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**COMPETITION AND TRADE PRACTICE POLICIES:
AN OVERVIEW**

by

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WP 111

September 1996

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Competition and Trade Practice Policies: An Overview

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All developed market economies have some type of competition/trade practice policy. However, the specific nature of these policies varies widely. For example, cartels are illegal in most but not all countries. In some countries, mergers can be challenged by state authorities. And the abuse of market power is illegal in some nations, but not in others. The U.S. has the longest history of active intervention in marketplace competition through antitrust policy. However, some type of competition policies also exist in even the most laissez-faire nations. The relevant question is not whether to have antitrust/competition policies, but rather what to include in the statutes and how to enforce them.

Alternative Mechanisms for Social Control of Industries and Markets

There are several alternative approaches to the social control of markets and industries:

- Private enterprise in a laissez-faire environment, which minimizes government control over market structure or business behavior;
- Private enterprise regulated by antitrust/competition policies;

- Private enterprise with government cooperation and planning;
- Private enterprise with direct regulation of certain aspects of conduct and performance (public utility type regulation);
- Public ownership.

Most economies use a mixture of these approaches. National defense, police and fire protection, and highways are usually publicly owned. Monopolies such as local phone, electric and gas service have historically had direct regulation. The degree of state involvement increases progressively down this list of alternatives, as does the direct cost to taxpayers of the regulatory function; i.e., the antitrust/competition policy approach is considerably less intrusive and costly than public-utility type regulation or public ownership.

Recent experiences with deregulation and the privatization of state-owned industries in both centralized and market economies indicate that direct regulation and public ownership can result in massive inefficiencies. What is less clear is how much competition must be introduced for their performance to improve. Some Eastern European countries, in moving toward more market dependence, have found they have converted state monopolies to unregulated private monopolies, with a concomitant decline in performance. Changing from public ownership to private enterprise can involve several difficult transitions as competitive rivalry is gradually introduced through new entrants and foreign competitors, and as competition policies are implemented.

For example, Hungary was a centralized economy until 1990, and had no need for competition law. Now, Hungary's new Competition Agency is learning how to interpret

and enforce 1990 competition statutes. Privatization involved creating many dominant private companies that had previously been state enterprises. One Hungarian economist commented, "It's a good thing we have lots of foreign investments in Hungary to create some competition."

The last decade witnessed a shift in many countries from regulated and state-owned industries to industries more subject to market controls. However, in making this shift, people sometimes ignore a few simple but essential points:

- Market control can offer superior performance, but only if there is a reasonable degree of competition.
- Public utility regulation and market control are alternative control mechanisms. If industries are deregulated, antitrust policies become more important for maintaining effective competition. If a laissez-faire approach is pursued blindly so that competition declines, a more intrusive regulation may be called for.
- Deregulation often does not mean that competition policies should be weakened.

In many cases, the reverse is true. Willard Mueller has commented:

...the extent of government involvement in price and wage decisions is directly related to the *amount* of market power in the economy. We therefore have a choice: Enlarge the area of competitive markets, or enlarge the area of government involvement in business pricing decisions..

Competition Policies: An International Comparison

The last 15 years have seen a global trend toward economic liberalization, the opening of markets, and the encouragement of trade. As essential complements to this economic liberalization, it is not surprising that many nations strengthened their

competition laws. James Rill, former Assistant Attorney General for Antitrust, U. S. Department of Justice, commented in 1992:

In just the last five years, countries as diverse as Canada and Brazil, Italy and Czechoslovakia, and the Russian Republic and Kenya have enacted new antitrust laws and created agencies to enforce such laws....[T]he world now seems to have reached a consensus that sound competition law is a vital component of a free market economy....Over the last ten years, the competition laws and policies of many countries have converged in a manner that would have seemed remarkable in 1980. (pp. 270-273)

Ironically, the U.S. was an exception to this trend. Antitrust policy in the U.S. was generally weakened through a sharp decline in the enforcement activities of federal agencies, the appointment of many judges who were agnostic regarding the prevalence and impact of monopoly power, and the more widespread acceptance of the "Chicago School" of economic thought concerning competition policy.

Despite the convergence of competition policies, important differences remain reflecting substantial disagreements about the goals of antitrust. For instance, competition policies may be in conflict with trade and industrial policies, particularly in smaller nations.

