The role of competition in the promotion of competitiveness and development: Experiences from a sample of developing and least developed countries[♣]

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1. Introduction

The role of competition policy in development strategies and the specific features of institutional design that are most conducive to development have been constant areas of enquiry in development economics. Standard economic theory tells us that competitive forces work best and deliver the expected outcomes when there exists a market that is not overridden by distortions. The model of free market economies is a theoretical construct with great historical power. It is the model that is introduced at the beginning of every economics textbook and has been canonized with the authority of Adam Smith, the founder of modern economics. Free competition is a fundamental assumption in any market economy and has even been seen as one of the foundations for democratic societies.

However, few standard economic texts refer to Adam Smith's caveat about the need to "cultivate" free competition. He understood only too well that “people of the same trade seldom meet together even for merriment and diversion, but the conversation ends in a conspiracy against the public or in some contrivance to raise prices” (Smith, 1776).

Smith indirectly pointed to the need for corrective actions against anti-competitive practices. As part of good governance and institution building, an increasing number of developing and least developed countries have adopted competition policies at national level, as part of a coherent set of policies to create comparative advantage and internationally competitive industries. Competition policy can have a positive impact on a number of key macro- and micro-economic ingredients for competitiveness and development. Despite growing evidence of the benefits of adopting a competition law and policy, the gap between the assumptions of theories and the realities in many developing and even developed countries still remains.

While there is growing consensus that competition laws and policies are necessary for sound economic development, there is still disagreement on how to achieve this objective. Key concerns which have been raised by developing countries considering adopting a competition law or strengthening competition in their economies referred to whether such a law is necessary given trade liberalisation, whether it would damage international competitiveness, and whether increased competition would raise unemployment or cause other social problems.

Several objections about competition policy objectives have been raised. In particular, concerns have been voiced about the constraining effects of competition policy on other development strategies and major debates have addressed the potential conflict between competition policy,

on the one hand, and strategic trade and industrial policies, on the other. Strategic trade policy makes a compelling argument in favour of temporary protection suggesting that development requires modern technology, which must be acquired and cultivated, and that learning by doing must occur within national borders and sheltered from import competition. Examples of successful industrial policies are found in past and recent history, particularly in East Asia. For such policies to succeed, governments must be able to identify strategically important industries and some firms that can act as “national champions” once the learning-by-doing phase has been carried out under appropriate funding and protection. However, despite a number a success stories, no systematic positive relationship has been found between firm size and profit, export activity, or research and development, and an equally large number of notorious failures of industrial policy can be cited. Indeed, even if we could show that governments had in the past been able to pick winners by ignoring the, admittedly highly imperfect, natural selection process of the market to help them, we could not be sure that such a process would work today, even in more advanced developing countries, let alone in other countries with less capability.

It is therefore not surprising that conflicting views on the relevance and the content of competition policy in developing countries still coexist. The point of departure of this paper is that in developing countries markets work imperfectly and rather slowly and that competition policies can play a crucial role, together with other public policies, in enhancing the development prospects of their economies. The paper explores these issues and places the current debate surrounding the role of competition policy in the wider context of pursuing effective development strategies an increasingly globalized economy. The paper seeks to pull together the mechanisms through which competition policy can contribute to improved economic performance and the prerequisites for development-oriented competition policy implementation. The main policy question is going to be addressed throughout this paper is twofold: “Competition policy: to have or not to have?” and, if so, “How to maximize the expected benefits arising from competition, given the existing policy and economic constraints?”

The remainder of the paper is structured as follows. The next section reviews the arguments in favour of competition and competition policy enforcement. Section 3 looks at the complementarities between trade and FDI liberalization and adoption of domestic competition laws and policies. Section 4 seeks to clarify the need for competition policy as part of a deregulation and reform package. Section 5 spells out the pre-requisites for effective policy implementation in developing countries. The last section concludes.

