



## National Champions National Interests Vs. Competition: Where to Strike the Balance?

### FRAMING THE ISSUE

*“All public authorities must be, and increasingly are, concerned by the problem of cross-policy coherence, be it at the micro or macroeconomic level. Contradictions between policies can spill over and cause inefficiencies to each instrument, undermining their respective credibility and creating a climate of insecurity.”*

*Alexis Jacquemin, Chief Economic Advisor to  
the European Commission*

Policy coherence across public sector departments is an important determinant of their efficiency and ability to reach overall policy goals, and therefore, should be ensured by all means. Overlaps and conflicts would, however, seem inevitable. During the policy-making and enforcement process, extra efforts should be made to either attain coherence or provide remedies for any contradictions in different national policies. This, in many cases, has posed no small a problem to governments.

Competition law and policy, for example, has an extensive interface with other government policies, as the objectives of different policies can be complementary, or in conflict with competition. In areas, such as privatisation, international trade, investment and regional development policies, there are often conflicts with the objectives of competition policy. A case in point is the often-talked-about dichotomy between the objectives of competition policy and industrial policy, which has been a well-debated issue of economic governance. Their differing objectives often raise questions on the issue of priority given to competition policy *vis-à-vis* the industrial one.

Time and again, controversy has raised its head on account of various governments' conduct when it comes to choosing between simultaneous aims of ensuring full and free competition in the market and making a mark on the international stage by promoting “national champions” — companies strong enough to take on global competitors and act as national flag-bearers in the global market<sup>1</sup>. This question involves striking a balance between achieving competitiveness, progress and efficiency for the economy as a whole and preserving consumer welfare and the degree of competition in the segments concerned.

Different approaches have been adopted by countries worldwide with varying justifications. But the debate is still far from over and solutions still awaited.

### Industrial and Competition Policy Interface

Industrial policy, in broad sense, is defined as a generic issue, referring to a set of measures, aimed at promoting industrial development. In a rather narrow sense, and as termed in this paper, it is “the policy, which affects the economic welfare of a country by intervening in the allocation of resources between industries (or sectors), or in industrial organisation of specific industries (or sectors)”<sup>2</sup>. That is, industrial policy basically refers to the governments' support to specific industries, possibly through approving economic consolidation and intervening into industry structure, *i.e.* “picking winners”, and channeling market forces into working for particular interests of those “winners”. This unequal treatment to various economic actors is justified by the achievement of economies of scale and gaining efficiency. Thus, in the long run, it helps in the development of the economy as a whole, thereby, contributing to attaining national development goals. This latter end, in every case, is an executive decision and requires to be properly considered by policymakers and the enforcement agencies in the governance process.

However, the industrial lookout towards that end is not always compatible with the route mapped out under another policy instrument — competition policy.

By nature, competition policy refers to those measures that directly affect a firm's behaviour and structure of the industry.

“There is general consensus that the basic objective of competition policy is to protect and preserve competition as the most appropriate means of ensuring the efficient allocation of resources – and thus efficient market outcomes – in free market economies. While countries differ somewhat in defining efficient market outcomes (or, rich market returns), there is general agreement that the concept is manifested by lower consumer prices, higher quality products and better product choice”<sup>3</sup>.

Competition policy tends to be more universally applied within a country, to protect the general competition process and not particular “competitors”<sup>4</sup>. This means, unlike industrial policy, which seeks to gain economic efficiency *per se*, competition policy seeks to achieve that efficiency in a relative blend with fairness<sup>5</sup>.

Given the two policies' incompatible objectives as such, their interface problems—which the “national champion” argument is part of—will arise when industrial considerations are incorporated into the formulation and application of competition policy. Generally, industrial policy considerations with competition dimensions often arise in three situations:

- When governments opt for protecting and nurturing “infant” and/or “strategic” industries, or temporarily protecting sunset industries from foreign competition. This type of industrial policy often consolidates domestic firms, thereby, reducing domestic competition as well as preventing foreign firms from entering by acquiring the assets of local failing firms.