The relationship between competition, trade, and industrial policies varies from country to country. Trade liberalization is often complementary to, but an inadequate substitute for, effective competition policy. Trade policies are more vulnerable to politicization and industry/labor pressure than competition policies. For example, the performance of the U.S. steel and auto industries deteriorated in the 1950s and 1960s in large measure because of a lack of effective competition. Penetration of the U.S. market by foreign competitors provided the competitive rivalry that antitrust policies had not preserved. Steel and auto industry performance improved sharply in response to this

competition. However, both industries were successful in persuading the federal government to institute trade restraints in the 1970s-80s that were costly to the American public. Voluntary import quotas on Japanese automobiles in the early eighties are estimated to have cost American consumers nearly \$16 billion in artificially inflated prices for new cars (Adams and Brock). Thus, trade liberalization can have clear competitive benefits but is vulnerable to protectionist tendencies.

Although there is a coalescing of competition policies internationally, there remain important differences in the exceptions allowed for trade purposes. Relatively small countries such as New Zealand and Canada are sensitive to international competitiveness issues since their economies are so dependent upon trade. This concern shows up in their competition policies. Canada's 1986 Competition Act, for example, states goals of expanding opportunities for Canadian participation in world markets and ensuring that small and medium-sized enterprises have an equitable opportunity to participate in the economy. The role of trade is also reflected in Canadian enforcement of the Competition Act. The Canadian Competition Tribunal, which has the responsibility for issuing remedial orders for antitrust violations, can use sector-specific trade liberalization measures as alternatives to remedies such as asset divestiture.

Whereas U.S. antitrust policy plays a minor role in trade and international competitiveness, this is not so with some countries. In general, smaller countries that are not part of trading blocks have greater trouble balancing competition and trade policies.

The role of efficiency varies as much as international trade issues in the extent to which they are considered in competition policies. For example, certain types of cartels and

mergers are allowed on efficiency grounds in some countries. Mexican enforcement of its 1992 Federal Economic Competition Law is but one example. Mexico's Federal Competition Commission, in considering several mergers in 1994, found that high market shares were offset by efficiencies, which would be needed to compete with foreign firms, particularly as a result of NAFTA (Van Fleet). Although efficiency defenses are allowed less in the U.S. than in many countries, their usage has increased in the last 20 years.

The strongest competition policies are those of the U.S., Germany and the European Economic Community (EC). The German and American systems have served as models for competition policies for the rest of the world. In both countries, judicial decisions play a critical role in defining and enforcing antitrust law. Dependence on courts encourages clear interpretations of antitrust statutes: what market share constitutes monopolization; what behavior constitutes predation; what mergers will substantially lessen competition.

By contrast, in the UK, Spain, Sweden, and to a lesser degree Japan, reliance is put on a regulatory system in which the interpretation and enforcement of the law rests with an administrative/political system. Such systems are usually associated with competition policies that serve a variety of goals, allow greater political discretion, and usually result in weaker enforcement. For instance, although the language in Japan's Antimonopoly Act (1947) was modeled after the U.S. Sherman, Clayton and FTC Acts, enforcement by Japan's Fair Trade Commission was relatively unaggressive until the 1990s when a U.S.-Japan trade negotiation group successfully identified several impediments to trade (First).

Competition policies depend on the language of the relevant statutes and how they are interpreted and enforced. In addition, there is considerable variance in exemptions

allowed to a country's antitrust laws. In the U.S., exemptions are relatively rare, whereas in Japan, exemptions are widely used.

Competition laws are generally based on two concepts: market power and dominance. Market power includes shared as well as unilateral power, and depends in turn, on market share, concentration, entry barriers and product substitutes/differentiation. Dominance leads to unilateral market power and is particularly influenced by market share and entry barriers.

Competition policies may attempt to influence market behavior by focusing on the structure of markets, firm conduct, or on market performance. Structural policies such as merger laws are generally found only in large economies, the U.S. and Germany having the toughest. Small countries rarely exercise significant merger control because of the perception that large firms are better able to compete in global markets. From a global perspective, however, several countries have recently adopted stronger merger control policies.

The greatest commonality in the competition policies of countries is with regard to the regulation of conduct. For example, price fixing is now illegal in virtually every country.

