation

Some countries have the view that privatisation is a sufficient tool to increase efficiency, and that there is no need for national competition law. Thailand's government, for example, argued that privatisation policy is the most important policy to build a competitive environment (OECD 2004, p. 2). In Singapore the government decided to commence a programme of corporatisation and privatisation in services to foster competition and market discipline (APEC 2005). Specifically for developing countries in transition, Zambia questioned the necessity of competition law if privatisation is paired with trade liberalisation and deregulation, and noted that developing countries place "greater emphasis [...] on privatisation and not on the economic efficiencies to be created thereafter" (OECD 2002, p. 7). In this sense, Taiwan stated that especially in the early stages of economic liberalisation, a country could achieve efficient allocation of resources and better choice for consumer through trade liberalisation, and de-regulation, supplemented by privatisation (OECD 2004, p. 2). The representative to the OECD Global Forum on Competition of Pakistan even alleged that it has been "realised around the world that privatisation can create market discipline without running the risk of concentrating ownership" (ibid., p. 3). Furthermore, China argued that the current time of transition from a planned economy to a more free-market economic system was not the time to establish a comprehensive competition law. Moreover, it was argued that administrative monopolies were a specific phenomenon of the transformation process and would only decrease with progress in further reforms. Again, as a consequence, there was no need for the adoption of a comprehensive anti-monopoly law at this time (OECD 2001, pp. 6-7).

Whether a firm is owned by the state or in the hands of the private public has nothing to do with the efficiency the firm produces or with the intensity of competition of the market it operates in. As has been argued in the chapter on 'State-owned enterprises' (Chapter 4.1.8), privatised firms are not per se more efficient than state-owned firms, provided the latter are submitted to hard budget constraints and have to operate on a level playing field with private enterprises (i.e. the state-owned firms do not have to fulfil political objectives next to the maximisation of profits). Additionally, privatising firms is neither a necessary nor a sufficient condition to increase the contestability of a market. Where privatisation is supplemented by the removal of entry-barriers (with which the formerly state-owned firm had been protected from competition), the effect of intensifying competition has its roots in the removal of entry-barriers and not in the act of privatisation. Hence, privatisation as such cannot fulfil any of the objectives of competition law and, consequently, cannot act as a substitute for the enactment of national competition law.

The concept of ‘corporatisation’ on the other hand targets the efficiency and profitability of a state-owned firm without necessarily privatising the firm. In theory, corporatisation would in fact submit a formally protected firm to competition, and hence to ‘market discipline’. However, if the respective market is not contestable, for example because there is a natural monopoly or there are entry-barriers, the process of corporatising a firm does not increase the intensity of competition. Corporatisation also remains a powerless substitute for national competition law. This assessment of the claim pertains just as much to economies in transition from a planned system to a system of competitive market governance, as to economies during their early stages of economic liberalisation, as for any other market-governed economy. In this respect, the experience with the sequencing-question of economic reforms gained by the Central and East European transition countries can tell us that any gradualism in the field of competition only prolonged the costs of transition. The most efficient and cheapest design of economic transition proved to be an immediate switch from one coherent system to another and any intermediate step produced nothing but incoherent outcomes which could not persist over time. This also applies to administrative monopolies which – given the new system of economic governance – also face the need of profound reform and learning.

Furthermore, a market in which privatised and corporatised firms operate side by side is just as much – or perhaps even more – in need of competition law as is any other market comprising only private firms. Without adequate competition supervision, corporatised firms might try to solidify their inherited market power by turning to unfair practices and nothing would be gained in terms of beneficial effects of competition. In this respect, UNCTAD reports that in some cases, privatised firms “took advantage of weak Governments to monopolize markets” (UNCTAD 2002a, p. 4). Competition law is precisely the right tool to fight this uncompetitive behaviour.

4.2.4 Direct measures like price control

One of the obvious policies substituting competition law in respect of consumer welfare and resource allocation are direct measures like price controls, business licenses, and even state planning, as well as outright nationalisation of firms that – according to the opinion of the government – do not act in the interest of consumers. It has been argued by some countries that such measures can act as substitutes rendering the adoption of competition law unnecessary. Examples for such policies include generally economic planning in socialist countries with price fixing focused mainly on prices of basic needs (food, rent, energy), price fixing in Kenya “to develop the economy and protect consumers” (OECD 2001, p. 2), price controls and state ownership in Mexico “to eliminate the evils of private monopoly” (OECD 2004b, p. 12), maximum selling prices for sugar in Thailand for the sake of consumer protection (APEC 2005), as well as Korea’s attempts to control, to direct, and to protect many market activities with business licenses to achieve a more beneficial allocation of resources (Wise 1999, p. 4).

In an economic system governed by markets, prices are determined by supply and demand and expectations about how these will develop in the future. This price-mechanism signals to investors how to allocate resources to maximise profits, and in the aggregate, this mechanism assures efficient allocation of resources. Hence, interference in the market mechanism inevitably produces distorted signals and reduces overall welfare. Only where market failure exists can intervention in the market be welfare enhancing, provided the intervening body can in fact remove the market failure (e.g. natural monopolies) (Motta 2004, p. 25). Usually such markets are governed by a sectoral regulator. The objective of enhancing consumer protection through price controls (e.g. for basic consumption goods) is rather a political one. As a tool of social policy, it is, however, suboptimal in as much as it distorts signals and will typically prompt investors not to engage in the production or improvement of goods or services where regulated prices are lower than marginal costs. A shortage of supply is the result, exerting upward pressure on prices. For social goals, a transfer mechanism by way of redistribution can fulfil the objective without the detrimental effects of price distortions.

4.3 Competing priorities political and opportunity costs

The policy-objectives of competition laws do not always harmonise with other objectives a government may want to pursue. In some cases, conflicts in policies emerge, and countries may choose not to enact competition laws, if the rival objective supersedes the objectives of efficiency and consumer welfare.

4.3.1 Regional policies

The mechanisms in contestable markets allocate economic activity to regions where the activity provides the highest returns. Whilst this conforms to an efficient allocation of resources and maximises welfare of citizens overall, the result of the process, more employment in one region, less in another, may still be undesirable in the view of a specific country. In the absence of migration, job losses in some regions can be a huge burden for the whole country, as the inhabitants of such less advanced regions still need some form of support, or because such regions can be seen as a waist of (human) resources. In fact, regional policy, i.e. the avoidance or moderation of these effects, plays an important role in the European Union, where economic cohesion across regions is an explicit policy-goal[21], despite the fact that this is at variance with the objectives of competition law. In a crucial view, Pakistan stated that "structural policies pursued by the developing countries have easily restrained and distorted effective competition, […] e.g. regional policies which may favour an inefficient and marginal part of a certain sector of the

21 Even some aspirants of EU membership with some form of competition law already exclude state aid for regional policy (see e.g. Romania: *OECD* 2003, p. 4).

economy and, thereby, discourage an efficient part of the same sector located in another area" (OECD 2004, p. 4).