- When formulating competition policy, policymakers are under pressure to provide “flexibility” spaces for granting more favours to domestic actors through:
  - Special exceptions and exemptions for certain practices (e.g., export cartels, IPR-related agreements), enterprises (e.g., state-owned enterprises, services of professionals) and sectors (e.g., utilities); and
  - Immunity to certain cases based on the “national/public interest” criterion, despite the adverse effects they might have on competition.
- When strategically applying competition policy to complement industrial goals.

It is while dealing with mergers and acquisitions (M&As) falling within the “national interest” scope that the “national champion” policy is most relevant. The emergence of a “national champion” may be through internal growth; but most frequently, it is through M&As. Therefore, while promoting “national champions” may be in line with industrial policy, the process to acquire such dominance (through M&As) and the potential behaviour of those champions may well be subject to regulation of competition policy. And thus, the conflict between competition regulations and industrial policy objectives.

Advocates of “national champions” think that competition policy should not be too concerned with the emergence of dominant firms, or with mergers that will create firms with large shares of the domestic market, if largescale operation is essential to succeed in the world market. Their argument gives priority to industrial considerations, with such justifications as economies of scale, international competitiveness and the necessity of joining hands for joint R&D undertakings. In response, opponents point out that the promotion of these dominant firms may raise serious competition and consumer concerns, and therefore, should be eliminated for the sake of competition policy.

## Where do the National Champions Stand?

### *The US approach - Preference for “Pluralism”*

Initially, in the United States, the Justice Department, Federal Trade Commission (FTC) and the US courts have been insulated from statutory requirements and political pressures to pursue industrial policy considerations in the formulation and application of competition policy. The expressed focus of the US anti-trust legislation is to preserve a sufficiently unconcentrated market, so that companies are forced to compete and offer new or improved products at cost-reflective prices.

In evaluating changes in market concentration from M&As (which primarily fall under Section 7 of the Clayton Act 1914) towards the emergence of “national champions” *inter alia*, the US used to have the most stringent policy in the world, striking down even mergers among small firms in unconcentrated markets<sup>6</sup>. Nowadays, with the increasing competitive challenges posed by the globalisation process, the US merger analysis has become far more concerned about protection to a dominant domestic firm’s ability to compete “legitimately” and “competitively”. In the latest Merger Guidelines, the government agencies state that they will not challenge mergers with substantiated efficiencies, which are unlikely to be produced in the absence of the merger, if these efficiencies are sufficiently great to counteract any consumer harm. Also, the greater the probable adverse effect of the merger, the greater must be the efficiencies to nullify the effect<sup>7</sup>.

However, efficiency claims *per se* are still not recognised as an absolute defence to an otherwise unlawful merger. They rather constitute a factor that, in some circumstances, may be weighed in the determination of net competitive effects. To date, there has been no case where the efficiency defence in an M&A transaction has been accepted<sup>8</sup>. It has even been stated that competition has been the industrial policy of the US<sup>6</sup>. Most common exceptions to be cited are the treatment of export cartels, R&D consortiums and agricultural cooperatives.

Interestingly, it has also been observed that some large mergers have been smoothly approved by the US competition authorities (e.g., G.E-Honeywell and Boeing-McDonnell Douglas cases), though they might have led to high market concentration. Presumably, the US may be strategically promoting the concept of “national champions” without a declared intention. Besides, given the huge size of the US domestic market with a great consumption power, they may afford to have a number of domestic firms competing with each other, and at the same time, enjoying the advantage of size, as compared to firms from smaller economies. It can, thus, be assumed that the US can preserve their firms’ international competitiveness without promoting specific “national champions”.

### *Triumph of Japanese Industrial Goals over Competition Concerns*

Since the Meiji Restoration (1868), Japan has used industrial policies to catch up, and more recently, to compete with Europe and the US. After World War II, the US occupation government imposed an anti-trust law, modelled after the US law on Japan. Following the American withdrawal, however, the Japanese law was weakened and enforcement was subordinated to the needs of industrial policymakers. Within the bureaucracy, the Japanese government’s Ministry of International Trade and Industry (MITI) enjoyed higher status than the Japanese Fair Trade Commission (JFTC), and superior political influence. When conflicts emerged between MITI and JFTC objectives, competition policy was given the short-shrift to meet the needs of Japanese industrial policy.