Competition policies directed at performance exist in several countries, particularly aimed at abusive pricing by dominant firms. However, laws that permit the state to dictate prices or outputs are incompatible with the growing philosophy that markets do a better job of determining prices and output than governments (Boner and Krueger).

The impact of domestic competition policies on international competition is of

growing interest. The best example of international competition law is that of the EC, which is based on Articles 85 and 86 of the Treaty of Rome. Article 85 prohibits agreements and concerted practices between firms that affect trade between member nations. Article 86 prohibits the abuse of a dominant position by one or more concerns within the EC that affect trade among member nations. Competition law is enforced at two levels: each member country regulates commerce within its own borders and the European Commission regulates trade among the member countries. The EC example illustrates the growing interconnections between competition law, international trade and industrial development.

Periodic Fascination with Cooperation

Antitrust assumes firms naturally prefer to cooperate. This assumption leads to legal restrictions on cooperative behavior in order to encourage rivalry. However, periodically a resurgence of laissez-faire philosophy occurs reflecting confidence that *potential competition* will prevent the development of enduring monopoly power. These periods of *anti-antitrust* can increase interest in industrial policy, government-industry planning, industry consolidation and/or cartels. The 1920s-1930s was such a time period in Germany, Japan and the U.S. Government-sponsored cartels in Germany and Japan were developed as part of an "industrial rationalization" movement. Excessive competition was blamed for low prices and too much output during the depression years, and cartels were seen as a means of managing these problems.

A similar cartel and rationalization movement occurred in the U.S. culminating in

the National Industrial Recovery Act (NRA) of 1933. The NRA replaced competition with a system of government and business-directed cooperation, essentially suspending the antitrust laws to accommodate NRA codes. Fortunately for the U.S., the Supreme Court found the NRA unconstitutional. President Franklin D. Roosevelt gave impetus to a new antitrust movement and reliance on competition when he appointed Thurman Arnold head of the Department of Justice (DOJ) antitrust division and created the Temporary National Economic Commission (Mueller).

In Germany and Japan, cartels were perceived by the Allies as encouraging and supporting the war initiative. The peace treaties with both of these countries made cartels illegal (with some exceptions), and instituted competition policies modeled after those of the U.S.

Interest in government-industry planning (industrial policy) and a weakening of antitrust enforcement surfaced again in the U.S. during the 1980s under the Reagan and Bush administrations. However, this occurred when the superiority of market-driven economies over government-regulated or controlled economies was being acknowledged worldwide. Although there has been some weakening of U.S. antitrust policy, compared to competition policies in other countries the U.S. policies remain strong.

U.S. Antitrust Policies

U.S. antitrust statutes are somewhat stronger than those of most other countries. In addition, the U. S. allows relatively few exemptions to antitrust laws. The U.S. also has a complex three-legged enforcement mechanism that is less amenable to politicization than

those in other countries. In the U.S., antitrust laws are enforced by:

- The two federal agencies, the Department of Justice (DOJ) and Federal Trade Commission (FTC).
- The 50 state attorney generals who can enforce both federal and state antitrust laws.
- Private parties, who initiate the great majority of antitrust cases.

The triad of enforcement agents has meant that different federal administrations cannot easily turn enforcement on or off. During the Reagan years, for example, although enforcement activity of the DOJ and FTC dropped sharply, it was partly offset by increased state activities.

Relative to competition policies in other countries, U.S. policy has placed more emphasis on: merger restrictions; per se treatment of price fixing and market allocation conspiracies and cartels; private antitrust litigation; and market structure as a major determinant of competitive behavior. Historically, most other countries have judged price fixing and cartels with "the rule of reason" in which gains are weighed against losses; however, other countries are now moving toward per se rules. Other countries place more emphasis on conduct and performance criteria and less on structure than the U. S. Treble damage possibilities and liberal discovery laws make private antitrust lawsuits more widely used in the U.S.

While there remain significant differences in the competition policies of countries, including the impacts these policies have on their food industries, it is also clear that competition policies and probably industry-government linkages are becoming more

similar internationally. History shows that while the effect of U.S. antitrust policies on its food industry varies over time, this is due to variations in enforcement rather than the laws themselves, which have changed little since 1950.