Economic literature extensively discusses whether regional policy is welfare enhancing for a country (or a target region within the country) or rather incurs welfare costs (see e.g. European Commission 2004, Puga 2001, and Martin 1999). Since this discussion in a broader sense goes well beyond the purpose of the present study, we focus on the effect of regional policy on competition. If regional policy takes the form of indirect or direct state aid to companies in less advanced regions, it affects the respective intensity of competition between firms inside and outside the target region. Such a regional policy would not be in conformity with the objectives of competition law, namely to guarantee a level playing field. However, where regional policy takes the form of alleviating regional disadvantages due to an insufficient endowment with immobile factors of production, for example the supply with infrastructure, it does not impinge upon the competitive position of rival firms and hence is compatible with competition law. In fact, a regional policy that is targeted at compensating locational disadvantages, can be built into a national competition law, as exemplified in the European Union.

4.3.2 Political costs

In some countries, there seem to be concerns that adopting and implementing a competition law may cause political costs. Political costs emerge if a government, for lack of public support, finds itself unable to introduce policies or laws which will have positive and desirable effects in the long term but impose certain burdens in the short term. Competition law has long term effects, governments need short term development results. Pakistan gave some indication how developing countries often need to achieve short term results, whereas competition law achieves long term effects, and needs to be supported by a deep-rooted competition culture within the society (OECD 2004, p. 2). The Latvian competition authority saw the existence of short-term adjustment costs ('by-effects'), but claimed that the long-term effects will prevail (OECD 2002, p. 2). Representatives from Argentina pointed out that "there is a danger of attributing to competition policy social costs that are really the result of more systemic changes relating to a movement away from pervasive regulation and state ownership" (WTO 1998a, p. 15).

The theory of political economy suggests that politicians primarily pursue a policy that is beneficial for themselves (mandate). Hence, for politicians it is often more beneficial to reduce actual social problems with short-term fixes, rather than maximising welfare over time. However, from an economic point of view, there is no question about taking the measures which maximise welfare over time. In the particular case of developing countries, eliminating social problems might even be welfare enhancing, as it could help to stabilise a country politically; political stability in turn is one of the most important conditions for economic development. This does not question the need for competition law as an instrument to increase static and dynamic efficiency. Competition law should rather be designed in such a way that it meets country specific particularities. For example, in the case of South Africa, racial imbalances were specifically targeted by the provisions of the competition law and that neither contradicted the goals pursued via the introduction of the competition law, nor did it cause other significant and undesirable problems.

4.3.3 Social policies

A competitive, market-based economy rewards the economically active and successful participants and withholds the fruits of economic activity from the economically inactive and unsuccessful participants. Where markets are imperfect, however, it is typically the weakest members of society that are affected most; "especially the illiterate and the poor, suffered most from market failures and asymmetry of information" (UNCTAD 2002a, p. 4). A competitive free-market system typically results in an unequal distribution of income. The objective of a social policy is to provide some extent of redistribution to alleviate gross inequality and poverty by providing access to a social security system (unemployment benefits and healthcare). Additionally, social policy can target economic inequality where it is related to characteristics beyond the control of the participant, like racial imbalances. Social policy, therefore, is derived from a political objective, but becomes relevant in economic terms where unused or underused resources produce a gap between actual and potential output and where gross inequalities contain the danger of social unrest and political turmoil. In some developing countries, given large income inequalities and many uneducated and poor members of society on the one side, and limited resources for compensating social policies on the other side, the enactment of competition laws was not granted the highest priority.

For example, Thailand argued that other economic and social policies, like dept-relief for small farmers, a people's bank, a bank for small and medium enterprises, health insurance, drug rehabilitation centres, etc. were more important than a competition policy (OECD 2004, p. 2). In the same way, Jamaica stated that developing economies do not generally place the implementation of competition law on their priority list, because they have limited resources and more pressing social problems (ibid., p. 2). Another example is Malaysia, which stated that its affirmative action policy to reduce poverty and to remove racial economic imbalance was one of the constraints against the implementation of a competition policy (OECD 2003, p. 2). In Kenya, even after the adoption of and amendments to the competition law, "national priorities gravitate towards more veritably mundane sectors such as health, poverty alleviation and education" (OECD 2002, p. 4).

Other developing countries (e.g. India, Tunisia) raised the concern that competition law might increase unemployment and might have a negative impact on the survival of (small and medium sized) enterprises (WTO 1998a, p. 14, and Cooke and Elliott 1999). Similarly, Egypt reported that "competition was seen as a social burden and a political liability, as it may lead to the ultimate exit of uncompetitive firms and hence the possibility of increasing unemployment" (Mahmoud Mohielding, Professor in Economics and Senior Advisor to the Egyptian Minister of Foreign Trade: OECD 2002, p. 6). Pakistan raised the claim that "in most developing countries, competition is restrained by industrial policy […] to protect the labour force against the risks of dismissal in the case of failing industries" (OECD 2004, p. 3). Such a conflict also seems to be felt in China: this is the interpretation of Xue Zheng Wang, state administration for industry and commerce (ibid., p. 3).

A special case is that described by Taiwan: "In 1978, in order to provide more employment opportunities for veterans, the Government set up the Liquefied Petroleum Gas Supply Division (the LPGSD) under the Veterans Affairs Commission (the VAC), and requested the CPC [Chinese Petroleum Corporation] to designate the LPGSD as its sole dealer of LPG [Liquefied Petroleum Gas]" (OECD 2004, p. 2).

Social policies are typically viewed as an integral part of a competitive market economy (although each country chooses a different comprehensiveness and depth of social objectives). Social policy does not have to be in conflict with any of the provisions of a competition law. A common misperception is that the effects of competition law are responsible for social costs that emanate from reform policies targeted at establishing a coherent economic system which enables the country to fully reap its potentials of economic development. In this respect, the representatives of Argentina to the WTO stated that "there is a danger of attributing to competition policy social costs that are really the result of more systemic changes relating to a movement away from pervasive regulation and state ownership" (WTO 1998a, p. 15). This can even be said about the effect of competition law of forcing uncompetitive companies out of business. This rather reflects the dismantling of structures that inefficiently bind scarce resources, which could be allocated to new, more efficient, use, and could afterwards produce more for the benefit of society as a whole. This is the essential truth best described by Schumpeter's intuitive concept of 'creative destruction'. Any industrial policy that attempts to support uncompetitive firms is misguided. Increasing unemployment due to the exit of inefficient firms can only lead to unemployment (i.e. resources remaining idle after having been freed from an inefficient use), if the labour market is dysfunctional, e.g. due to rigidities in prices or the relocation of factors (amongst which insufficient locational flexibility of labour is the most prominent).

Nonetheless, the introduction and enforcement of competition law incurs costs and might, therefore, rightly not be seen as a priority in developing countries with limited resources. Here, the developed world does offer technical and financial assistance, as it is in its own interest to promote the enactment of competition laws in countries it trades with. Moreover, this form of assistance could be regarded as very effective development aid. The claim, however, that a developing country typically has more pressing (social) problems and needs than the enactment and enforcement of competition law, is shortsighted. In the vast majority of such cases of social problems, a competitive business environment would be the most appropriate and lasting remedy. The solution followed by Taiwan, namely burdening the most successful industry with the social need to take care of veterans, cannot convince, as this industry will subsequently have a competitive disadvantage compared to foreign suppliers. The playing field becomes tilted against the national industry. In case of South Africa, social policy was more coherently included into the latest amendment of its competition law. The "Government, for its part, was an enthusiastic proponent of competition law although it, too, was careful to insert broader social goals (for example, employment creation and Black economic empowerment) into the objectives of the Competition Act" (OECD 2004, p. 3).

