Viewpoint

TRADE LIBERALISATION AND COMPETITION POLICY

#1/2007

This viewpoint paper is to help people understand the crucial nexus between liberalisation and regulation, as the two sides of a coin. It is accompanied by a flow chart to illustrate the issues in a lucid form.

The process of economic liberalisation started in several countries across the world during 1980s and 1990s. This was when most of the countries adopted policies of deregulation, privatisation and trade liberalisation. This was also the time when the World Trade Organisation (WTO) came into being. The WTO is a bundle of several agreements on goods and services, with various rules on how they are produced and traded, ensuring that there is healthy competition in the global market place. However, this is not enough, and therefore, at times, there was strong demand for competition rules to be integrated in the international trading system.

Trade and economic liberalisation aided competition in the market, by increasing the basket of goods and services with better quality and lower prices. Yet, anti-competitive practices undertaken by economic players or induced by inappropriate government policies have negated the gains of liberalisation. With the adoption of market oriented reforms, there were several players in the market resulting in competition. But at the same time, many abuses too creep into the system. In order to balance the system, price controls and market regulations were put in place. But by and large they proved ineffective. This is why countries adopted competition and economic regulatory laws to promote a healthy market and economic democracy.

The main objective of competition policy and law is to preserve and promote competition as a means of ensuring the efficient allocation of resources in an economy. This should eventually result in fair prices and adequate supplies for consumers and, it is hoped, faster growth and a more equitable distribution of income.

While going through a phase of privatisation and deregulation, often monopoly power is transferred from the public to the private sector which harms the interests of consumers, especially the poor. This situation requires an appropriate regulatory mechanism.

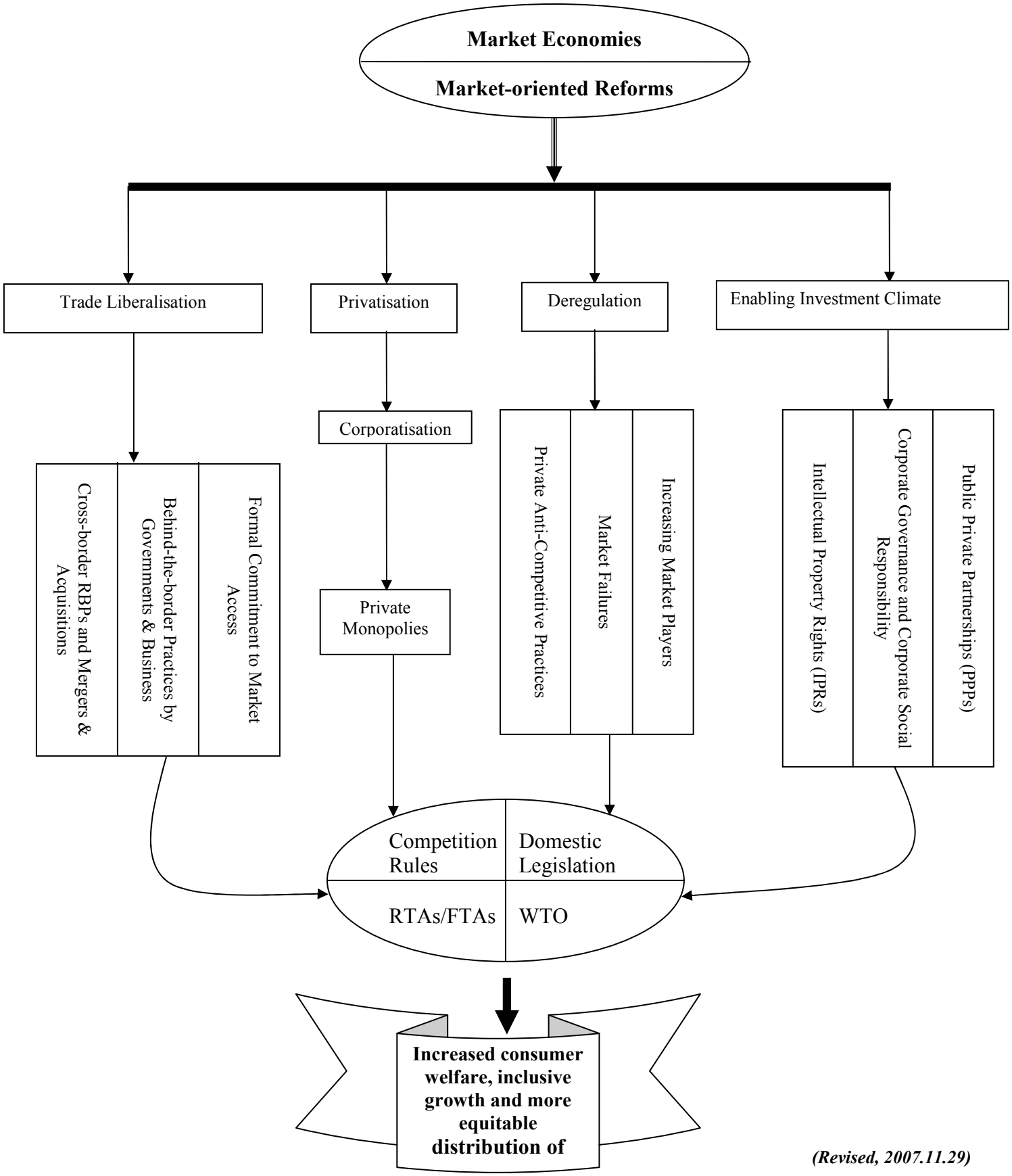
International anti-competitive practices can also be harmful to small and developing countries without effective competition laws. Cross-border mergers and acquisitions that lead to market dominance and the restrictive practices that some trans-national corporations engage in also further necessitate competition rules.

Competition policy also promotes good governance in the corporate sector as well as in governments by diminishing the opportunities for rent-seeking behaviour and the corruption that often accompanies it. Competition law and regulatory tools are invoked mainly to take care of firm behaviour and market failures. Governments often intervene when markets fail but in the absence of a clearly defined competition policy and regulatory mechanisms, the intervention can be arbitrary and serve vested interests rather than the poor. It regulates the economic activity within the country by protecting business and consumers against abuses of economic power and promoting efficiency and consumer welfare.

With liberalisation, many players enter the market which also improves the investment climate of the country. Enhanced investment climate gives way to investment in the infrastructure segment which may come in form of government investments, private investments or by way of a public private partnership. Increased investment leads to growth which in turn results in consumer welfare. 'Investment'

thus gets increasingly integrated with trade. Competition policy plays an important role in removing barriers to market entry for foreign investors.

Further, competition law provides necessary safeguard against arbitrary decision-making, apart from dealing with anti-competitive business practices by such investors. Investment through the M&A route is another area where there is significant interaction between investment and competition policy.



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