Nature of U. S. Antitrust Laws

Sherman Act of 1890. The Sherman Act does not mention competition, yet its primary concern is the protection of the competitive process. Section 1 of the Act prohibits “every contract, combination in the form of a trust or otherwise, or conspiracy in restraint of trade.” The Supreme Court has concluded that certain restraints, particularly price fixing, are always unreasonable and hence should be considered *per se* illegal. Restraints not included in the *per se* category are judged by the rule of reason, whereby each restraint is examined within its industrial context.

Section 2 of the Sherman Act provides that “every person who shall monopolize, or attempt to monopolize, or combine or conspire...to monopolize any part of trade...shall be guilty of a felony.” There are different legal standards for “monopolization” and an “attempt to monopolize.”

Clayton Act of 1914. The Clayton Act proscribes specific trade practices thought to injure competition even though they fall short of attempts to monopolize. The Act seeks to reach business practices in their *incipiency* that might lead to adverse economic effects. Types of conduct covered by the Act are price discrimination (Section 2), exclusive dealing and tying contracts (Section 3), mergers (Section 7), and interlocking directorates (Section 8).

The most significant parts of the Act are Sections 2 and 7. The Robinson-Patman Act

of 1936 amended Section 2 of the Clayton Act. The current version of Section 2 prohibits discrimination in price "between different purchasers of commodities of like grade and quality...where the effect of such discrimination may be substantially to lessen competition or tend to create a monopoly in any line of commerce, or to injure, destroy, or prevent competition with any person who either grants or knowingly receives the benefit of such discrimination, or with customers of either of them."

The Celler-Kefauver Act of 1950 amended Section 7 of the Clayton Act. The current Section 7 provides that no person who is engaged in commerce (or in activities affecting commerce) may directly or indirectly acquire the stock or share capital or the assets of another who is also engaged in commerce when the effect of the acquisition "may be substantially to lessen competition, or to tend to create a monopoly." The underlying objective is to prevent merger-induced structural changes falling far short of actual monopoly. Many authorities believe that the amended Section 7 has been the most important antitrust statute in the period since 1950.

Federal Trade Commission Act of 1914. The FTC Act overlaps and extends the Sherman Act. The FTC Act gives federal sanction to the common law principle that business persons must not only compete but must do so within certain bounds of conduct. Section 5 of the FTC Act prohibits "unfair methods of competition." Congress intended the FTC, as a body of experts, to define this language by identifying which business practices are unfair. Today the FTC Act is generally recognized as covering all unfair practices including some covered by other statutes.

Federal Antitrust Enforcement in the Food System.

Tables 1 and 2 summarize DOJ and FTC cases in the food system from 1950 through 1984 (Marion). Table 1 gives the number of DOJ complaints, informations, and indictments, as well as the number of FTC complaints and consent orders by statutory provision for seven periods from 1950 through 1984. Table 2 reveals the distribution of cases by statute and major food industry for 1950 through 1984. Since one case may allege more than one violation, Table 1 shows that 901 cases charged 961 violations. Table 2 does not include food system cases which do not fit within the major industries listed.

The great bulk of all complaints involved conduct-related cases. Over a third (328) of the 961 challenges involved Section 2 of the Clayton Act; a quarter of them (249) involved Section 1 of the Sherman Act, and another quarter (254) involved Section 5 of the FTC Act. Although fewer in numbers, the structure-related cases under Clayton Act, Section 7 and Sherman Act, Section 2 represented a sizable enforcement effort, whether measured by resource commitment or probable effects on market structure.

The most notable aspect of the enforcement pattern portrayed in Table 1 is the downward trend in the number of complaints. Although the number of attorneys employed by the DOJ and the FTC rose between the early 1950s and the late 1970s, just over one-third as many complaints were issued in 1976–1980 as in 1950–1955. The number of cases brought during 1981–1984 declined sharply, especially those brought by the FTC. During 1983–1984, the FTC brought only thirteen antitrust cases in food, a historic low; it brought no cases on price discrimination, resale price maintenance, monopolization, or attempt to monopolize. The most consistent area of enforcement involved challenges of

Table 1. FTC and Department of Justice Antitrust Cases in the Food System, by Statute, 1950-1984