The Japanese government takes a more pragmatic approach to anti-trust enforcement, one that makes allowances for national goals, such as, industrial catch-up. It takes into account other collective values and extenuating circumstances in weighing enforcement decisions against the letter and spirit of anti-trust laws. Included within are such considerations<sup>9</sup> as:

- economies of scale,
- enhanced efficiency,
- optimal use of scarce resources,
- international competitiveness,
- heightened productivity,
- business cycle stabilisation,
- industrial orderliness,
- price stabilisation, and
- economic security.

Believing that large-scale enterprises were required for promotion of technical change and for Japanese firms to compete effectively with their Western counterparts, MITI encouraged mergers between leading firms in key industries. In Japan, the pro-national champions industrial policy has, thus, always enjoyed favour over competition concerns.

### *The National Interest Criterion*

Besides the above two approaches, a more common one is the incorporation of the concept “national interest” or “public interest” and the likes, into competition legislation. This provides the space for “flexible” application of competition policy keeping in view the industrial policy objectives. This is the regulatory space that some nations provide for promoting their “national champions”.

In the UK, until the recent competition legislation reform, the pro-national champion argument, particularly in high-growth or hi-tech sectors, has been quite popular. In monopoly and merger cases, the relevant legislation in the UK is the Fair Trading Act (FTA) of 1973, under which the Monopolies and Mergers Commission (MMC) was asked to consider public-interest criterion in its exercise. The FTA’s definition of public interest was widely framed; therefore, the competition authorities could use their powers to promote the interests of a domestic firm against foreign competition by taking a relatively relaxed view of market dominance and mergers<sup>10</sup>.

Since 1979, the UK government has stressed that the primary consideration in deciding whether to refer mergers would be that of competition. However, there have been two cases, where enabling domestic firms to compete internationally has been closely relevant with the concept of breeding “national champions”.

The first is the 1987 report on the merger between British Airways and British Caledonian. The MMC recognised that the merger would create a “national champion” better equipped to compete internationally, but it also noted the adverse effects on competition with smaller UK airlines. The merger was allowed after British Airways entered into undertakings (subsequently strengthened after intervention by the European Commission) to cede some of its landing slots at London’s Gatwick Airport to the competitors.

The second example is that of the 1989 consortium bid of GEC and Siemens for Plessey. The MMC’s 1986 report on the proposed merger between GEC alone and Plessey had identified an adverse effect on competition in the domestic defence and telecommunications markets, and the merger was blocked. The 1989 report, however, placed conditions on a merger involving the same two companies, but did not seek to block it. The MMC noted that the market in question had become more international, and that GEC and Plessey were already involved in a joint venture in the telecommunications sector. The view was taken that competitive pressures from Japanese and US companies in the telecommunications market required larger UK units to compete<sup>10</sup>.

According to the UK “Merger References: Competition Commission Guidelines”, issued in June 2003, as required under the Enterprise Act 2002, the Secretary of State can “intervene into the consideration of a merger that she thinks might raise one or more public interest considerations. *Such considerations must be specified in statute* and the only one so far specified in the Act is ‘national security’, which includes public security”. The Act also provides for an *exceptional* category of mergers, which can be

referred to on public interest consideration grounds only. These are mergers involving a government contractor (past or present), who holds confidential material related to defence—so, triggering the consideration of national security—but does not meet the normal qualifying threshold relating to turnover or the share of supply. Where this type of merger (called, a special merger situation) is referred to, the question of whether the merger will result in a substantial lessening of competition is not an issue that can be considered.

In Germany, as illustrated in the utility case, specifically cited synergy advantages of mergers, industrial policy concerns and strategic considerations may enter merger control decisions in favour of “national champions” through the use of special exemptions granted by the German Ministry of Economics in particular cases (See Box 1).