2. Competition policy: to have or not to have?

Competition is unambiguously a good thing in neoclassical economic theory. This stems from a belief that competitive markets give consumers wider choice and lower prices and give sellers stronger incentives to minimize their costs and eliminate waste. In addition, in competitive

markets, firms need to innovate and adapt quickly to changing circumstances, thus creating dynamic efficiency. Competition also induces firms to pass on cost reductions to consumers and better satisfy their specific preferences. Some of the effects of competition are not easily measurable, since much of the evidence is inconclusive, ambiguous or over-aggregated. However, the existing empirical evidence supports these theoretical arguments. For instance, Ahn (2002) reports in a recent survey of the literature that a large number of empirical studies seem to confirm that product market competition encourages productivity growth. Nickell (1996) is representative of such a study. He finds that for a sample of 676 UK firms over the period 1975-1986, competition was associated with both higher productivity levels and productivity growth. Disney et al (2000) extends this study to a larger data set of around 143,000 UK establishments over the period 1980-1992 and finds similar results.

If the benefits of competition *per se* are difficult to assess, even more difficult is to assess the benefits of competition policy enforcement. Because of these difficulties, there is a paucity of studies quantifying the effects of competition law enforcement. Nevertheless, there is still evidence that the application of competition policy enforcement has had a positive economic impact, both in specific cases and by having a more general deterrent effect, helping to create a climate favourable for competition. For instance, surveys in the United States have found that price cuts tend to occur at the outset of an investigation, before the actual bringing of a case. Even where firms investigated for price fixing are not charged, there may be price reductions, and trend-adjusted prices may remain lower than their pre-investigation levels for a considerable time after the termination of a price-fixing case (Feinberg, 1984). Similar responses to competition cases were found in a time-series study of producer price indexes for 10 products from the mid-1950s to the mid-1980s involved in cases where the European Commission and/or the German Federal Cartel Office (FCO) had found that anti-competitive practices had occurred (Feinberg, 1986).

In many developing countries, however, the benefits of competition policy have yet to emerge visibly, because enforcement has been hampered by lack of resources, reliable data, or sufficient information about production costs, market shares and consumer behaviour. However, in many cases, the competition authorities have played an important role in the formulation of liberalization, privatization and deregulation policies, ensuring that their objectives are growth inducing. Kee and Hoekman (2003) examined the impact of competition policy on profit margins and concluded that government policies to facilitate entry and exit of firms can have important effects on industry.

Although there is limited empirical evidence concerning the impact of competition policy in developing countries a few authors who have analysed this aspect have reached similar conclusions.[1] For instance, Kahyarara (2004) showed that various aspects of competition policy played an important role in improving Tanzania's economic performance. The evidence provided

by firm-level indicators (such as investment, productivity and export performance) suggests a robust positive relationship between government measures aiming to stimulate competition and protect consumers against anti-competitive practices. Firm-level investment after the adoption and implementation of competition law in Tanzania was over one-fold higher than firm-level investment in the pre-competition period. At the same time, firms that seem to be affected by anti-competitive practices invest 30% less than otherwise (Kahyarara, 2004:285). As international competitiveness depends on a country's ability to consolidate, upgrade and diversify its productive capacity, a well-implemented competition policy may act as a crucial ingredient in a successful development strategy.

Moreover, as the experiences of many countries have demonstrated (the Korean case is a *locus classicus* in this regard), in the long run full confrontation with competition has been essential to ensuring the continuing development of industries, at all stages of development (Hur 2004; Yun 2004). In order for protected industries to gain significant economies of scale and become globally competitive in the true sense of the term, "infant industry" protection should be transparent, time-limited, applied selectively, made conditional upon meeting performance standards, involve minimum discrimination, and, above all, be constantly reviewed.

It has to be also recognised that providing protection to the domestic sector, particularly to infant industries, is the second best option. For instance, Amsden and Singh (1994) shows that even in Korea, a typical example for the infant industry argument, there existed more competition than is often thought, and not all of the growth was due to government protection and subsidies.[2] Based on a panel data set of manufacturing firms from Korea for the period 1990-2002, Yun (2004) also argues that although increased monopoly rent may boost up productivity growth on the short term, it may hinder economic development in the long run, and that the latter effect is prevalent.