	Sherman Act												Actual Cases ^b
	Clayton Act				FTC Act		§1		§2				
	§2	§3	§7	§8	§5	Civil	Criminal	Civil	Criminal	Civil	Criminal		
1950-1955	48	1	3	2	51	19	32	10	9	175	158		
1956-1960	210	1	18	0	38	11	19	2	0	299	290		
1961-1965	47	0	11	0	39	14	21	5	5	142	130		
1966-1970	15	0	14	0	24	10	11	1	0	75	70		
1971-1975	7	1	16	2	72	33	26	3	0	160	152		
1976-1980	1	1	18	0	19	15	17	0	0	71	64		
1981-1984	0	0	7	0	11	12 ^c	9	0	0	39	37		
Total	328	4	87	4	254	114	135	21	14	961	901		

Source: Compiled from Commerce Clearing House *Trade Regulation Reporter* and *Blue Book*.

^aThis column, a horizontal sum of the columns to its left, gives the total number of times all statutory provisions shown have been alleged for the indicated time period. This column is to be contrasted with the column giving the total number of actual cases. The differences between the two columns stem from cases alleging more than one statutory violation.

^bThis column shows the total number of complaints, consent orders, and indictments. The totals given for the Clayton Act derive from Department of Justice cases and FTC complaints and consent orders. The Department of Justice often institutes both civil and criminal actions in the same facts. Hence two complaints may correspond to what is really one set of facts, particularly for Sherman Act section 1 cases.

^cThe Department of Justice issued four price-fixing complaints in 1984 involving Waldbaum, Inc. This was counted as one complaint.

**Table 2. FTC and Department of Justice Cases in the Food System,
by Leading Industry and Statute, 1950-1984.**

	Bakery Products	Beer and Liquor	Milk and Dairy Products	Fish and Seafood	Fruits and Vegetables	Tobacco and Tobacco Products	Total ^b
Clayton Act							
Section 2	3	4	18	32	111	10	178
Section 3	1	0	3	0	0	0	4
Section 7	8	16	11	1	3	3	42
Section 8	1	0	0	0	0	0	1
FTC Act							
Section 5	19	5	35	10	14	28	111
Sherman Act							
Section 1	42	42	43	15	18	17	177
Section 2	2	0	9	3	7	2	23
Total ^a	76 (79)	67 (67)	119 (104)	61 (57)	153 (145)	60 (59)	536 (511)

Source: compiled from Commerce Clearing House *Trade Regulation Reporter* and *Blue Book*.

^aIf a complaint or indictment challenged a firm on several statutory provisions, each provision has been entered separately. For this reason, a vertical summation of the cases for an industry may exceed the total number of cases in the industry; the actual number of cases in an industry is given in parenthesis.

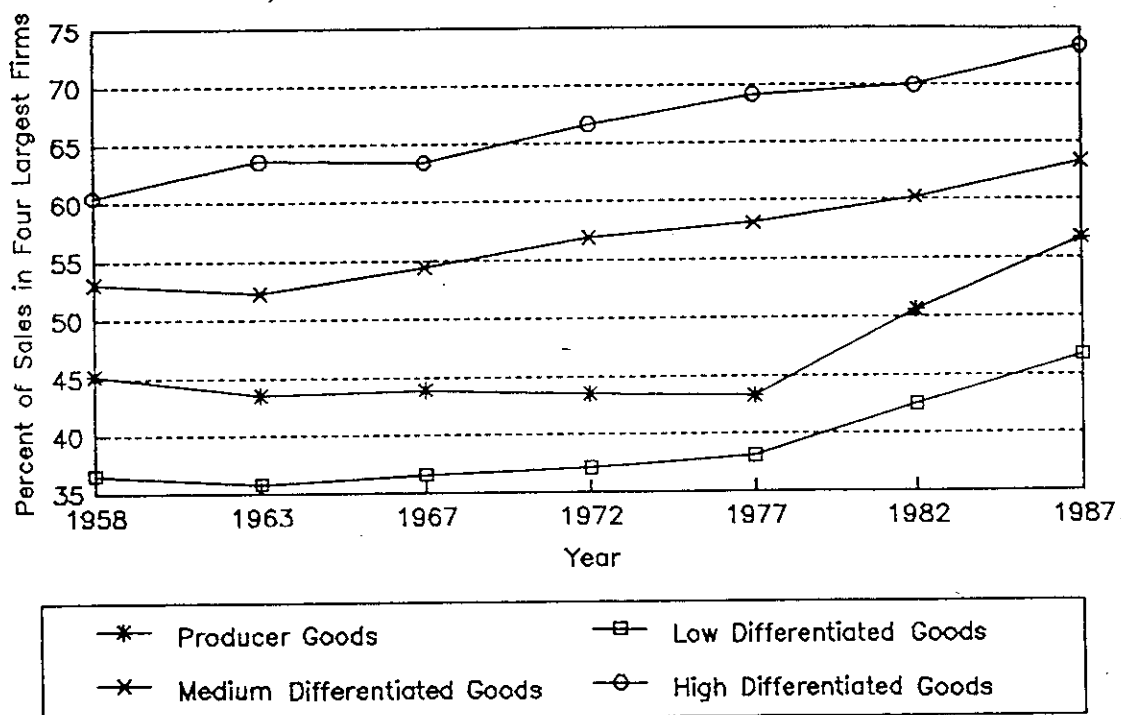
^bBecause other products are also involved, this column does not equal totals given in table 1.