In a similar approach, Section 96 of the Competition Act of Canada provides that an anti-competitive merger can pass smoothly if the parties can establish that the likely efficiency gains to result from the merger will be greater than, and will offset, the effects of any prevention or lessening of competition resulting from the merger<sup>11</sup>. This section was inserted into the Act in 1986 with high hopes that it would play a significant role in facilitating efficient restructuring in Canada. Since then, it has been also subject to lengthy disputes between the Canadian Commissioner for Competition and the competition courts in many cases.

Under the same philosophy, Australia’s Trade Practices Act provides the possibility of the Australian Competition and Consumer Commission (ACCC) granting immunity, on public interest grounds, for M&A cases, which would or might otherwise breach the provisions on “substantial lessening of competition”. This mechanism is called “authorisation”. Once authorisation is granted, no one can take action under the Act to overturn it. A wide range of matters have been considered to constitute a public interest, including:

### Box 1: The German Utility Case

In July 2002, when Germany’s Economics Ministry overruled a Federal Cartel Office (FCO) decision, rejecting E.ON AG’s proposed \$10.2-bn takeover of Ruhrgas AG, Europe’s largest gas importer, it heated up a national debate as well as re-ignited the international debate on “national champions”. The case has been evaluated as a prominent signal of strengthening industrial policy objectives into the application of competition policy, thus, having severe implications for the credibility of both regulatory authorities, destabilising consumers’ and market competitors’ confidence as well as eroding the role of competition policy in economic governance.

#### Veto to the Merger

The German FCO based its veto on competition grounds. Accordingly, the merger raised a multitude of competition policy questions, both for the electricity and gas sector. It would have major implications due to vertical integration: Ruhrgas’ gas import contracts and high-pressure pipelines were merged with the E.ON’s sizeable interests in regional and municipal gas distribution. This would strengthen E.ON’s already dominant position in gas and electricity distribution in Germany, in effect, reducing competition in these markets.

The new company might also have an incentive to discriminate against prospective competitors in the electricity generation and retail sectors by offering disadvantageous terms for gas transportation and supply. Besides, competitive implications of the merger did affect consumers. A lack of competition in the Germany energy sector might remove the incentive for E.ON-Ruhrgas to pass on benefits from the merger to consumers. Furthermore, a weakening of competitive pressures on E.ON-Ruhrgas after the merger might increase E.ON’s scope for price hikes.

**The German Monopolies Commission** also gave a negative evaluation of the merger’s competition implications *vs.* possible public interest argument.

Meanwhile, the **German Minister of Consumer Affairs** warned in June 2002 that the take-over would harm consumers’ interests. She exhorted the Ministry of Economics to impose conditions on the merger, which ensured that the merger was in the interest of German consumers and not only in the interest of E.ON.

#### The Ministererlaubnis

The **German Economics Ministry** approved the bid on the basis of the *Ministererlaubnis*, pursuant to which, the Minister may approve a merger that has been vetoed by the FCO, if the anticompetitive effects are outweighed by advantages to the entire economy or it is justified by a predominant public interest. Relevant considerations include economic efficiencies and other wider interests, such as national employment or *energy policies*, or *enhancement of international competitiveness*.

The Ministry argued that “it will help create a global player that will benefit the German economy” and secure Germany’s gas supply, 90 percent of which is from abroad; and imposed some conditions upon the merger, which fell short of minimum requirements to secure competition and consumer concerns, as evaluated by economists and analysts.

After some failed efforts to block the merger on proceedings grounds by opponents, E.ON now managed to get through. On assessment, some German scholars controversially termed the *Ministererlaubnis* as “keeping the back door open for industrial policy” and the Economics Ministry’s conduct as “short-sighted national interest”.

Sources: Enese L.D., *The E.ON-Ruhrgas Merger: The German government decides against competition*, National Economic Research Associates’ *Energy Regulation Brief*, 8/2002 <<http://www.nera.com>>; and CUTS, *ReguLetter*, No. 8 September 2002 and No. 10 March 2003.