4.3.4 Environmental protection

Damages to the environment caused by economic activity are typically not visible to companies as costs. As long as such damages cannot be properly internalised, the political objective of environmental protection has to be pursued by some form of intervention into the market. Therefore, a policy, like that applied by Romania, which allows state aid if it serves environmental protection (OECD 2003, p. 4), need not to be at variance with competition law.

From an economic point of view, the fact that environmental damage does not show up as a direct cost, is a market failure. Hence, government intervention, for example via state aid to eliminate or prevent the damage is not efficiency-compromising or welfare-reducing, provided the benefits companies receive from the intervention correspond to the real costs of the prevention or removal of the environmental damage. Only where the political objective to provide *additional* support for companies who are willing and active in preserving the environment tilts the level playing field, would efficiency-defined welfare be compromised.

4.3.5 Systemic reform and economic transition

A country faces a particularly difficult situation during systemic reform from a socialist planned economy to a market-governed system. A complete overhaul of all institutions, mechanisms, and even norms and values of society is happening at the same time. A stable monetary constitution, including institutions like the central bank and contestable commercial banks and a convertible currency have to be created. The state has to retire from controlling the economy, formally state-owned companies have to be privatised, and new companies, as well as the workforce, have to learn to act in free markets where liberalised prices govern demand and supply. Typically, this transition takes some time and is accompanied by several years of severe economic recession. The formally state-owned companies have insufficient experience to operate within a competitive environment. Productivity and technology and hence fixed capital is largely obsolete due to the previously practiced autarky from world markets during the socialist era. Competitiveness mostly relies on low wages. Investment is constrained by above-average interest rates due to risks premiums and monetary stabilisation policies.

Countries facing these transition-related difficulties are easily tempted to feel that enacting and enforcing competition law in those circumstances is a mistake, and that the effects of the competition laws might aggravate the transition recession. As a case on point, the Polish parliamentary debate in 1999 on the reform of the national competition law evolved around the worry that the resulting discontinuation of state aid to domestic companies would aggravate transitional recession. MP Kraus stated in the Polish Sejm: "At the current level of economic and social development of Poland we are facing a problem: not how to restrain, but how to increase state aid" (Cylwik 2005, p. 19).[22]

However, in light of what systemic reforms have to deliver, i.e. competitiveness of domestic firms, the call for state-aid appears to be rather odd: to make formally state-owned companies fit in terms of competitiveness, transition economies would do best if they introduced competition at home so that domestic firms quickly learn to adapt. In terms of gradualism, the infant-industry claim (see chapter 4.1.2) may provide a rationale to grant the newly exposed companies some time to adjust to become competitive, but this concept strictly refers to newly emerging or newly exposed firms and this is obviously not the case when introducing a competitive environment in the domestic economy amongst domestic enterprises. Where the call for state-aid refers to competition against foreign companies (e.g. in the form of imports or foreign investors), the issue of granting domestic firms a competitive head-start against foreign firms does not impinge upon the issue of introducing competition between domestic firms in domestic markets. Even then, state-aid is not an optimal policy, as it is typically granted to a selection of domestic firms and hence introduces distortions which in turn reduce efficiency and eventually competitiveness of domestic firms vis-à-vis their foreign competitors.[23]

In sum, transformational recession does not contradict the enactment of national competition law. Rather, competition law can serve as the most effective tool to help the economy to overcome the structural weaknesses it inherited from the past and to learn how to prevail in a competitive environment.

4.4 Competition law building

Overcoming the arguments against introduction of competition laws may be a daunting task for any developing or transition country. However, once a decision in principle has

22 Interestingly, this statement was made despite the fact that the country was required to enact a competition law in the framework of accession negotiations.

23 In this respect, a neutral policy would have to treat all domestic firms equally, as e.g. an undervalued exchange rate would do.

been taken in favour of the development of competition supervision, the real challenges are only beginning. Three separate issues have to be resolved. First, suitable competition laws have to be drafted and adopted. Second, a supervisory authority with adequate powers and resources has to be created. Third, the laws have to be applied and enforced in an effective manner, gradually building legitimacy for the laws and the bodies applying them, i.e. a culture of competition.

4.4.1 Preparation and adoption of suitable competition laws

Overcoming resistance

Before a country invests serious resources into preparation and adoption of competition laws, its government, its citizens and its businesses have to embrace the idea that competition is a virtue for society and that the enactment of competition law will promote general welfare. Many transition and developing countries report that the lack of a competition culture makes the enactment of competition laws very difficult or even impossible (for Cameroon: OECD 2004, p. 3, for Albania: ibid., p. 2). Initial conditions may speak against the introduction of competition law: "The initial conditions include substantial resistance to market-oriented reform manifest in competition-suppressing policies at all levels of government, fragile political support for competition agencies, little indigenous expertise in competition law or industrial organisation economics, courts ill suited to adjudicate antitrust disputes, frail transparency safeguards and consequential vulnerability to corruption, and resource and data shortages" (Kovacic 2002, as found in OECD 2002).

"Most people and most businesses want their suppliers and their customers and sometimes their competitors to be subject to the stringent application of competition law. This is for their own benefit. However, when the law is applied to themselves they do not welcome it. It is usually harmful to their interests, and they put these ahead of any acceptance that there may be public interest considerations. And in any case they often fail to see the public interest considerations that may be involved in cases affecting their own immediate interests." And: "This inevitably leads to strong pressures against competition law. The losers from competition are most often a powerful lobby while the winners are a weak one." And: "...the size of the property rights involved in competition law is very large and this exacerbates the tensions. In just about every country there is quite strong opposition by business lobbies to the vigorous application of competition law. They seek its watering down, they may support its general application but seek special exemptions and special deals, and since the amounts of money involved can be very large they press vigorously to weaken competition law. This is one of the reasons why the question of competition advocacy must be addressed in discussions about competition law" (Allan Fels, AO, Dean, Australia and New Zealand School of Government: APEC 2005).

Consequently, the competition council of Romania stated that “mentalities” and the “attitude” of the population at large is the “main challenge” to the enactment of competition law (Theodor Valentin Purcárea, President of the Competition Council of Romania: OECD 2004, p. 3), and the Zambian representative of the national competition authority concluded that “in developing countries, promoting compliance to the competition law is still unattainable task because business is generally reluctant to comply with it, governments ignore it and in some cases do not want to know what it is and the public at large do not understand what it is all about” (G. K. Lipimile: OECD 2002).

Theoretically, a developing or transition country could decide to wait until a sufficiently strong competition culture has developed and the introduction of competition laws is supported by a majority of the population or at least by the most powerful stakeholders. However, such a strategy could take a long time and competition advocacy may be difficult in the absence of supervised and therefore fair and efficient competition. During all this time, competition would be sub-optimal, and economic efficiencies, i.e. welfare gains, would remain unclaimed.