mergers under Clayton Act Section 7, although activity in this area also was down sharply since 1980 despite a great increase in merger activity.

Effects of Enforcement Activities in the U.S. In recent decades a substantial percentage of the antitrust agencies' resources were devoted to food industries. What is the significance of this effort? Price-fixing and related restraints among competitors remain unlawful. These prohibitions appear to have been enforced effectively in the most conspiracy-prone food industries. Although one never knows how many conspiracies go undetected, the law is certainly effective in preventing the kinds of elaborate schemes required in cartels, as well as many less formal enduring price-fixing arrangements.

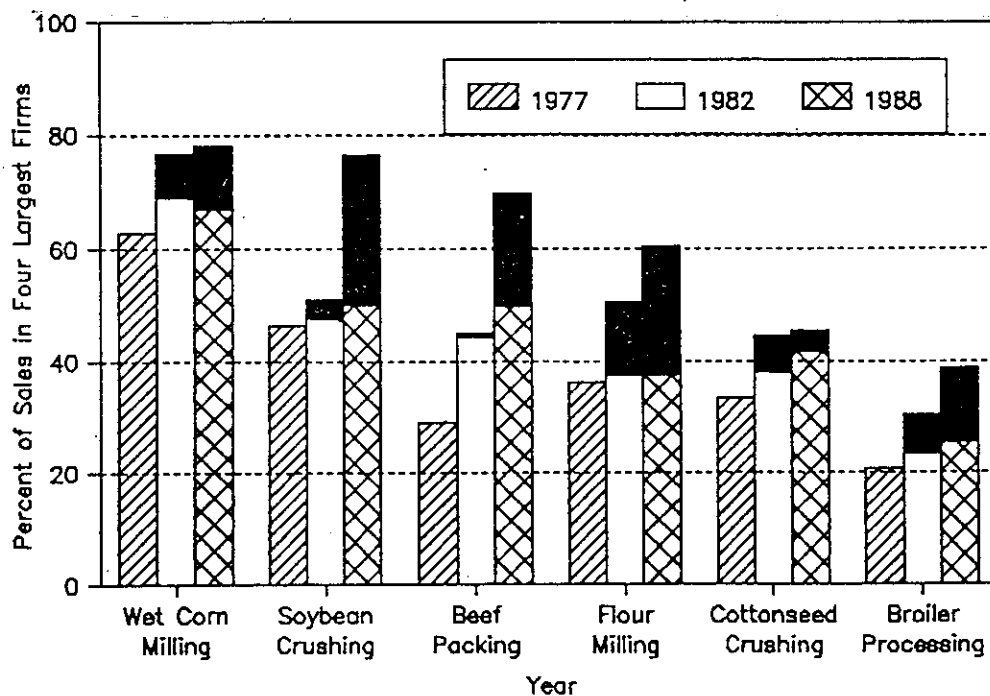
Historically, the antitrust agencies and U.S. courts have taken a dim view of horizontal mergers. This tough attitude has likely prevented many industries from becoming even more concentrated. This conclusion is suggested by the consequences of the 1980s when merger policy was greatly weakened. Figure 1 indicates the trends in four-firm concentration in 78 food manufacturing industries, classified by type of product (producer vs. consumer good) and by level of product differentiation. Producer-goods industries and consumer-goods industries with low differentiation had low and stable levels of concentration from 1958 to 1977. Their concentration then increased sharply in 1982 and 1987. Case studies of six industries exploring the cause of this sharp increase showed horizontal mergers accounted for two-thirds of the increase from 1977-1988, while internal growth accounted for the remaining one-third (Figure 2). Clearly, shifts in enforcement make a big difference and are responded to quickly by industry. Merger enforcement seems to have had less influence on concentration trends in medium and highly