- fostering business efficiency, especially where this results in improved international competitiveness;
- industrial rationalisation resulting in more efficient allocation of resources and in lower unit product costs;
- industrial harmony;
- growth in export markets; etc.

They all implicitly and explicitly refer to the introduction of industrial policy into competition policy, thus, in specific cases promoting the creation of “national champions”.

In the UK and the Netherlands, government intervention into the enforcement of competition policy in regulating mergers and acquisitions with regard to “national interests” is now limited to national security grounds at most. However, in industrialised countries, like Germany, Canada and Australia, the “national champion” argument still has considerable significance, though not least in the developing countries.

### Developing Countries’ Perspective

In developing countries the pro-national champion industrial policy has considerable force. The argument that less developed economies and small markets can, at best, sustain one or two firms in an industry capable of achieving scale of economies, undertaking research and development and securing world markets in competition with advanced trading partners and giant TNCs, as a stimulus for other sectors, has been used at times to give industrial policy precedence over competition policy, given the low level of development and the limited capital resources here.

The brewing industry in Latin America has recently witnessed a spate of consolidation despite their anti-competitive effects. On the 31<sup>st</sup> of January 2003, Companhia de Bebidas das Americas (AmBev), the world’s fifth-largest brewer and Brazil’s leading beverage company, and Quilmes Industrial (Quinsa) S.A., the largest brewer in Argentina, Bolivia, Paraguay and Uruguay, announced successful closing and completion of their merger. This move lays the foundation for a regional consolidation. That is, this “allows for the optimisation of operating processes, a stronger financial position for both companies and enhanced competitive position against other international competitors in the region”. Similarly, in many other Latin American countries, national markets are dominated by one or two brewers: Grupo Modelo and Femsa Cervez in Mexico; Polar in Venezuela; Bavaria in Columbia, Ecuador, and Central

American countries, and Backus in Peru, on the anticipation that such dominant firms will help compete efficiently with foreign brewers<sup>12</sup>.

Colombia’s competition law (Decree No. 2153,1992) provides exemptions for cases of R&D cooperatives, and exceptions to be made for mergers and acquisitions that may have overriding efficiency and other public interest benefits. Venezuela’s competition law also contains provisions for authorising exemptions but requires they benefit consumers or users, and be least restrictive of competition. Accordingly, Venezuela’s President and/or the Ministerial Council can, after hearing representations made by the Superintendent for the Defence of Free Competition, over-ride or authorise a particular business practice.

Another developing country, South Africa has also been trying to pursue these two aspirations concomitantly. The objective of the South African Competition Act takes into account a range of concerns that will not necessarily be consistent with each other in the actual evaluation of cases. The Act is aimed at promoting and maintaining competition in order to, *inter alia*, “promote efficiency, adaptability and development of the economy” and “expand opportunities for South African participation in world markets”. To an extent, the objectives reflect the differing pressures on policymakers and their prioritisation will depend on the development of precedents from cases<sup>13</sup>. In South Africa, the “national champion” argument, therefore, can be favoured on a case-to-case basis.

However, for developing countries, other factors contribute to their desire to create globally competitive entities. These include, trade liberalisation, perceived to be threatening their national policy space and largely favouring multinationals, and the proposed multilateral competition framework in the WTO<sup>14</sup>.

In India, two government departments—one responsible for competition and the other for WTO issues—were at odds on whether to provide for national treatment in the new competition law. Opponents pointed out that this would inhibit the Government’s desire to promote “national champions”<sup>14</sup>.

Other developing countries, such as Pakistan and Malaysia, are also resisting attempts to bring competition within the WTO ambit for the fear that it would limit their ability to base their economic development on the promotion of national champions and other industrial policy considerations<sup>14</sup>.