Proper appreciation of the virtues of competition law requires considerable sophistication as well as the prioritization of the general good over personal interests. This makes competition law particularly unsuitable for a bottom-up approach, where the government essentially waits until legislative and administrative action is demanded by the public. On the contrary, competition law is an area that requires strong leadership, including the willingness to take unpopular decisions that do not reap tangible benefits in the short term.

At the same time, a government does not have to commit political suicide in order to get competition laws enacted against powerful vested interests. There are ways and means of deflecting forceful opposition and of broadening support. First, a government could seek the endorsement of independent experts. Academics, think-tanks, and independent consultants are examples of domestic experts that could be called upon to support the introduction and explain the benefits of competition laws. International organisations, such as the OECD or sub-structures of the UN, as well as international consultants, could render support from outside the country.

Second, the government could isolate the strongest opponents by publicly explaining why these entities oppose the enactment of competition laws and how they are pursuing particular interest to the detriment of the common good. Along the same lines, a government may have to address proposals for alternative measures that supposedly provide similar benefits at lower cost (see above, Chapter 4.2) and explain – with the help of neutral experts – how these alternatives fail to accomplish similar welfare gains and/or serve particular interests over the common good. Another argument against (some of the) potential alternatives may be their incompatibility with obligations accepted by the country in the context of WTO accession, in particular the national treatment requirement under Article III of the GATT 1947.

Third, the government could pursue a carrot-and-stick approach. On the domestic level, powerful opponents could be bought out by offers of short-term financial compensation. Although sub-optimal, such measures are less damaging than the continued absence of effective competition supervision. By contrast, permanent exceptions in the competition law for these opposing forces need to be avoided, if possible. On the international level, the government could seek financial aid from Western donor countries and organisations and use this aid as a sales argument on the domestic level. Finally, if all else fails, the government could put the blame on the IMF and/or the World Bank and declare in the domestic arena that it has little choice but to implement the competition laws. Obviously, the latter strategy is not helpful for the development of a competition culture.

The drafting procedure

There are many ways of going about the actual drafting of competition laws. Some countries have relied heavily on foreign models and/or international assistance in the development of their laws (for a broader discussion of these issues, see Sunshine 2000, pp. 61-93). The Central and Eastern European candidates for EU membership are a case on point. They were strongly encouraged – to say the least – to adopt more or less identical laws as they are applicable at the level of the EU and/or in various of its Western Member States (the process obviously continues with those CEECs that have not yet achieved member status, see for example Petrović and Štritof 2001, pp. 469-495). This was not necessarily the best approach that could have been taken, however. Where a country takes over foreign laws, suitable or not, it will be difficult to instil a feeling of ownership in the domestic interlocutors (administrators, attorneys, business leaders, judges, etc.). For the case of the CEECs, it was further argued that "the practice of merely translating EU laws or the laws of a Member State such as Germany is also inadequate in light of the fact that these Western competition rules have not been designed for and are ill-suited to deal with certain problems (privatization and the dissolution of State monopolies) that are distinct and typical for transition economies" (Emmert 2004, p. 668) Therefore, in particular where "privatization was less successful or has not happened yet and State aids to ailing monopolists [are] still […] rampant […], the CEECs will have no choice but to develop their own solutions and legal rules" (ibid., p. 668).

Other countries take more time and develop (competition) laws that are distinct and different from those applicable elsewhere. Although such an approach may seem preferable, it has its drawbacks. First, the procedure may simply take too long, valuable time is lost, and welfare gains are delayed. Second, a thorough domestic debate may turn into the opening of Pandora's box, giving opportunity to all kinds of entities to insist on special language or exemptions in the law for their particular interests. Third, novel solutions may reflect a trial-and-error approach and may compromise the overall quality of the law and, hence, its acceptance by the public.

The question is, therefore, how a country can pursue an individual approach to the development of competition laws that reflects its sovereignty and its needs, while at the same time avoiding the drawbacks outlined above.

China, for example, took a long time to develop a draft version of an anti-monopoly law, despite broad support by international organisations and other countries. Questions that were discussed at length included the desirable scope of the anti-monopoly law (e.g. whether or not to include natural monopolies), the nature and definition of a monopoly, what constitutes an abuse of a dominant or monopoly position, how to deal with intellectual property rights, etc. (OECD 2001, pp. 5-8). In this process – as with other legislative projects – China sought and obtained input from various sources, without, however, simply translating or copying foreign models. Members of parliament and staff working for the legislative drafting service of the Chinese parliament met with academics and other experts from the United States and various European countries in a series of workshops to be informed about the strengths and weaknesses of their respective competition laws. The Western experts, in turn, were informed about the specific goals China was trying to pursue with its competition laws and were asked to give their opinions on these goals and the best ways of achieving them. On the basis of the workshops and expert opinions, a series of draft articles was prepared by parliamentary committees and services and circulated to domestic and foreign experts for comment. On the basis of the feedback, the drafts were more and more refined. Eventually, after several years of work, a highly sophisticated and broadly supported piece of legislation was submitted to the full parliament for adoption.

Obviously, not every piece of legislation needs and merits this kind of effort and not every country in the world will have Western donors competing with each other for the opportunity of accompanying the multi-annual procedure described above. However, the model as such seems to be interesting in particular for countries contemplating important legislative measures – such as a competition law – and seeking to integrate non-standard policies or considerations.[24]

Different laws for different countries: About quality, scope and exceptions

At the Second OECD Global Forum, the claim was raised that due to lack of experience, emerging economies frequently have difficulties with formulating adequate competition laws. The sheer complexity of the matter, questions about the scope of legislation, problems related to the multitude of stakeholders, and whether or not a country's specific needs could be considered, were given as examples (Mahmoud Mohielding, Professor in

24 Switzerland generally uses a similar system of open discussion with a multitude of experts and stakeholders, albeit on a more domestic level, prior to the adoption of important pieces of legislation. For details see *Gabriel* 1997, in particular pp. 110 et seq.

Economics and Senior Advisor to the Egyptian Minister of Foreign Trade: OECD 2002, pp. 2-6).

When it comes to the contents and language of the competition laws to be adopted, three issues have to be considered separately. First, the need for high general quality of legislation is often underestimated, although the quality directly impacts the acceptance of that legislation by the respective interlocutors and its successful application in practice.[25] Fortunately, there are not only many studies that provide guidelines how good legislation has to be structured and developed,[26] there are also various international organizations that provide technical assistance for drafting (Sunshine 1995, Sunshine 2000) and/or training programmes for legislative services and drafters.[27] Nevertheless, a number of countries have raised concerns. For example, Russia complained about the complicated application procedure, the long delay before a request was approved and assistance was actually forthcoming, the high level of bureaucracy involved, and the language barrier for technical assistance (OECD 2002, p. 7). This could be an indication for the IMF, Worldbank, OECD and other Western cooperation partners that law reform support offered from various sources may cause confusion on behalf of the potential recipients and that some form of best practice codes or benchmarking/accreditation procedures may be required.