So far we have seen that there are many ways in which competition and competition policy enforcement can have a positive impact on the overall economic prospects of developing countries. However, there are two types of criticisms against the benefits of competition and competition policy. The first type of criticism argues that sometime safe secure markets for monopolistic firms will provide them with a guarantee of profit for investment and innovation. Although there are circumstances when this might occur, there is little evidence that such policies work systematically. Furthermore, it has been argued, a too-narrow definition of competition policy objectives may be detrimental for developing countries. For instance, promoting transparency in market transactions can harm competition by enabling companies to engage in tacit collusion. Likewise, aiming at very high quality standards for products to ensure consumers get good-quality products may run the risk that such standards will limit dynamic competition. Excessive competition may also negatively affect the stability of small and medium enterprises. Deregulation of interest rates and rapid entry by new banks in small markets may lead to "excessive" competition, which forces banks to make risky investments to boost their margins,

sometimes with destabilizing effects for the entire financial system. Excessive competition was also mentioned as one factor contributing to the downward trend in commodity prices.

Notwithstanding these arguments, “excesses” of competition could hardly be thought to exceed the negative aspects arising from the absence of competition. In fact, there is growing empirical evidence that, in general, more competition leads to more innovation and accelerates productivity growth and that there is a strong correlation between the effectiveness of competition policy and growth.

The second type of arguments is clustered around the idea that adopting competition laws and policies in developing countries is not a priority. For instance, it is argued that trade and FDI liberalization are more effective, and perhaps less expensive, policy tools to promote competition in domestic markets. A second argument is that competition policy may reduce the "policy space" available for developing countries to adopt a development-oriented package of regulatory policies. Each of these arguments will be dealt with in some details in the subsequent sections.

3. Trade, FDI liberalization, and competition policy: overlapping or complementary tools?

One argument in the trade and competition policy debate is that trade liberalization may act as a proxy for domestic competition policy. Some authors have even argued that trade liberalization can be a perfect substitute for domestic competition laws in small economies (Blackhurst 1991). According to the proponents of this view, the lowering of trade barriers increases competition from imports for those local producers of tradable goods and services mainly dependent on the domestic market. The additional competitive pressure obliges these firms also to improve their productivity and keep down prices to consumers. In addition, the liberalization of international trade, including the reduction of tariff barriers and the elimination of most quantitative restrictions on imports and exports, allows producers to expand their horizons to world markets, rather than relying exclusively on small domestic markets. By taking up the new export opportunities, they are able to increase output and lower costs through economies of scale. Moreover, because strong competition is usually encountered in export markets, these firms are generally under pressure to devise more efficient methods of production, better marketing techniques and quality improvements in their products. This often results in lower prices and better-quality goods, not only for foreign customers, but also for domestic consumers.

Based on such arguments, for small open economies, trade liberalization is frequently assumed to provide the required market structure for competitive industries so as to prevent monopolistic behaviour. While this argument carries some weight, for a number of reasons, trade liberalization alone is often not enough to maintain an optimal level of competition in all economic sectors. Firstly, a number of trade barriers still exist and new ones are often introduced to compensate for

the reductions in tariffs and abolition of quantitative restrictions on trade. For instance, contingent protection and in particular anti-dumping, has become a major bone of contention in international trade. Many economists are of the view that most anti-dumping actions do not in fact involve "predation" by dominant firms against importing country competitors. On the contrary, it is often observed that, when domestic firms file anti-dumping complaints, this increases the potential for anti-competitive practices to occur at home.[3]

Secondly, trade liberalization may not by itself eliminate the propensity of firms to engage in anti-competitive practices. Firms may simply widen the basis of the cartels they operate. Moreover, when collusion is based on prices, reduced trade barriers may increase cartel stability, by making retaliation for price cutting easier, promoting a more collusive understanding between domestic and foreign competitors about not exporting into each other's domestic markets (something similar to voluntary export restraints, but privately enforced). This argument suggests that, as in other instances, anti-competitive private barriers can easily replace governmental barriers to trade.