### Box 2: Consolidation of the New Zealand Dairy Industry

Another remarkable case of developing “national champions” was recently reported in New Zealand (NZ). The country’s two dominant dairy manufacturing companies, NZ Dairy Group and Kiwi Co-operative Dairies, have been supported by the dairy industry and facilitated by the NZ Government to merge with the international marketing group, the Dairy Board, to create the country’s biggest exporter, to be initially known as Global Dairy Company, but since renamed as Fonterra Co-operative Group Ltd. The merged entity, Fonterra, now controls 95 percent of NZ’s milk supplies, contributing 7 percent of NZ’s annual GDP and ranks as the world’s 14<sup>th</sup> largest dairy company. NZ Commerce Commission, an independent body that regulates business mergers, has rejected a similar proposal from the Dairy Group in 1999 despite claims about industry development benefits from a consolidated dairy industry as:

- benefits of the adoption by the industry as a whole of best practices from each co-operative;
- structure for funding industry & good research;
- benefits to NZ of having a large TNC based in this country;
- tangible benefits due to reduction of duplication in ancillary facilities, plant production flexibility and rationalisation, etc.

However, in the changed context, the merger transactions, seen by the industry as the best way of building on the gains already achieved and providing a financial platform to pursue offshore investment strategies, facilitated by the NZ Government by its *introduction of a legislation to exempt them from the business acquisition provisions* of the country’s Commerce Act, has successfully got approved, enhancing the international competitiveness of the dairy industry, one of dominant importance to NZ economy.

Source: Ministry of Agriculture and Forestry, New Zealand <<http://www.maf.govt.nz>>.

**Box 3: The Kodak-Fuji Case**

In May 1995, Kodak filed a ‘301 case’ with the US Government, complaining that Fuji in Japan was restricting Kodak’s access to the Japanese market for photographic films and paper.

The allegation by Kodak focused on Fuji’s exclusive distribution agreement with retail stores in Japan, maintenance of resale prices and Fuji’s practice to enforce those contracts. It is claimed that since *Fuji has a dominant position in Japan*, with a market share of 75 percent, it precludes Kodak from selling *via* the regular retail system in the country. This allows Fuji to *maintain high prices in Japan* and *block rivals from access to the distribution channels*, while dumping its products in foreign markets through *cross-subsidisation*. Kodak’s complaint emphasises the fact that Fuji’s business practices violated even the Japanese anti-trust law, and the Japanese Government tolerated this.

Since 1996, the US invoked various WTO procedures with respect to Japanese measures affecting consumer photographic films and paper. Finally, in March 1998, a WTO panel rejected the US claims against the Government of Japan.

*Source: CUTS, Trade, Competition & Multilateral Competition Policy, 2000, p.5-6*

**Striking the Balance**

The debate on “national champions” goes on. Rationale for the quoted practices, as already summed up earlier, has been mainly based on the “critical mass” argument that the emergence and evolution of industry-leading firms is necessary for achieving economies of scale, enhancing international competitiveness and promoting R&D capacities.

Meanwhile, many counter-arguments can also be cited. It has been pointed out that obstacles to export growth may face industry participants of all sizes. It is not apparent that, simply by entering into a collaborative arrangement, like a merger, a participant’s ability to compete internationally is enhanced. Size is often not necessary to enhance the ability to compete on world markets. It has been convincingly argued that, in many cases, domestic rivalry rather than national dominance is more likely to breed businesses that are internationally competitive. When firms merge with an aim—for instance, to enhance exports, there are chances that domestic prices may rise until they reach import parity (if the goods were previously priced below import parity) while exports are at a lower price. A dominant entity, or a “national champion”, may use its market power to increase domestic prices and so subsidise its export price. Ultimately, domestic consumer and industry may be forced to pay a higher price in order to underpin the champion’s export sales<sup>15</sup>.

Furthermore, while the positive effects of promoting “national champions” are strategic and need to be strongly justified, there is a high potential of consumer welfare and competition abuses. The most prominent tendency in the business world is to maximise benefits. Here, the “national champions” may possibly abuse their dominance or accrue economic rents at the expense of consumers and other industry participants. Distortions in one market may “ripple” out to other sectors of the economy, particularly for the production and sale of other goods’ relevant markets. Thus, it should be recognised that the exercise of insulating one particular business practice or firm from the general application of competition policy is likely to have other direct and indirect adverse impacts on the economic structure as a whole. Whether the costs of such policy instrument are outweighed by the benefits needs to be carefully assessed.