FIGURE 1. CONCENTRATION TRENDS IN 78 U.S. FOOD MANUFACTURING INDUSTRIES, GROUPED BY DIFFERENTIATION OF PRODUCTS



Source: Rogers and Ma.

FIGURE 2. CONCENTRATION OF SALES IN SELECTED FOOD MANUFACTURING INDUSTRIES, 1977-1988



Note: Solid Fill Area Is Increase Due To Mergers.

Source: Marion and Kim.

differentiated food industries. Here, advertising-related product differentiation appears to be the major cause of increasing concentration.

An important conclusion from the trends in Figure 1 is that technology is not the primary determinant of industry concentration. The scale requirements of new technology are expected to affect firm size and industry concentration in producer goods industries as much or more as in consumer goods industries. Figure 1 indicates that in food manufacturing, producer good industries were stable and relatively low in concentration from 1958 to 1977. The sharp increase in 1982 and 1987 appears to mainly reflect changes in merger enforcement, not the dictates of technology. A similar trend is apparent in all manufacturing for the years 1947-1992.

The effectiveness of the price discrimination law (Clayton Section 2 as amended by the Robinson-Patman Act) is difficult to judge. Prohibitions against secondary-line price discrimination have been largely effective in eliminating most of the anticompetitive price discrimination arising because of the superior market power of large retail buyers, the main objective of the framers of the Robinson-Patman Act. The Act has been less effective in addressing primary line discrimination, conduct that falls short of the predatory behavior prohibited by Section 2 of the Sherman Act. This is partly due to the antitrust agencies' recent reluctance to enforce the Act because of their lack of sympathy for it.

In recent years, there have been several attempt-to-monopolize and monopolization cases brought under the Sherman Act, Section 2 and the FTC Act, Section 5. Defendants have almost invariably prevailed in these cases. The present law in this area is, at best, effective in preventing only the most egregious types of predatory conduct by single

dominant firms. Since relatively few food industries have such structures, the law does not have much application.

The greatest gap in existing U.S. antitrust law is the inability to deal with the possession and use of market power by oligopolists, especially differentiated oligopolists. Although innovative approaches have been proposed that would treat tightly-knit oligopolies as shared monopolies, this approach has been rejected to date. This immunizes those oligopolistic industries that can exercise monopoly power without explicit agreement and can maintain their power without illegal acts. It presents the greatest anomaly in the U.S. antitrust laws: loosely knit oligopolies that must conspire to achieve market power are proscribed by per se standards of the Sherman Act, Section 1, but tightly-knit oligopolies that can reach a monopoly result without conspiring are immune from antitrust prosecution under Section 2 of the Act.

Retail scanner data allow more precise analyses of market power than in the past. For example, a proposed approach that has particular relevance to merger enforcement is brand-level analysis of pricing power. This approach directly attacks market power that is based on advertising, market segmentation, and other nonprice strategies. Cotterill describes the application to merger enforcement:

...[M]ergers that increase market shares even a small amount can elevate price in an industry without tacit or explicit collusion....Essentially if the merger is between two brands that compete with each other (high cross price elasticities) then the merger internalizes and eliminates the price depressing effect of this competition. Each brand's demand is more inelastic after the merger. Not only are the prices of the merged brands higher, a ripple effect leads other nearby brands to elevate prices.

Brand-level demand analysis supplements rather than replaces traditional structural analysis of market power. As a firm expands the number of brands in its portfolio, it likely

also expands market share and internalizes cross-price effects for brands of products like cereals. This results in price levels increasing as market share increases. There is growing evidence that in food manufacturing, unilateral power based upon advertising, market segmentation, and product proliferation may be more important than tacit or explicit collusion (Cotterill; Sutton).

What Have We Learned About Markets, Competition and the Role of Government?