Thus, even if one believes that trade liberalization is of vital importance, countries may not be able to rely on this delivering its full benefits without having a competition policy. Therefore, even in the presence of more liberal trade policies, an effective competition policy is a highly desirable ingredient since private actors, fearful of the consequences of trade liberalization and stronger competition, may be inclined to protect their interests and market shares by introducing cross-border anti-competitive practices, such as international cartels, abuse of dominance, and abuse of intellectual property rights (Hoekman and Holmes, 1999). In some circumstances, such practices can limit international trade even more severely than the former high tariffs and just as severely as the non-tariff barriers. Domestic suppliers may enter into exclusive arrangements with their local distributors, which effectively deny importers access to some markets. Large retail chains may refuse to distribute traded goods. An international cartel may be established to fix prices, so that traded goods cannot be sold more cheaply than the equivalent domestically produced items. If an effective competition law is in place, such anti-competitive practices can be challenged. However, in countries where there is no competition law, the benefits of trade liberalization could be lost through such anti-competitive conduct in the domestic market.

It is increasingly clear that trade-related anti-competitive practices impair the process of development in developing countries more significantly than has previously been thought. This is true for at least three reasons. Firstly, given their narrow domestic industrial base, developing countries have to rely on imports of intermediate goods. To the extent that such imports are subject to anti-competitive practices either by domestic firms (for example an import cartel) or by foreign suppliers of these imports (for example an export or international cartel), the importing country will be penalized by higher than necessary import prices. The first practice clearly falls within the objectives of a national competition authority. However, prosecuting cartels among

foreign suppliers is a more daunting task for developing countries, which in many cases will need international cooperation.[4]

Secondly, to achieve their developmental goals, developing countries need to rely on export-oriented strategies. However, the gains expected to arise from recently eased market-access conditions at a multilateral level or through preferential schemes will be severely limited if private anti-competitive practices are still in place. Thirdly, foreign firms feel freer to engage in across-the-border anti-competitive behaviour when the countries to which they export do not have a domestic competition law and can neither individually nor through cooperation with foreign competition authorities challenge the firms' market behaviour. Thus, countries that do not have a domestic competition law will be the prime victims of international anti-competitive practices. Ensuring that measures are in place to deal appropriately with such arrangements should be one of the major objectives of any national competition framework.

The need for competition law is also evident when foreign direct investment is being liberalized, as the impact of FDI is not always pro-competitive. It is often the case, in fact, that foreign direct investment takes the form of a foreign corporation acquiring a domestic enterprise or establishing a joint venture with one. By making such an acquisition, the foreign investor may gain a dominant position in the relevant market, enabling it to enjoy a high profit margin, and charge prices well above a competitive level. Another scenario often encountered in developing and transition economies, is where the affiliates of two separate multinational companies (MNCs) have been established in competition with one another in a particular market, following the liberalization of foreign direct investment in that country. Subsequently, the parent companies overseas decide to merge. With the affiliates no longer independent of one another, competition in a host country may be virtually eliminated and the prices of the product increased, even if the market in the MNC home country may be very competitive.

These adverse consequences of mergers and acquisitions by MNCs can be avoided if an effective competition law is in place in the host country. As UNCTAD (1997) points out, competition law enforcement signals to firms that inward investment that is motivated by the pursuit and eventual abuse of a dominant position will be dealt with by competition law. As mentioned earlier, one element typically found in competition law is a prohibition of any merger, acquisition or takeover likely to substantially lessen competition or prevent access to a market. Being realistic, we know that even developed country competition agencies have limited scope to ban more than a few mergers outright. However, they can often impose conditions on such mergers – and what is striking is that we find that several developing countries have also been able to impose conditions, for example brand divestiture on foreign MNCs, provided they act in time (CUTS, 2003).

It is also argued that an economy that has implemented an effective competition law is in a better position to attract foreign direct investment than one that has not. For instance, Noland (2003) found that the degree of industry concentration is negatively correlated with inward FDI. Even though subject to certain caveats, this suggests that oligopolists may indeed be able to impede foreign entry using the techniques described in the preceding section. This is because Incumbent firms often attempt to exclude new entrants by denying them effective access to goods or factor markets. This can be done by firms acting in concert horizontally across an industry (as in the case of a cartel) or vertically (such as in the case of a network of exclusive dealerships).