Mention can also be made of another counter-argument: a dominant firm may succeed in keeping imports out of its home market. For example, such a firm may control distribution mechanisms *via* a vertical integrated structure, or

it may be able to use its dominant position as a supplier to coerce independent distributors and/or retailers from buying competitive imports. While such activity tends to do greater harm to the consumers of the country, where the “champion” is based, it also distorts trade flows and is likely to be a source of friction between/among trading partners. The Kodak-Fuji case on the distribution system of photographic film and paper in Japan can be cited as an example in this regard (See Box 3).

However, historically and across nations, the “national champion” argument is justifiable. Given some competition and consumer concerns over times, this industrial argument still has its position in many regulatory systems.

Competition policy, as any other policy instrument, does not exist and evolve in a vacuum and interaction is something inevitable. The challenge is to strike the right balance, so that the pursuit of national development goals is not misused by special interest groups and wrong “winners” picked, proving detrimental to competition and consumer welfare.

**Special Implications for Developing Countries**

Nevertheless, in advanced countries, the essential focus of competition policy is promotion of allocative efficiency and reduced prices for consumers. Hence, they offer case-to-case treatment to “national champions”. However, for developing countries, the central objective must be the promotion of long-term productivity growth. Rationale for industrial priority considerations in competition policy is, therefore, more justified in the greater dynamic context of growth and development than the static one, pursued by advanced economies.

In developing countries, an optimal level of competition that fits well with the industrial policy may be needed rather than “excessive” competition. Giving the local concerns, breathing space to build industrial capacity and achieving commercial success in world markets is the way to apply the strategy in an apt manner. The experiences of industrial objectives preference in the newly industrialising economies of East Asia and in Japan (already stated above) can illustrate the dynamic benefits to be derived by helping domestic firms become more efficient and competitive, even “champions”. For example, the success of the Korean industrialisation programme relied on a big business-oriented growth strategy, together with regulations on entry and protection from foreign competition<sup>16</sup>.

**Box 4: Pros and Cons about “National Champions”**

**Pros...**

- Economies of scales
- International competitiveness
- R&D promotion
- Spillover effects to stimulate other industries and economic development of home country
- National security grounds
- Dynamic growth and development

**...and Cons**

- Possible abuse of dominance
- Anti-competitive precedents
- Reduction of competition in relevant markets
- Consumer interest concerns
- Possible distortions to FDI, trade flows and frictions among trading partners
- Possible misuse by special interest groups

In Korea, the government helped create the giant corporation, the *Chaebol*, which went on to capture the world markets. Korea was an industrially-backward country in the 1950s. Its per capita manufacturing output in 1955 was \$8 compared to \$7 in India and \$56 in Mexico. During the last four decades, Korea has managed to transform itself into an industrial and technologically sophisticated economy. It is the world's leading country in electronic memory chip (DRAM) technology. Until the Asian financial crisis, it was expected to become the fourth-largest producer of automobiles in the world by the year 2000<sup>16</sup>. However, Korean industrial production now has managed a resurgence, with rapid growth in semi-conductor and audio-visual communication equipment production. Exports climbed 22.3 percent on-year to \$15.8bn in June 2003, led by increases in automobile, wireless communication equipment, semi-conductor and ship exports.

Albeit as a result of the lax enforcement of competition policy, Korea has one of the highest levels of industrial concentration in the world, the giant Korean *chaebols* compete with each other fiercely and significantly for government support. It is provided in return for meeting specified export performance targets, new product development and technological change<sup>16</sup>. The "national champion" policy, in this case, has been strategically applied to bring maximum benefits for the country.

Besides, we also need to take into account the dramatically increasing pace of innovations in numerous industries today, which forces companies to expend unprecedented amounts on further developments. Such developments benefit consumers enormously, and therefore, should be encouraged. Yet, many firms in the developing countries find such investment beyond their reach, leading to a *de facto* surrender of emerging markets to large incumbent firms from the developed countries. Combining to become larger firms (national champions), with the backup of governments, can help them pool knowledge to better compete against large incumbents or consortia in other countries. It can also allow firms to eliminate duplication of efforts, thereby, increasing the resources available to conduct research or bring new products to market. In addition, synergies between unique skills and technologies can lead to the development of a better product than either company can produce independently.