Second, with respect to the general scope of suitable competition legislation, countries have expressed uncertainty whether, for example, network or natural monopolies should be given transitional periods before competition laws are applied to them, or whether they should be covered at all (ibid., p. 2). With respect to substantive coverage, collusion between otherwise independent enterprises (cartels), and abuse of dominant positions, are the two areas that are generally accepted. Even here, questions have been asked, for example whether the law itself should provide definitions for “dominance” and other technical questions. As has been discussed above, developing and transition countries frequently do not consider the adoption of merger control rules a priority (see above, Chapter 3.2.2 and Chapter 4.1.4).

In light of the fact that anti-competitive behaviour leads to economically sub-optimal results regardless of who engages in it or in which sector it takes place, we suggest that

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25 An example is provided by the Russian Ministry for Antimonopoly Policy, which considers the “lack of transparency” of its legislation to be a significant administrative barrier for business and concludes that overly complicated and inhomogeneous competition regulations may hamper international economic integration. See *OECD* 2002, p. 8.

26 The seminal work on the topic is still by *Dale* 1977. For more recent literature, see, for example, *de Wilde* 2000, pp. 293-319, *Kellermann* 1999, pp. 7-30, and *Popelier* 2000, pp. 321-342.

27 To give just one example, the Sir William Dale Center for Legislative Studies at the Institute of Advanced Legal Studies of London University provides courses in legislative drafting, a Jean Monnet Course on Legislating for EU Membership and Accession, and even an MA in Advanced Legislative Studies, see http://ials.sas.ac.uk/research/dale/cls.htm

competition legislation should be comprehensive, including, for example, rules on the conduct of natural monopolies. In particular in countries with large state sectors, it can be important to include rules on competitive public procurement. Proven examples of legislation, like the rules adopted by the EU, can serve as inspiration, at least as far as coverage is concerned.

On that basis, it seems clear that the size of a firm per se does not have to be bad, in particular where an enterprise has grown to a dominant size because of superior performance or because the market does not sustain a large number of competitors. In these cases, the emphasis has to be on prevention of abuse. The less a country wants to do about the size of enterprises, for example if it allows growth via mergers and/or does not provide powers for the breaking-up of large enterprises, the more it has to do to ensure effective prevention of abuse of market power. This will be addressed in more detail below, when we come to the structure and powers of the supervisory authorities.

Furthermore, somewhat more detailed explanations and definitions would seem to be useful for laws that have to be applied by administrative authorities and have to be supervised and enforced by courts with little or no experience in the matter.

However, there are indeed areas that may not need to be addressed in a competition law. "Unfair competition" may be one of those. If it is defined as predatory pricing and the like, i.e. a kind of domestic equivalent to antidumping law, it can be perfectly controlled in the context of abuse of dominant position. Smaller companies without market power should be of no concern here because aggressive pricing will be limited in time and scope and may indeed serve pro-competitive ends. If unfair competition is more broadly defined as "unfair trade practices", there is the problem with abuse of the competition procedures, i.e. with sluggish firms taking resort to competition law in order to harass aggressive competitors.[28] This last-mentioned concern contributed to resistance against the adoption of competition law in general, for example in Egypt (Mahmoud Mohielding, Professor in Economics and Senior Advisor to the Egyptian Minister of Foreign Trade: OECD 2002, p. 8).

Third, some countries raised concerns about the ideal design of competition law and whether national particularities could be taken into account (Kovacic 2002, pp, 301-302). Concerns especially question whether a western style competition law addresses the needs of developing and transition countries. Zambia noted the difficulties of drafting a model competition law for developing countries and rejected the idea of a 'one-size-fits-

28 It is probably fair to blame a considerable part of the sluggishness of the German economy on the German law against unfair trade practices (Gesetz gegen den unlauteren Wettbewerb, UWG). This law is regularly invoked by established firms and trade associations against aggressive market entrants trying out innovative forms of advertising or distribution. To give but one example, until the amendment of the law in 2004, special sales by retailers were restricted to seasonal sales and shop closing or renovation sales. Other than that, rebates and other discounts were illegal.

all' approach. "Competition laws of developing countries have often been modelled on those of developed countries, without being adapted to the special needs of emerging market economies" (OECD 2002, pp. 6, 8). The same concerns are raised by Cameroon (OECD 2004, p. 2). Malaysia added that further (country specific) research may need to be conducted, for example on M&A activities, restrictive business practices, suitable sectoral regulatory frameworks and exemptions, and also on the issue of acceptable market-share (OECD 2002, p. 2).

The integration of country specific features is a recurring theme discussed by developing and transition countries. It is based on the notion that there is no "one-size-fits-all" when it comes to legislation, including competition law. While this statement cannot be refuted, we suggest that it should be applied with care. The quoted statement by Malaysia illustrates why. Once the door is opened for national specificities, there is a very real risk that final result is a watered down law that does not provide effective supervision of competition and does not generate the expected welfare gains. Alternatively, further studies are merely used as an excuse for extensive or even indefinite delay of the laws.

National specificities can and should be taken into account when it comes to the integration of the competition rules into existing national legislation on procedural matters, legal remedies, and the like. They can also be listed as secondary goals to be taken into account, as it was done, for example, by South-Africa with respect to the achievement of broader ownership structures regardless of traditional racial boundaries. However, competition laws must not question basic economic facts in the guise of national specificities. Price fixing by cartels is welfare-reducing in Malaysia just the same as in Europe and the definition of dominance as the ability to act independently from market forces does not need to be re-invented for each and every country either. If a country genuinely believes that certain country specific parameters warrant a different approach in principle, it should bring in independent academics or consultants with a clear mandate for the scope of their studies and a narrow time line.

Compatibility with existing national laws and institutional structures

When introducing competition laws, various related national laws have to be adapted or created at the same time. If the structure of the supervisory authority is not dealt with in the competition law itself, it has to be regulated elsewhere. The same is true for the powers of this authority and the legal remedies against its decisions. In substantive law, there may be a need for amendments to a multitude of other laws. This requires a resource-intensive process (both in terms of finances, time and human capital) that can deter governments from even trying. The Competition Department of Albania stated that "As far as competition law is concerned [...], there are very complex relationships between competition policy and other economic policies, such as commercial policies, including tariffs, quotas, subsidies, antidumping actions, internal regulations, export restrictions, industrial policies, of regional development, industrial property, privatisation, scientific and technologic development, investments and taxes-relationships which [have to be] reflected in the respective legislation" (for Albania: OECD 2004, p. 2, for Malaysia: OECD 2002, p. 3, for China: OECD 2001, p. 7, and for Cameroon: OECD 2004, p. 3).

Allan Fels, Dean of the Australia and New Zealand School of Government, reported that "Some promarket minded persons oppose competition law because too much intervention is needed to achieve good market outcomes. […] Once the [competition] law has been enacted a plethora of activities must occur; the establishment of institutions such as regulatory institutions and courts; the undertaking of investigations; decision making in the light of investigations; judicial processes including appeals; educational activities and so on" (APEC 2005).

Pursuit of multiple objectives via competition law

Many developing or transition countries are concerned about competition laws as being too one-sided in favour of large enterprises and against social and other non-economic goals. The ugly face of Manchester capitalism, they claim, needs to be moderated by *also* stating other goals of society in the competition laws. Although this sounds good on paper, it rarely works in practice.