In countries where competition laws are enforced, multinational corporations expect competition authorities to ensure a level playing field between domestic and foreign firms, including among MNCs. However, when considering the prospect of investing abroad in a developing economy without a well-established competition law, foreign investors face the uncertainty of not knowing if, and when, competition legislation will be introduced and, perhaps more importantly, how it will be implemented. There are, of course, other areas of uncertainty that may tend to discourage foreign direct investment, notably political uncertainties, the slow pace of economic development, exchange rate movements, obstacles to international trade and government regulations and, of course, any discriminatory application of competition laws. Nevertheless, when a foreign investor has to make a choice between two or three alternative locations for a particular investment and these are of approximately equal merit, the country that has an effective competition law may be favoured.

In order to ensure that a developing country gains the full benefit of foreign direct investment, government policy in that area must be consistent with the objectives of competition law. Sometimes, in order to attract a large-scale foreign investment by an MNC, a national or local government may offer that corporation exclusive rights to supply its goods and services to the public authorities. It may even agree that no other firm will be given approval to enter the market in question. Such inducements are evidently anti-competitive, and the crucial question is whether competition policy objectives should be outweighed in certain circumstances by the economic benefits that the foreign direct investment can bring.

4. Competition policy and deregulation: is there a need for both?

From this short account it becomes clear that competition policy is complementary to the main policies aimed at trade and FDI liberalization undertaken in most countries of the world during the last 10–20 years. During the same period, many developing countries have also introduced various domestic reforms, involving greater reliance on markets and less emphasis on state intervention. Underlying these reforms is a renewed confidence that market forces and the individual decisions of consumers and privately owned businesses, can make a greater

contribution to economic and social development than an inward-looking centralized economic system. However, the potential benefits of a shift towards a more market-oriented economy will not be realized unless business firms are prevented from imposing restrictions on competition. Deregulation of previously regulated sectors, including state-controlled monopolies such as utilities and "network industries", for a long time considered for the most part to be "natural monopolies," need to be subject to competition review by competition authorities or sectoral watchdogs to ensure that these firms do not abuse their dominant position in the market. It is now considered likely that competition is possible in markets once thought of as naturally monopolistic, especially telecommunications, but experience worldwide shows us that incumbent monopolists often have tricks up their sleeves to inhibit this.

A large number of developing countries have undertaken regulatory reforms aimed at ensuring that regulations serve public interests better and reinforce competition in the market place. These reforms have been introduced in industries such as communications, transportation, public utilities, agriculture, and financial and professional services. They have included privatization and the liberalization of restrictions on market entry, and have also related to prices and business practices as well as universal service obligations, although there are important differences across countries and industries. One of the principal objectives of these reforms has been to broaden the scope for markets to allocate resources, and improve general consumer welfare and economic efficiency. Given these considerations, there is a clear interface between competition law and policy, deregulation and consumer welfare.

All these economic reforms have one important feature in common: the need for competition policy if market-oriented policies are to be given the best possible chance of success. For example, price liberalization, if not accompanied by competition laws and policy aimed at controlling economic behaviour and structures, can result in substantial price increases and reduced benefits for the overall economy. If monopolistic structures are allowed to continue unchecked, price liberalization will not proceed satisfactorily. The same can be said of privatization of state monopolies into private monopolies. Finally, as shown in the previous section, opening of markets through import competition and FDI liberalization might bring enhanced competition, but if no safeguards exist, foreign firms might also engage in anti-competitive practices and abuse dominant market positions (UNCTAD, 2002). This may take the form of predatory behaviour to eliminate local competition, or perhaps more likely cartels and market-sharing agreements possibly in cooperation with local firms, which deny consumers the benefits of trade liberalization. Hence the need for a strong and effective competition law which will only permit anti-competitive agreements or conduct where there are demonstrable net public benefits.

Competition law and policy are therefore intended to regulate anti-competitive behaviour by firms, whereas deregulation is aimed at minimizing market-distorting government intervention.

Regulation is meant to control the behaviour of firms in sectors where market failures are widespread and where we cannot rely on competition alone. But regulatory policies can also act as a barrier to competition when measures taken by state administrations (e.g. central or federal government, local government) or by bodies enjoying a governmental delegation prevent or hamper effective competition, e.g. by licensing restrictions on investment for new entry, and lead to a loss in welfare. Such measures are to be found in as diverse activities as telecommunications, financial services (banking and insurance), professional business services (accounting, lawyers, architects, etc.), and the energy sector (electricity, gas), as evidenced by an abundant literature.

