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**Working Group on the Interaction
between Trade and Competition Policy**

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The following communication, dated 9 September 1997, has been received from the Hong Kong Economic and Trade Office with the request that it be circulated to Members.

I. INTRODUCTION

1. Members agreed at the meeting held on 7-8 July 1997 that this Working Group should discuss, *inter alia*, the relationship between the objectives, principles, concepts, scope and instruments of trade and competition policy, and their relationship to development and economic growth. This submission aims at enhancing the conceptual understanding on trade and competition policies, so as to facilitate the study of issues relating to the interaction between them as mandated by the Ministers in Singapore.

II. OBJECTIVES, PRINCIPLES, CONCEPTS, SCOPE AND INSTRUMENTS OF TRADE POLICY

2. Trade policy can be subdivided into two broad categories: trade liberalization policies and trade protection policies.

(a) *Trade liberalization* aims at a more efficient use of scarce resources in the importing country (e.g. by replacing less efficient domestic production by imports) as well as in the exporting country (e.g. by promoting more productive export industries rather than less efficient import-substitution). Non-discriminatory trade liberalization tends to enhance microeconomic "technical efficiency" (use of fewer inputs for the production of the same level of output at the firm level), macroeconomic "allocative efficiency" (use of national resources in the most productive and least costly manner at the country level) and consumer welfare (maximization of consumers' surplus).

(b) *Trade protection* tends to restrict or distort international trade for the benefit of domestic import-competing producers or export industries. Typically, such policies enable them to charge higher prices and produce larger quantities than might be economically justifiable in open markets without the trade restrictions and distortions. Therefore, trade protection tends to distort the efficient allocation of resources between markets and within markets, reduce the potential national economic welfare (e.g. in terms of real income and consumer welfare), and redistribute income for the benefit of the protected producers at the expense of consumers and taxpayers.

3. GATT/WTO law provides worldwide legal disciplines for the use of alternative trade policy instruments (such as tariffs, non-tariff trade barriers, trade discrimination, and subsidies). The GATT/WTO law ranks these instruments according to their economic efficiency: the less trade-distorting

a policy instrument is (e.g. border tax adjustments, production subsidies, non-discriminatory tariffs), the fewer legal restraints the law imposes on its use. The underlying objective is, as stated in the GATT and WTO Preambles, to enhance economic welfare and international trade through reciprocal trade liberalization. The GATT/WTO law does not prescribe specific policy objectives: WTO Members remain free to decide on what policy objectives they want to pursue. For instance, they may maintain tariffs, adopt safeguard measures against "injurious imports", and decide freely on their domestic, economic, environmental, social and other laws and policies as long as the measures introduced are within the confines of the GATT/WTO law. Under the dispute settlement mechanism, Members may also challenge any "nullification or impairment" of benefits under the WTO Agreement. Nonetheless, the GATT/WTO also sanctions certain measures which can be trade restrictive and distortive. Anti-dumping is a case in point.

III. OBJECTIVES, PRINCIPLES, CONCEPTS, SCOPE AND INSTRUMENTS OF COMPETITION POLICY

4. The primary objective of competition policy is to make the market as competitive as market forces, including technology, permit. Many argue that efficiency should ultimately be measured in terms of consumer welfare. Similar to trade policy, competition policy can be subdivided into two broad areas: competition-enhancing and competition-regulating policies.

- (a) *Competition-enhancing policies*, like trade liberalization, aim at promoting open markets and rivalry among firms so as to enhance "productive X-efficiencies", "allocative and dynamic efficiencies" and "distributive efficiencies" throughout the economy. This is achieved by promoting competitive business conduct (e.g. by means of deregulation initiatives to allow more open competition between firms; and prohibitions of collusion by private firms, abuse of private market power, discrimination by public enterprises) as well as competitive market structures (e.g. by enhancement of an economy's contestability by maintaining a liberal trade regime, controls of market concentration and prohibition of state aids). While trade policy rules are primarily addressed at governments in their role as regulator of the national economy, competition policy rules are primarily targeted at private economic operators.
- (b) *Competition-regulating policies* are often adopted in circumstances where free or unrestrained competition may not be practicable and a controlled monopoly or oligopoly can be justified. These are common in sectors where a very high level of investment is required, where there is a need for prudential supervision or where there is a need to protect the long-term interest of consumers. Under these circumstances, there may be a case for the use of different control instruments to regulate or even restrain competition to make sure that consumer welfare will not be compromised. For example, such policies may permit collaboration among firms on R&D so as to enable economies of scale whose beneficial effects may outweigh the disadvantages from less competition.

However, some competition-restrictive policies, like trade protection policies, aim at improving the national terms of trade (e.g. support for trade monopolies and import or export cartels in an attempt at "rent-shifting" for the benefit of domestic firms); protecting regulated industries and international cartel arrangements among public firms in spite of economic inefficiencies (e.g. in the airline, maritime, communications and electricity sectors). As a result, consumer welfare will be impaired.

5. In contrast to the worldwide GATT/WTO legal disciplines and comprehensive trade policies/laws in all WTO Member economies, there are no worldwide legal disciplines on competition policy. Economies tend to take their domestic conditions, e.g. history, market structure and state of economic

development into account when formulating domestic competition policies. In this regard, the Working Group is aware that there is no international consensus on core competition principles for the formulation of competition policies.