Korea made the experience that if competition policy follows multiple objectives, then the actions of the authority may become inconsistent and the policy may lose support of the public (OECD 2003, p. 3). In this context, the representative of the South African Competition Tribunal stated that "[t]he co-existence of industrial policy and competition law is tense and generally provides a playing field tilted against competition the more so in developing countries where the regard for competition is thin at best, where old producer lobbies remain active, where new entrants to the business world are pressing for protection and are usually extremely close to the new democratic governments, and where the imperative for redistribution in favour of selected interest groups is overwhelming. [...] I recall the palpable discomfort of the trade unions and many of the parliamentarians at supporting a pro-market piece of legislation, their consciences only assuaged by the notion that they were defending the market from their old class enemies. [...] By the same token I recall the palpable discomfort of the business lobbies, dominated by representatives of big business, at supporting a statute to which they would have to answer, their misgivings tempered only by the pro-market character of competition law" (ibid., p. 4). "The business sector, dominated by large, domestically-owned conglomerates and steeped in protectionism was intensely suspicious of the intentions underlying the introduction of robust competition enforcement" (OECD 2004, p. 3). Other examples were given by the Ivory Coast (OECD 2002, p. 6), Tanzania (OECD 2004, p. 3), and Zambia (OECD 2002, p. 7).

These concerns can be boiled down to the following broader issues: i) if other goals are included in competition laws, they may take precedence over the enforcement of fair and open competition; ii) other goals may be a floodgate for regulatory capture; iii) they may make the competition laws susceptible to abuse by anti-competitive forces against competitive firms (see more generally: Kovacic 2001 and Cuts 2003, p. 17, and Khemani and Dutz 1995).

Palatable versus enforceable laws

Some countries are experiencing the temptation to water down their competition laws in an attempt at reducing political opposition against their adoption. This can be done by way of entering competing goals, as discussed in the previous section. Alternatively, it can also be done by taking refuge into very general and unspecific language in the law. However, soft or elastic terms in competition law – as in any law that permits government intervention in the market and/or restrictions of individual (economic) freedoms – are problematic in several respects. Either the law becomes quite unsuitable to be applied and enforced in practice and remains largely dead letter. Insufficient or non-existent enforcement (possibilities) make the laws as such undesirable, see Khemani and Shyam and Dutz 1995, as found in OECD 2002. They are also a waste of resources, as stated by Cameroon (OECD 2004, p. 2). Alternatively, the law is hijacked by the administration – often at the request of vested interests (lobbying, corruption) – and used against certain firms, sectors, or activities, in unforeseen and unforeseeable ways.

The best precaution against either of these risks is to be very open about the goals of the respective legislation in the drafting phase and to be very clear and transparent about its application and enforcement in the law itself.

Shock therapy versus phasing-in

Another attempt at making competition laws more palatable is to grant grace periods to certain firms or sectors, i.e. to delay the full application of the law, or to provide for gradual phasing-in, for example with respect to penalties.[29] Taiwan claimed that it would not have been possible, politically speaking, to adopt the competition laws without such transitional periods (OECD 2002, p. 2). In Brazil, "a phased approach to the implementation of competition policy" (WTO 1998a, p. 17) was chosen for lack of financial resources and expertise.

Although such an approach may be sub-optimal from an economic perspective since it delays the enforcement of fair and open competition and, therefore, the generation of

29 Even the European Commission and the Court in Luxembourg have frequently avoided financial penalties in cases where a form of conduct was investigated and prohibited for the first time or where a previous approach was given up for stricter standards.

welfare gains, countries may have little choice. There are, however, better and worse ways of phasing-in competition laws. First, a transitional period should be used for transition, rather than for simple waiting. For example, the need for training of administrative staff, attorneys, and judges can justify a transitional period. Second, industry specific, let alone firm specific delays should be avoided, since they create an uneven playing field. Third, the duration of the transitional period(s) should be clearly stated and extensions should be avoided.

Costs of the preparation and adoption of suitable competition laws

One of the most widespread concerns in transition and developing countries is the lack of financial resources to cover the costs of developing a competition law, its implementation, enforcement, and the corollary measures to advocate its benefits and develop a competition culture (for Latvia: OECD 2002, p. 4, for Romania: Theodor Valentin Purcárea, President of the Competition Council of Romania, OECD 2004, p. 3, for Zambia: OECD 2002, p. 8, for Albania: OECD 2004, p. 2, for Thailand: OECD 2002, p. 4, for Brazil: WTO 1998a, p. 17, for Cameroon: OECD 2004, p. 3). The perceived lack of financial resources even led Egypt to question whether “the Egyptian legal system [is] ready and equipped for dealing with and enforcing a sophisticated law such as the competition law?” (Mahmoud Mohielding, Professor in Economics and Senior Advisor to the Egyptian Minister of Foreign Trade, OECD 2002, p. 12). In the case of Kenya, the cost-argument was raised against attempts to amend the competition law in order to make it more effective (ibid., p. 4).

In this respect, it is helpful to distinguish the costs of development of the law and the subsequent costs of its application and enforcement. The latter will be addressed below. However, with regard to the initial costs related to the drafting and adoption of competition laws, these are frequently overstated or inflated due to inefficient procedures. If a country wanted to avoid an elaborate procedure as it is applied in China or in Switzerland, it could simply hire a small group of academics or consultants and charge them with the first draft, including explanations or commentary. Furthermore, if a country is genuinely interested in building a competition culture, it should not be difficult to persuade the Worldbank, the IMF, the OECD or another donor organisation, to pick up the costs of drafting the basic legislation.

4.4.2 Creation of competition authorities with adequate powers and resources

Suitable and independent structures

Competition law without supervisory authorities is hardly worth the paper it is written on. Unfortunately, it is not easy to create a structure that is both effective and cost efficient (Serebrisky 2004)[30]. For example, in the case of the Ivory Coast, "[t]he Competition Commission, in the eyes of economic operators, is a body mandated by the government authorities to 'judge' and punish those among them guilty of breaches of the rules on free competition. Thus a company that is the victim of an anti-competitive practice would hesitate to complain to the Commission for fear of reprisals..." (OECD 2002, p. 6). In Korea the claim was raised, "[if the] competition authority pursues political goals, it may reduce consumer welfare because the authority can be captured by the interests of group with strong power" (OECD 2003, p. 3).

Experience, in particular in the Central and Eastern European transition countries, has taught us that newly created competition authorities need special support because they not only have to establish themselves and win the trust and collaboration of the private sector. They also have to fight for recognition from and cooperation with other, more established administrative units of government.

Similar to the central bank, a competition authority should be independent from any other governmental agency. In particular, it should not be part of the ministries dealing with finance, taxes, and/or the economy, since the competition authority may at times have to enforce decisions against these ministries, for example in state aid cases (see, for example, the statement made by the Chinese representative to the OECD 2004, p. 2). The German example quoted above also shows that any oversight by parliament, individual ministers, the cabinet, or even the president or prime minister is to be avoided, as it opens the door for political pressure and capture. By contrast, if the competition authority is subject only to the law, the constitution, and the oversight of the courts, it can be shielded from these pressures and act in genuine independence.

Human and financial resources

Personal independence of its leadership and personnel has to be part and parcel of the institutional independence of the competition authority. If the civil servants working for the competition authority could be transferred or even demoted at will, they would hardly be able to work against vested interests for the best of society at large. Therefore, they have to be adequately paid and their mandate has to be sufficiently long in order to allow them to act without fear or favour.