Regulatory barriers to competition can negatively affect not only market entry but they also can prevent market exit, for instance through public subsidization or the granting or prolongation of monopoly rights. In addition, they can make it harder for resources to be allocated from one sector or market segment to another. They can be considered barriers to mobility, which prevent resources from being transferred into more-efficient sectors or segments, and which in the end will reduce allocative efficiency (UNCTAD, 2001a). Competition agencies could therefore perform important advocacy and consumer protection roles in the regulatory reform process. Competition agencies may also be instrumental in drawing attention to how regulation may unnecessarily restrict competition and how part of the solution to this problem may lie in the universal application of general competition law. The experiences of many countries show success in removing some of the severe restrictions on competition in regulated sectors. However, despite significant progress through competition advocacy and competition law enforcement reported by many countries, changes in the affected sectors occur relatively slowly (UNCTAD, 2001b).

From a market structure point of view, the competition authorities should be consulted when a process of regulatory reform is being undertaken as part of a privatization programme. They should be given legal powers to impose divestiture measures on existing monopolies or to control or prohibit mergers that undermine competitive market structures. If they are not given such powers, for instance because of a lack of human resources, it should be made possible for them to suggest divestiture measures or merger controls to an executive authority that has those powers. Nevertheless, it is clear that the dominant pattern of distribution of roles between competition agencies and regulatory agencies is rarely one whereby competition authorities simply replace regulatory agencies. The division of responsibility between competition authorities and regulators has proven difficult to agree in developing countries. Experience suggests that there is a real danger of capture where a regulator has just one or a few major firms as its "clients" (CUTS, 2003; Tirole, 1999).

Studies of these relationships show that the competitive process can be appropriately stimulated by the intervention of competition authorities when firms in a regulated sector abuse their privileges to the detriment of consumer interests and the efficiency of firms that use their

regulated services. The experiences so far suggest that there are specific regulatory regimes in many sectors and there is no unique model for the relationship between sector-specific regulators and competition authorities either across countries or sometimes even within a country. However, one particular model – the mandate-driven division of labour approach – appears to be somewhat more common than others. It is clear, at least, that sectoral regulators should be separated from regulated firms or entities and should assume obligations regarding accountability and independence from the executive branch of government. Also, institutional changes should be effected in order to guarantee their independence (UNCTAD, 2001a).

5. Competition policy and sound institutional environment

The previous analysis argued that simply "rolling back the frontiers of the state", without having in place an appropriate policy to deal with the potential of anti-competitive practices in the deregulated sectors does not necessarily lead to a sound institutional environment. Similarly, one should not be overly simplistic in promoting the importance of competition policy as a major and independent determinant of long-term growth. Competition policy is a complex, cross-cutting policy instrument that is affected by a number of related factors. Failures in the overall infrastructure that effective competition policies need for their enforcement will obviously reduce the expected benefits stemming from the adoption of competition policy and laws at national level. As a number of developing countries still struggle with deficiencies in their overall institutional infrastructure, an appropriate balance should be found between the objectives and reasonable achievements of competition policy in developing countries.

However, these very specific implementation difficulties make the case for competition policy in developing countries actually stronger. This argument becomes clearer when realizing that factors that facilitate collusion, predatory strategies, market concentration (such as weak credit markets, high entry barriers and existence of capacity constraints) are likely to be more important in developing countries. Therefore, the design of a body of simple and transparent competition policy rules for developing countries, in particular for horizontal collusion and abuse of dominant position remains a worthy task. The optimization of the use of scarce human and material resources for regulatory purposes is also crucial. Furthermore, a competition agency will be valuable for its educational role in advocating the social benefits of fair competition.

It must be stressed that the argument in favour of competition policy made in the previous section needs to be qualified. It is necessary to establish that competition is, overall, a positive force for economic development. It is then necessary to show that firms left to themselves will resist pressures for markets to operate competitively: they will form cartels, create entry barriers and lobby governments. Once we see this, we further need to show that government policies to promote competition (including having a competition law) can actually remedy this in a cost-

effective way. It would be just as naive to suppose that competition policy always works perfectly as to suppose that markets work perfectly when left alone. Therefore it is important to establish what the pre-conditions are to get the maximum benefits of competition and of competition policy.

