Competition and competitiveness

SHOULD EC COMPETITION POLICY PROMOTE AND PROTECT "EUROPEAN CHAMPIONS"?

Competition policy has long been recognised as one of the most powerful weapons in the European Commission's regulatory arsenal. But, against a backdrop of growing unease about the ability of European companies to compete with rivals in China and the US, some policymakers are now asking whether the regime needs a fundamental shake-up. In February, the EC's veto of the proposed merger of the train businesses of Siemens and Alstom drew a stinging rebuke from the economy ministers of Germany and France, who argued that such decisions were preventing European firms from reaching the scale required to compete effectively in an increasingly globalised and digitised economy. Instead, they contended, the EC should be promoting an industrial strategy that allows "European champions" to stand up to competitors from countries with laxer antirust rules. Were the ministers' concerns valid? If so, might their proposed cure prove effective?

It is not just about trains, it's about the economy

The French and German ministers for the economy, Bruno Le Maire and Peter Altmaier, did not pull their punches in their criticism of the EC's decision to block the Alstom-Siemens merger. In an unprecedented joint statement, they argued that the commission had failed to recognise the growing threat posed by the rival Chinese train builder, CRRC, and had overlooked the potential benefits of the merger resulting from increase in scale and innovation. This was not in their view an isolated error of judgment by the EC, but a reflection of the short-sighted way competition policy was being applied. And it was damaging the European economy.

The ministers went on to set out a manifesto: competition policy in Europe, they proposed, should consider the longer-term impact of globalisation and digitisation on the level of competition faced by European businesses. It should also acknowledge that European firms do not enjoy a level playing field when vying with subsidised companies from countries outside the bloc (*read: China*) or large digital platforms (*read: the giants of Silicon Valley*) that have built an apparently unassailable lead over European challengers. Some of these platforms have benefited from technology developed by the US government, according to Mariana Mazzucato, an economics professor at University College London and one of the speakers at a high-profile EC conference on the digital economy earlier this year. By failing to take account of these considerations, the EC was preventing the emergence of large European rivals that could compete against the likes of CRRC in China or Google in the US.

Underlying these concerns is perhaps a deeper anxiety that Europe is lagging behind the US and China. The Chinese economy has now eclipsed that of the EU on some measures to become the world's largest. And while it may be unrealistic to expect per capita income growth rates in developed Europe to match those of developing China, the EU is losing ground to the US as well. At the corporate level a similar picture seems to emerge: of the ten largest companies in the world by market capitalisation in 2019, eight are American and two are Chinese; European firms, by contrast, are conspicuous by their absence. Paired with these fears about European competitiveness are wider worries about the impact of globalisation. While many acknowledge that deeper integration of the world economy has benefited consumers, there is growing anxiety that European companies and workers are losing out in the medium term, hindering growth and exacerbating inequality.

The right tool for consumers

Antitrust watchdogs in Europe have traditionally had a one-track mission: to make sure that markets deliver value for consumers by seeing to it that competition remains strong wherever it operates across the economy. The risk of consumer detriment resulting from the abuse of market power should not be taken lightly. Returning to the Siemens-Alstom case, the EC concluded that the merged entity would gain a combined share of more than 60% of the European market for very-high-speed trains (with speeds of over 300km per hour) and would face limited competition in the critical area of rail signalling. Central to the EC's conclusion was its assessment that CRRC was not a strong competitor to Siemens and Alstom for contracts of very-high-speed trains in Europe. This finding was based on an analysis of the bids made by different competitors for contracts in Europe. CRRC was winning bids in other parts of the world and in lower-end markets, especially in China, but was not competing head to head in Europe or for very-high-speed train contracts.

A lessening of competition would have allowed the merged entity to increase prices or reduce quality, without risking the loss of too many customers. If that were to happen, the EC concluded, rail transport companies and – ultimately – European travellers would lose out. This fear seemed to be shared by many national competition authorities in Europe – including the Autorité de la Concurrence in France and the Bundeskartellamt in Germany – which backed the EC's decision to prohibit the deal.

The righteous tool?

But perhaps this would be missing the point of the criticism laid out in the French and German ministers' joint manifesto. By reviving the idea of national or regional champions – now in the context of the European economy – Le Maire and Altmaier were suggesting that promoting consumer welfare should not be the only goal of competition policy. Instead, antitrust authorities should be given a wider remit to promote fairness, job creation and economic growth in Europe in addition to consumer welfare. The ministers did not deny that consumers might stand to gain from strong competition in a globalised economy delivering better products at lower prices. But, they indicated, there may be a balance to be struck between what is in the narrow interests of consumers and these wider considerations.

Underpinning these proposals is the idea that there are unavoidable trade-offs between competing economic objectives, and in particular –

- between promoting the interests of European consumers and European workers;
- between promoting competition for consumers within Europe and promoting the competitiveness of European businesses on the world stage; and
- between promoting short-run consumer interests and longer-term economic growth.

On this view of the world, Europe's current competition policy regime is grossly imbalanced: in being tasked with narrowly prioritising the interests of European consumers, it is ignoring – and indeed damaging – the separate interests of European workers, European competitiveness and European growth.