However, effective implementation of competition law requires more than just structural arrangements. A number of additional conditions have to be created both inside and outside of the competition authority itself. Besides the need for sufficient material re-

30 And *Emmert* 2004, p. 667: "Structural weaknesses of the institutions and their staff are frequently exacerbated by poorly drafted laws which are either home-made and reflect the drafter's lack of experience, or they are imported and basically just translations of EU or Western statutes."

sources[31], these conditions primarily circulate around the need of training, both as far as staff of the competition authority is concerned (for Cameroon: OECD 2004, p. 3, for Brazil: WTO 1998a, p. 17, for Jamaica 2003, p. 5, for China: Xue Zheng Wang (state administration for industry and commerce), OECD 2004, p. 3, for Malaysia: OECD 2002, p. 3, for Vietnam: OECD 2002, p. 3, for Kenya: OECD 2002, p. 4, for Tanzania: G. Mkocha, OECD 2004, p. 4, for Mexico: OECD 2004, p. 3, for Egypt: Mahmoud Mohielding, Professor in Economics and Senior Advisor to the Egyptian Minister of Foreign Trade, OECD 2002, p. 8, for Chile: APEC 2005, for Albania: OECD 2004, p. 2, and for Estonia: OECD 2002, p. 2, for Turkey: WTO 1998a, p. 18), and with respect to its interlocutors.

Within the competition authority, countries should seek to put together a team of highly motivated and educated lawyers and economists, working in teams and with a flat hierarchy. Experience in CEECs has shown that the training needs of this staff often far exceed the expectations, since the private sector is very keen to lure these kind of experts away with higher salary offers. This suggest a three-for-one rule, i.e. for every post that needs to be filled, at least three candidates have to be trained.[32] Furthermore, it can be beneficial to give to the competition authority certain powers to experiment with procedural rules, much like the concept of pilot courts suggests (for a detailed analysis, see Dakolias and Said 2000). Along the same lines, the competition authority should have the possibility of suggesting amendments to the law to parliament.

As far as other stakeholders are concerned, the net has to be cast rather wide to encompass not only members of the judiciary but also attorneys and in-house legal counsel in larger enterprises. Otherwise, "[i]f there is a cartel of silence among national lawyers, where legal counsel of both sides is either oblivious to the fact that EU competition law should be applied to the case at hand or where counsel feels it might be relevant but hopes – for lack of any specific knowledge – that the other side in the same position will not raise the issue either, we cannot expect effective application of the law" (Emmert 2004, p. 668). Thus, training should take place for civil servants, judges, prosecutors, attorneys, in-house counsel, and most importantly for university teachers in law, economics, business administration, and related subjects. Bar associations should include competition law in their continuing education programs and requirements and universities should be encouraged to make it a mandatory subject. Only by including the broadest number of parties in the educational efforts, will a genuine competition culture gradually emerge.

31 For example, the Chilean competition authority complained that it does not have the necessary resources (both economic and human resources) to carry out the necessary investigations, see *APEC*.

32 For a critical analysis of the training provided to civil servants in CEECs in the wake of EU accession, see *Emmert* 2004, p. 663: "All too often, the seminars (training seminars on EU law for civil servants, judges and prosecutors) have been offered in an unstructured manner or to an ever changing group of participants. And, most definitely, there was no systematic benchmarking and assessment of successful learning."

Relationships with other state authorities – avoiding inconsistencies and overlap

Pakistan raised the concern that “equally related with privatisation [is] the inherent conflict between sectoral regulators (SR) and CAs. The issue is the appropriate demarcation of jurisdiction between the two so as to eliminate instances of overlapping or conflict” (OECD 2004, p. 3, and for Cameroon: ibid., p. 3). The competition authority of Romania aims to “establish a real and constructive inter-institutional dialog” (Theodor Valentin Purcárea, President of the Competition Council of Romania, ibid., p. 3). The government of Vietnam stated that in connection with the drafting of the competition laws, it faces the difficult task to build an independent competition agency “in accordance with the trend of limiting the establishment of new bodies and the merging of ministries in the light of administrative reform” (OECD 2002, p. 4). The Albanian Competition Department takes an active approach in this respect and reports that “the new law purposely has been discussed with about 60 different institutions, directly or indirectly related with the competition issues” (OECD 2004, p. 2).

Besides creating an institutionalized dialogue between different ministries and authorities, countries should also consider some kind of inter-institutional dispute settlement mechanism.

Investigative powers and complaint procedures, due process

A very important concern about the application of competition law is connected to the investigative powers of the competition authority and the mechanisms available to it to receive (anonymous) complaints. On the one hand, the authority has to be able to launch investigations of its own motion and it must have the necessary resources to do so whenever it believes that anticompetitive behaviour may be at issue. On the other hand, the competition authority should be able to receive complaints from competitors, from whistleblowers within a firm that is engaged in anticompetitive behaviour, and from any other interested parties. To protect informants against sanctions, the competition authority should be able to receive anonymous complaints and to withhold the identity of an informant from targets of investigations.

In the case of transition countries the concern was raised that: “...dangers of misguided competition law enforcement [...] include subversion to protect existing patterns of wealth and privilege, discouragement of investment and entrepreneurship, and detraction from other more pressing needs” (Kovacic 2002 as found in OECD 2002, and Pittman 2004).

The example of the EU has shown that the competition authority needs far reaching investigative authorities, including the powers of search and seizure, before it can enforce competition laws effectively. But mechanisms against abuse of such far reaching powers also need to be put in place. First, the competition authority is subject to control by the courts and has to follow rules of due process and other procedural guidelines. Second, an independent ombudsman could be authorized to receive complaints about misconduct of competition staff.

Where sufficiently clear and detailed rules about due process are missing, they may need to be created as part of or in connection with the competition law.

Specific concerns about capture and corruption

In Egypt the resistance against a competition law resulted not only from the fear that the government could misuse the law, but also from a fear of a possible misuse by competitors. In that country "the issuance of a competition law, has been facing some resistance but this time is not coming from the state but from the private sector that has various concerns regarding this law such as: 1. Fear of government intervention in a new form under the notion of protection of competition. 2. Possible abuse of the law by particular firms that may use it, unjustifiably, to charge competitors with unfair trade practices. […] 5. Just implementation of the law may be confronted by corruption and profiteering" (Mahmoud Mohielding, Professor in Economics and Senior Advisor to the Egyptian Minister of Foreign Trade, OECD 2002, p. 8).

Good working conditions, above average salaries, clear procedural rules, the requirement to provide reasons for each decision that affects the rights of firms or individuals, and oversight by the courts, should normally keep the risk of undue influence on decision-making procedures at the competition authority under control.

Costs of the operation of effective competition authorities

In case of Chile, the government acknowledged that having monopolies involves costs to society. But it also wondered whether the cost of the monopolies could still be lower than the costs of implementing anti-monopolistic policies (APEC 2005). The South African Competition Tribunal stated that even "[t]hose who favour a robust competition policy sometimes suggest to us we should not be doing merger regulation at all, that our limited resources should be devoted to prosecuting anti-competitive restrictive practices" (OECD 2002, p. 3). Jamaica stated that in small economies there is often a mismatch between national implementation capabilities and the demands of new competition laws (OECD 2003, p. 5).