One central argument in the current development debate is that good governance has become the key variable in explaining the economic performance of successful developing countries over the last few decades. Good governance of regulatory agencies is also a major factor that can improve sector performance. For instance, the empirical evidence provided by Oliveira et al. (2004) suggested a positive relationship between the level of independence of Brazilian regulatory agencies and the performance and effectiveness of their respective regulated sectors. Similarly, one of the most important lessons from the reform implemented in the electric energy sector in Peru, during the last decade, is that the benefits of privatization (for example in terms of lower prices of generation) could have been offset by incoherent policies and that the role of the competition agency has been instrumental in supporting the actions of the sectoral regulator and the privatization agency (Ruiz 2004).

Several authors also cautioned that merely adopting a competition law is no panacea (Gal 2004; Nkikomborirak 2004). Instead, what really makes a key contribution to competitiveness and development is properly implemented competition policies. Nkikomborirak (2004) illustrates the importance of a cautious policy on the adoption of exemptions and exceptions. In the case of Thailand, *de facto* and *de jure* exemptions from competition law without sound economic justification proved to be costly to the economy when effective regulatory regimes are not yet in place. Moreover, favouring a competitive environment in other economic sectors through other policies that are directly or indirectly linked to competition policy, (e.g. establishing production standards, defined property rights, consumer protection agencies, efficient institutional frameworks with adequate human, technical and financial resources) would also have a ‘multiplier effect’ on the overall benefits expected from competition policy implementation.

This points out that policy-makers in developing countries face the challenging task of designing appropriate competition policies that will bring about economic development in these countries. As Gal (2004) and Adhikari (2004) suggest, there are several characteristics in developing countries that certainly can make the task of competition policy design and implementation difficult. In line with the vast literature on the political economy of antitrust enforcement. Gal (2004) emphasised the great importance of institutional competence, credibility and independence of competition authorities for the effectiveness of competition policy enforcement. In addition, such pre-requisites for effective competition policy enforcement, even when they are in place, can easily be hampered by an inadequate judicial system, excessive bureaucracy, vested interests, or lack of financial and human resources. Adhikari (2004) provides telling examples of such difficulties in the case of competition policy enforcement in Nepal. Nepal is no

exception: such constraints are also faced by many other developing and least developed countries.

Therefore, as Gal (2004) argued, the successful implementation of competition policies in developing countries will depend on the "ecology of antitrust". If not part of a well-coordinated set of legal and economic institutions, the impact of competition policy on productive capacities and in favour of more competitive economies is likely to remain minimal. The existence of large informal activities (in some developing countries the informal sector is thought to account for as much as 60% of their GDP), the lack of well defined property rights, limited environmental, safety and health standards, underdeveloped consumer protection institutions and laws, limited capability to verify and check standards, lack of technical expertise and experience, may all limit the potential benefits stemming from an effective competition policy implementation.

Conclusions

Throughout this paper, it has been argued that competition laws and policies in their various forms can be used as a tool for enhancing competitiveness and development. That all countries, including developing countries and LDCs, are adversely affected by anticompetitive practices is unquestionable. Similarly, there is a widespread belief that the creation of competitive markets empowers the poor, provides them with employment opportunities, and increases their access to cheaper and better quality products. Competition policy is therefore an important institutional pillar for a thriving market economy as competitive pressures hone production efficiency and stimulate product and process innovation fundamental to international competitiveness and economic growth.

While recognizing that globalization and liberalization of goods and services markets had the potential to improve national welfare, market failures, especially in developing countries, can pose major challenges to their competitiveness. As governments increasingly become cognisant of the fact that international markets are characterised by imperfect competition rather than the ideal competition of liberal economic theory, the role of competition law and policy becomes fundamental in ensuring a "level playing field". In such a complex and dynamic economic environment, competition, competitiveness and overall economic performance are closely intertwined.

Furthermore, it is not only the degree of competition that matters, but also the nature of competition that stimulates growth. As developing nations implement structural reforms designed to stimulate economic growth through greater reliance on the market system, concerns regarding competition policy naturally arise. These nations have a unique opportunity to create new

conceptions of competition policy designed to promote the competitive process and foster development.