Economists and policymakers with interests in the performance of markets have often thought there are performance trade-offs in comparing an atomistic market of small firms to a concentrated market of large firms. For example, Schumpeter saw some degree of market power as facilitating firm innovations. His "creative destruction," the process of dynamic competition, was a major counterbalance to the market power that allowed some degree of monopoly rents. Lester Thurow, Malcolm Baldrige and others have argued that the international competitiveness of U.S. companies could be enhanced by relaxing our antitrust laws and encouraging industry consolidations, thus making them more effective in global competition, even though they might dominate domestic markets.

The evidence from many market "experiments" clearly indicates that a lack of competition negatively affects *most* dimensions of performance. The market "experiments" we have witnessed in the last 20-25 years include:

- The centralized economies of Eastern Europe have been converted to market economies with firms and resources privatized. We have observed what the enterprises in these countries have been forced to do in order to compete effectively with western

companies.

- Several industries have been deregulated in the U.S. (e.g., telephone, airlines, trucking) and elsewhere.
- State-run industries in market economies like the UK and Mexico have been converted to private companies.
- Some U.S. industries with highly concentrated oligopolies and lethargic performance have been exposed to competition from foreign competitors, either through imports or direct investment in the U.S., e.g., autos and steel.
- Evidence has been developed on the consequences of exclusive geographic territories in concentrated industries (e.g., mattresses, soft drinks), where *intra-brand* competition in domestic markets has been eliminated.
- The characteristics of successful firms and industries in global competition are better understood.
- There is more evidence on industry conduct and performance consequences when cartels are eliminated.

State-run firms, regulated public utilities, cartels, firms with exclusive geographic territories, and tight oligopolies or dominant firm industries all have one thing in common: a lack of tough competition. And there are similarities in the performance characteristics of these markets and firms: poor technical efficiency; bloated costs; high prices relative to costs; slowness in adopting new technology and developing new products; slow responsiveness to customer desires; and managers that are bureaucratic, unimaginative and risk averse.

In my opinion, the central finding coming from these experiments is that a lack of competition has broad impacts on firm and market performance. There are no redeeming market virtues from the quiet life. Perhaps this is simply the way human beings respond to an environment of pressure versus one of no pressure. For instance, in athletics, there is considerable research that indicates athletes show the most improvement when their competitors are strong. In universities, the most productive period of faculty is often prior to tenure. As individuals, we often grow the most during periods of great pain and suffering such as coming to terms with death, disease or divorce. And, people age more slowly if they are intellectually challenged.

Are people in their business roles any different? Is the "crucible of pain and pressure" important there also for good performance? The evidence from the above "experiments" supports Michael Porter's conclusions: industries that experience "tough competition" because of demanding customers and intense competitive rivalry in their home markets are more likely to be efficient, at the cutting edge in their products, and therefore to be able to compete well in global markets. Porter contends that tough antitrust policy enhances the global performance of a country's firms. Protecting one's firms from competition does the reverse.

A variety of things can influence the degree of pain and pressure on management. Leveraged buy-outs and "lean and mean" cost-cutting certainly create pressure and frequently improve efficiency temporarily. In the long run, however, the discipline of the market environment may be the most important determinant of tough versus soft competition. The degree of industry concentration and leading firm dominance, the level

of entry barriers, the degree of product differentiation, and international trade policies largely determine whether firms and managers experience “the quiet life” or the crucible of “pain and pressure.” The market environment represents a force external to firms and is not easily controlled. Competition policies that encourage highly competitive markets are likely to result in a higher level of performance in the long run than policies that encourage consolidation, protection from foreign competition and cooperative behavior.

This conclusion is more easily drawn for large countries like the U.S. and Germany than for small countries like New Zealand. In the latter case, achieving economies of scale so as to be able to compete in global markets may require relatively few firms in their domestic market. If trade barriers do not exist, however, foreign competitors are likely to be a constant threat to domestic firms and discourage the exercise of market power.

Economists tend to place a heavy emphasis on economic and technical efficiency and to assume that profit maximizing companies will continually strive to capture available efficiencies. However, I believe the last twenty years have indicated that effective competition is essential for achieving efficiency and technological progress, that inefficiency is widespread and substantial in the absence of competition, and that effective competition has far greater impact on performance than firm size. This conclusion will certainly not go unchallenged as economists continue to debate efficiency and market power trade-offs.

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