IV. COMPLEMENTARY FUNCTIONS OF TRADE AND COMPETITION POLICIES

6. Trade liberalization and competition policies serve complementary functions in many respects. For instance:

- Both aim at a more efficient allocation of economic resources and are mutually interdependent. A liberal trade policy may be the most effective means of enhancing competition between firms in the domestic economy. On the other hand, an effective competition policy in an exporting economy can help to prevent firms from the economy to gain and abuse their dominant market positions in domestic economy. Competition policies aimed at liberalizing *private* market access barriers and correcting market distortions can therefore be seen as a logical continuum of trade policies aimed at liberalizing *governmental* market access barriers and distortions.
- Trade liberalization and competition policies serve *general interests* of all domestic consumers (e.g. by promoting lower prices and better quality of goods and services). Competition policy can contribute to reforming trade protection policies, which often restrict competition and promote protectionist group interests at the expense of other citizens. For instance, in order to promote competition and economic welfare, anti-dumping and other safeguard measures should focus on "injury to competition" rather than "injury to domestic industry".

V. INCONSISTENCIES BETWEEN TRADE AND COMPETITION POLICIES

7. There are differences between trade and competition policies which at times bring about inconsistencies, hence distorting the efficient allocation of resources. For instance:

- Competition policy instruments are not subject to worldwide international legal disciplines and international dispute settlement mechanism as trade policy instruments. Means may not be available to redress private anti-competitive practices, such as import and distribution monopolies, which may impede international trade and effective market access of foreign suppliers.
- GATT/WTO law reflects a worldwide economic consensus on the optimal ranking of trade policy instruments according to their economic efficiency. There seems to be far less economic consensus on the optimal competition policies, for instance with regard to non-price vertical restraints and the taking into account of cost savings for producers (total welfare approach) in addition to consumer surplus (the consumer surplus approach gives no weight to cost savings for producers that are not passed on to consumers).
- Trade policy instruments (such as safeguard clauses) tend to focus more on producer interests and are politically convenient for assisting domestic groups. Hence they are more often used for non-economic policy objectives (such as foreign policy, environmental and health policies, social adjustment and income redistribution policies) than competition policy instruments which focus more on general consumer interests and economic efficiency. This "protection bias" of some trade laws is reinforced by the fact that they provide for more private rights to protection, and for less private rights to liberal trade, than competition policies/laws.

- Both trade and competition policies are often decided and administered in a fragmented manner without effective coordination among trade bureaucracies and competition policy institutions. For instance, trade policy-making processes concerning anti-dumping and other safeguard measures focus on "injury to domestic industry" without requiring an examination by the competition policy institutions of the anti-competitive effects of import restrictions on domestic competition. Similarly, competition policy institutions often decide (e.g. on the exemption of export and import cartels) without adequate regard to anti-competitive effects in foreign markets and without examination of the anti-competitive effects of other domestic policies. Competition officials may be concerned that the taking into account of non-competition policy objectives might render it more difficult for them to give priority to consumers' interests.

VI. RELATIONSHIP OF TRADE AND COMPETITION POLICIES WITH DEVELOPMENT AND ECONOMIC GROWTH

8. Modern economic research on the competitive advantage of nations suggests that open markets, liberal legal framework rules and a sound competition policy play a key role in fostering economic growth, innovation and continuous upgrading of productivity and product quality. In this regard, trade-liberalization and competition policies foster development and economic growth by limiting protectionist abuses of both government and private market power. They reinforce one another and result in a more efficient use of resources.

9. To help developing economies share in the economic growth generated through the interaction of trade liberalization and global competition, we support a dedicated study on the relationship between competition and development. Such a study should cover, *inter alia*, anti-competitive government and business measures and practices which may distort not only competition in developing economies, but also the competitive conditions of products originating from these economies; and examine the possible role of competition disciplines to promote trade and economic growth. The study should aim to contribute towards redressing the disadvantages to trade and development resulting from the anti-competitive behaviours, and to help maximize benefits to international trade and development of developing economies.

10. Over the past 50 years, international trade rules rightly gave priority to the reciprocal liberalization of governmental market access barriers. However, even today, some of these trade barriers (such as anti-dumping measures against imports even if the latter do not impair competition in the importing country) appear to be more harmful than private restraints of international trade. WTO Members should therefore continue to give priority to the liberalization of *governmental* market access barriers. To promote development and economic growth, national competition policies/laws can be no substitute for trade liberalization; nor can they be effective without international trade liberalization and transnational competition.

VII. CONCLUSION

11. The mandate of the Working Group on Trade and Competition Policy focuses on the "interaction" between trade and competition policy. This means, as stated by our Chairman, "... the Working Group is to study neither competition policy *per se* nor Trade Policy *per se*, but the interaction between the two".¹ We propose that further work should examine in greater detail areas of inconsistencies between trade and competition policies, as well as their mutual complementarities, with a view to identifying areas for further consideration in the WTO framework.

¹F. Jenny, Competition Policy in a Global Economy, New Delhi, March 1997, manuscript p. 20