But do these trade-offs really exist? To start with, it is not clear that loosening competition policy to facilitate the creation of larger European companies would help employment per se. Economies of scale and synergies such as those suggested in the merger between Alstom and Siemens often lead to job cuts. By taking job losses into account the Commission could then be required to block pro-competitive efficient mergers if these also lead to a reduction in the workforce. Furthermore, it may be unrealistic to expect that "European champions" would decide to locate their factories in Europe rather than in countries where labour costs are lower, particularly if they are competing with Chinese companies that benefit from lower labour costs.

Concerns about unfair competition from non-European firms – and the resulting costs for businesses and workers – may well be valid. Again, however, it is not obvious that overhauling the European competition regime would be the best way of levelling out the playing field:

- The strategy espoused in the ministers' manifesto would in essence amount to fighting fire with fire by affording European companies the same aid and privileges their rivals enjoy. If a non-

European country takes steps to support the creation of a national champion, then Europe will see you – and indeed raise you – by creating a pan-European champion. This could in principle prove effective in restoring the competitive balance between leading multinational businesses in different parts of the globe. But, in the process, it would come at a cost to the overall level of competition. In economics jargon, the outcome would look dangerously like a sub-optimal equilibrium: the favours granted to European and non-European champions would end up cancelling each other out – to neither side's benefit – while consumers everywhere would risk losing out. In the worst-case scenario, fierce competition between a host of firms would be replaced by bubble-wrapped rivalry between a handful of cosseted favourites.

- An alternative way of redressing the competitive imbalance would be to try to persuade non-European countries to back down and reduce the privileges they grant their own national champions. For example, if non-European companies are demonstrably benefiting from state subsidies or violations of intellectual property rights that would be illegal in Europe, then why not apply sanctions to these businesses similar to those European firms would face, as a pre-requisite for being allowed to trade in the EU? The EU has recently agreed tougher screening arrangements for foreign investments. In principle these could be extended to consider subsidies and respect for IP rights. It is true that such measures would give the EU direct influence only over trade in Europe (rather than, say, competition between European and Chinese companies for business outside Europe). But Europe remains an essential market for many international firms. The real prospect of being shut out of this market (or having to pay substantial financial penalties to retain access while breaching EU rules) may at least give non-European businesses and their political backers cause for thought.

What of promoting long-term European growth – and the engine that ultimately drives growth, innovation? Some have pointed to Airbus – perhaps the firm that comes closest to already having the status of a European champion – as an example of how regional cooperation rather than competition can enable European industry to maintain a technological edge. But the relation between scale and innovation is not clear-cut. For instance, large and reliably profitable companies may find it easier than small, unproven rivals to raise capital to invest in R&D. However, at the same time, they may have less incentive to undertake such investments than smaller, leaner rivals – particularly if the resulting innovations cannibalise the earnings from older products that they already sell. And if creating a small number of champions shrinks the pool of competitors, might this further erode incentives to innovate? Would Siemens and Alstom continue to invest as much in new trains if they faced little competition for existing sales?

The right tools for tomorrow?

This is not to say that promoting the welfare of European workers or the continent's competitiveness and growth are not legitimate objectives – or that they should be subordinate to the interests of consumers from the wider perspective of European policymakers. Nor would it be correct to assume that the existing antitrust regime is reliably delivering the best outcomes for consumers, and therefore need not change. On the contrary, the digitisation and globalisation of the economy is radically reshaping the dynamics of competition in many markets. The procedures that competition authorities follow may require an extensive rethink to address these challenges. In this regard, the EC's recently announced plan to explore whether its existing guidelines on vertical agreements remain fit for the digital age is eminently sensible. The report commissioned by the EC on digital markets makes a number of recommendations with regards to the application of competition policy, which we separately discuss in our article '*The Elephants in the room*'. These are broadly consistent with many of the recommendations put forward in a separate more recent report commissioned by the French Government to the *Inspection Générale des Finances* on competition policy.

But for the reasons discussed above, it is not clear that using competition policy to promote consumer welfare really involves compromising the interests of workers, competitiveness or growth. Even if such trade-offs did exist, a decision would then need to be taken for each merger investigation as to which fundamental objectives should take precedence. This is an inherently political judgment (that, frankly, should sit well above the paygrade of mere competition economists). But the Siemens/Alstom case suggests that gaining wide political support for such veto decisions would be difficult. The Netherlands, Sweden, Belgium, Finland, Denmark, Portugal and, more recently, Iceland all spoke out against the proposal. They fear that political veto powers would be used to build-up industrial champions in large countries, while consumers in smaller countries would lose out.

And, of course, agreeing a coherent set of parameters in Brussels would only be the first of many challenges. The proposals in the ministers' manifesto conveniently gloss over the other practical complexities of European political economy. For example, the interplay between European and national competition guidelines would need to be considered: if European competition rules promote European champions, then might individual member states apply the same logic to defy state aid rules and promote national champions?

In short, it would be preferable to use other policy levers – changes in trading legislation, better enforcement of intellectual property rights and investments in human capital – to boost European competitiveness, growth and workers' welfare than to seek to rebuild the antitrust rulebook based on these objectives. By demanding that competition authorities pursue multiple goals, policymakers would run the risk of undermining their effectiveness, and ultimately their legitimacy. In the final assessment, it would be better for competition policy do one job well than many jobs badly.