In this context, it must not be forgotten, however, that there is a revenue side to competition supervision, not only in the form of welfare gains based on economic efficiency but also in the form of fines from perpetrators. In principle, the revenue should be somewhat proportionate to the costs. A small country with few problems will not get much revenue from fines but will also not need a very large competition authority. By contrast, if there are many problems in a country, more resources need to be deployed to combat the anticompetitive behaviour but, in turn, this investment will also generate more income from fines.

4.4.3 Effective application and enforcement of competition laws

Getting it right the first time – building legitimacy via "good" decisions

When a country starts to apply competition laws, it lacks experience and there is a risk that at least some decisions come out the wrong way. "[R]epeated trial and error, caused by lack of relevant experience and know-how, may erode public and political consensus supporting competition policy" (Joseph Seon Hur, OECD 2002, p. 3).

There are ways and means, however, of reducing the risk of wrong decisions and improving the quality of the decisions for the sake of individual justice and overall legitimacy. First, it should be acknowledged that the relevant outcome is the final outcome of a supervisory procedure. If mistakes are made on the way, they may be correctable. For example, if the competition authority launches an investigation into potentially anti-competitive conduct of a number of firms, it should then confront these firms with its findings and a draft decision. Such a right to be heard before a final decision is adopted, already reduces the risk of major mistakes. Second, when a final decision is adopted, it should be supplemented with elaborate reasons, explaining exactly why and which factual basis the decision was taken. This gives the enterprise not only an explanation that may make the decision more acceptable but also a possibility to assess its chances of success in a legal challenge. Third, final decision could be subject to administrative review before the courts are involved. This can be a very useful instrument of self-control of the administration. Depending on the facts, suspensory effect may or may not have to be attached to such an administrative complaint but in any case, the decision in response should be taken by a higher level of authority within the competition authority, e.g. a review board that oversees the work of the actual case handlers. Fourth, adequately trained judges can provide a second level of review and catch any problems that have slipped through the system.

Final decisions on a case, internal review decisions, as well as all court decisions should be published on the internet and thus be available to others in similar situations. Adequate provisions for the protection of confidential business data have to be made, of course.

Another useful mechanism is the circulation of complaints, cases, and draft decisions – in an abbreviated form that takes account of confidentiality requirements – among concerned parties, such as suppliers, customers, and competitors of an investigated firm. The comments received will not only provide useful input for the decisions of the competition authority but will also contribute to the transparency and acceptance of the system overall.

Suitable enforcement powers and penalties

Another concern frequently raised by representatives of developing or transition country competition authorities relates to insufficient powers of sanctioning anticompetitive behaviour. In particular, the possibilities of fining the perpetrators are often too limited (see for example the statements made on behalf of Mexico, in OECD 2004, pp. 3-4).

Again, EU law can provide useful inspiration. A situation where fines are limited in absolute terms is bound to be inadequate for unexpectedly large cases. That is why in EU competition law, fines can be imposed up to 10% of the turnover of the enterprises in question. This is a sufficiently large range to serve as an effective deterrent and to make sure that the benefits of anticompetitive behaviour, once detected, will not outweigh the penalty.

Besides fines for the actual behaviour, the authority also needs to be able to impose periodic penalties against uncooperative enterprises, and it needs the power to issue cease and desist orders.

Checks and balances – political oversight and legal remedies

As a final point, it should be repeated that political oversight of competition authorities and supervisory procedures is undesirable. The process should be shielded from political considerations to the largest extent possible. The legality of investigative and punitive measures has to be secured via the courts, who will be even more independent than the competition authority and least subject to capture.

This, of course, does not cut the competition supervision entirely off from any political considerations. In case the government is not satisfied with the way the supervision is carried out, it still has the possibility of changing the respective laws. As long as the legislative procedures are sufficiently developed and require support from and independent and elected parliament, the risk that particular interests gain control of the process should be controlled.

4.4.4 Summary: Building a Competition Culture

As has been shown in the preceding chapter, many elements have to be brought together if a country wants to build a competitive and market-based system with a genuine competition culture. These elements will cost time and effort. However, the rewards are plentiful and broadly distributed in the form of better living standards for the large majority of the people. In any case, there are no real and realistic alternatives to competition law, if a country wants to develop and participate more fully in global trade.

5 Conclusions

The analysis indicates that in numerous countries the need to have a competition law has been realised. The rationales for the adoption of competition laws can be grouped in rationales from economic theory, and rationales derived by countries from experience in the economic and political sphere. The theoretical viewpoint that competition improves static and dynamic efficiency and the welfare of the consumers in the economy is one of the most obvious rationales for a competition law. In addition to that, an often mentioned rational is that competition law is needed in the process of privatisation, deregulation and liberalisation. For the latter, competition law is often seen as a remedy against anti-competitive practices by international mergers and cartels. Other economic reasons noted by particular countries are that a competition law could enhance the attractiveness to foreign direct investors, promote domestic enterprises in becoming international competitive, and could help to build-up a competition culture. In the political sphere the role of international organizations and regional agreements and competition law as a remedy against corruption are emphasised. A particular case is identified by South Africa. Within that country competition law is also used as a means to achieve social objectives, like the correction of a historically conditioned racial imbalance of ownership of resources.

However, there are also many claims raised why a national competition law might not be desirable or necessary. These claims include concerns that competition law could negatively affect the economic development of the countries, the argument that other policies could act as a substitute for competition law or have a higher priority, and questions how to develop and enforce a competition law in the given environment.

With reference to the claims that a competition law could compromise the economic development, the analysis indicates that this is not the case. A national competition law is rather an efficient tool that supports the economic development and economic development policies. This is the case, in particular, if the competition law emphasises dynamic rather than static efficiency. Furthermore, the analysis does not support the viewpoint that other policies could act as substitutes for competition law. Policies like a sectoral approach, trade liberalisation, and privatisation are rather complementary to a competition law than substitutes. With respect to competing priorities between several policies and a national competition law, the analysis suggests that those normally do not arise, if the policy measures and the competition law are well designed. A particular problem is that of limited resources. The claim is raised that developing and transition countries may not have the means to address social problems and to enact a competition law simultaneously. Therefore competition law is sometimes not conceived as a priority due to other pressing social needs. Such a viewpoint is short-sighted, however, because competition is welfare enhancing in the long term. Furthermore, the developed world does offer technical and financial assistance for countries which want to enact competition laws to overcome the existing limits in those countries, and in it is own interest to promote enactment of competition laws in countries it trades with. This form of assistance could be regarded as very effective development aid.

It is suggested that even in those cases in which the state wants to intervene actively to promote economic development competition law could be favourable. For example, a policy to build-up an internationally competitive industry through import substitution or promotion of national champions competing within the country and internationally, is supported by sensible competition rules.

Adoption of competition law is not the only bottleneck. Our research shows us that after adoption of a competition law, countries often fall short in its implementation. This suggests that even after the actual adoption of suitable laws, countries need a lot of support in the application and enforcement of their competition laws.

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