While some aspects related to the design and implementation of competition policy may still deserve further investigation, the discussion in the previous sections brought out one clear conclusion: mainstreaming a certain degree of competition into a successful policy framework is fundamentally pro-development. Ensuring that competition policy contributes to enhancing the development prospects of developing and least developed countries has been a longstanding preoccupation in UNCTAD (Brusick and Cernat 2004). Over almost four decades, UNCTAD's work in this area proved that the case for national competition policies can hardly be overstated. As noted in the introduction, Adam Smith clearly understood the significance of competition and market entry over 200 years ago. This widely held notion remained perennial in economic thinking and there is now widespread recognition of the need to adopt national competition policies, both for reasons of equity and on grounds of economic efficiency. Joseph Stiglitz, the 2001 Nobel Prize winner, makes the argument forcefully:

> "Strong competition policy is not just a luxury to be enjoyed by rich countries, but a real necessity for those striving to create democratic market economies." (Stiglitz, 2001)

Therefore, the economic rationale for competition policy remains of paramount importance. This is particularly so for those developing and least developed countries moving towards market-oriented reforms. Several specific reasons call for adoption of competition law sooner rather than later. Firstly, the adoption of liberalisation policies, the rise in privatisations, and the fact that most privatised entities in the utilities sector are natural monopolies underscore the importance of a solid competition regime to elicit the most favourable efficiency and welfare effects of liberalisation and privatisation. In some cases, privatisation and deregulation have taken place with scant regard for, and often in the absence of legal and institutional frameworks for competition policy. In a period of extensive deregulation, the adoption of competition law and policy represents a complementary measure that would "bring the state back" in ways that support and reinforce recent market-oriented reforms, while limiting the scope for unnecessary regulation. During such an adjustment process, one challenge ahead is to infuse competition principles with sound economic analysis that reflect the special characteristics in which firms and policy-makers operate when "rebuilding the ship at sea".

Secondly, the recent proliferation of massive international mergers, the existence of international cartels and their potentially negative impact on consumers (Evenett, 2003) puts forward a case for competition policy to equip developing countries with the tools to deal with the increased market power of multinational companies and their anti-competitive practices. Such evidence suggests that, once government-imposed trade barriers are gradually removed, the "underworld" of trade-related private anti-competitive practices becomes even more apparent.

Even though national competition policies may be poorly equipped to deal with such potential negative external influences, the importance of domestic competition policies stems also from the differential impact that domestic and competition from abroad may have during adjustment periods. In certain cases, competition among domestic firms may have a relatively more beneficial effect than foreign competition, not only because it increases rivalry with known competitors but also because it provides a 'level playing field' among similar competitors and a gradual exposure to competitive forces, before engaging in full-fledged competition on world markets.

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Notes

[1] A good example of such a studies is Carlin et al (2001). See also Dutz and Hayri (1999) who, using presence of antitrust policy as the main proxy for intensity of competition In a cross-country study (100 countries over the period 1986-1995), show that competition has a positive impact on growth, both in developed and developing countries.

[2] Glen et al (2001) also show that in many developing countries competition has been higher than is usually thought. Their study finds that the persistence of profits in a wide range of developing countries (Korea, Brazil, India, Jordan, Malaysia, Mexico and Zimbabwe) is less than that reported for developed economy markets.

[3] Several studies have found evidence that anti-dumping is closely related or leads to different forms of anti-competitive practices. For example, Prusa (1992) and Zanardi (2000) studied the incentives for collusion between domestic and foreign firms involved in anti-dumping investigations. Prusa presented a bargaining model to explain how anti-dumping petitions serve as a vehicle to achieve cooperative levels of profits among competitors. Zanardi (2000), using an extended version of Prusa's model, shows that incentives to collude depend on two basic parameters: coordination costs and the relative bargaining power of participating firms.

[4] In a number of papers, Evenett and colleagues have documented the extent to which international cartels still operate in markets where developing countries import a lot and there are increasing concerns that agricultural exports and imports of LDCs are dominated by the small number of traders concerned.