Michael Porter, who has studied a large range of industries in a wide range of nations, has concluded: "When faced with trade-offs, we should weigh progressiveness higher than static efficiency or a

### Box 5: Recommended Guidelines

- Any special authorisations for cases of economy-wide dimensions (here, for "national champions") in the name of national/public interests, with potentially serious implications for other areas, need to be thoroughly justified in *public hearings*, accessible by *the public*, in particular, and sufficiently affected parties, such as consumer interest groups and other economic actors, with closely-related interests.
- The process for such authorisations or special immunities needs to be *rules-based*, democratically *accountable* and embrace clear and *concise administrative procedures*.
- Such authorisations should be *balanced by well-designed conditions and obligations* as remedies to ensure that the potential benefits of having a "national champion" can be passed on to the whole national economy and consumers as strategically expected, especially for utility sectors, which is essentially related to the common public's interests (e.g., imposing binding requirements for the unbundling of network activities, unbundling of contracts to create secondary markets, etc.).
- For securing the realisation of obligations and conditions by "national champions" in specific sectors, a sector-specific regulatory body should be set up with the power of *continuous regulatory oversight* and with regular consultations with competition and consumer authorities.

snapshot of price-cost margins, because innovativeness is by far the most important source of economic growth and welfare, greatly outweighing price-cost margins (allocative efficiency), or even static efficiency"<sup>17</sup>.

Still, the balance needs to be struck. Otherwise, such a policy may end up benefiting national laggards—former state monopolies in developing countries—instead of the real "national champions". Besides, the potential misuse of this particular policy could seriously harm competition and consumers in both developing and developed nations.

### To Conclude

The debate and public concerns on "national champions" has underlined the challenge for policymakers around the world to strike the right balance. The lack of coherence between industrial and competition policy objectives has not caused many major problems so far, but it will not be possible for both to continue to develop along diverging paths without some problems arising in the future. Particularly, in the context of an increasingly integrated world economy, a national decision may have considerable implications for neighbouring countries and can seriously penalise other economic segments. This will set bad precedents or erode confidence elsewhere. This problem, therefore, needs to be addressed soon, for which clearly the first-best solution would be to correct at source. That solution, however, may not be feasible due to different policy objectives and constraints and contexts that governments face, in particular, in developing countries. Some guidelines for fair and well-designed remedies, in this case, may be the optimal option (See Box 5).

### Endnotes

- 1 Pradeep S. Mehta, *National Interests vs. Competition – Need to strike the right balance*, Business Line, 2002
- 2 Itoh et al., *Kokusai Boeki (International Trade)*, Tokyo 1985, p.4 as quoted by Takako Ishihara, *Industrial Policy and Competition Policy*, Japan 2000, p.2
- 3 OECD/GD(94)64, *Interim Report on Convergence of Competition Policies*, 1994 at Annex, *Areas of Convergence in Competition Policy and Law*, Para. 4.
- 4 WTO, *Annual Report*, Geneva, 1997, p.44
- 5 Edward M. Graham and J. David Richardson, *Global Competition Policy*, Washington, DC: Institute for International Economics, 1997, Chapter I, p.8-9.
- 6 *Ibid.*, Chapter II, Part 7 written by Eleanor M. Fox and Robert Pitofsky, p. 249
- 7 *Ibid.*, p.251
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This Briefing Paper is written by Alice Pham of and for CUTS Centre for Competition, Investment & Economic Regulation, D-217, Bhaskar Marg, Bani Park, Jaipur 302 016, India. Ph: 91.141.220 7482, Fx: 91.141.220 7486, E-mail: c-cier@cuts.org, Web Site: www.cuts.org. Printed by Jaipur Printers Pvt. Ltd., M. I. Road, Jaipur 302 001, India.