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EXECUTIVE SUMMARY

Competition—the process of rivalry between business enterprises for customers—is a fundamental characteristic of a flexible, dynamic market economy. By responding to demand for goods and services at lower prices and of higher quality, competing businesses are spurred to reduce costs, increase productivity, make investments, and adopt new technologies and organizational methods to innovate in processes and products. Both economic efficiency and consumer welfare are enhanced. Successful enterprises become stronger and more competitive, whether in domestic or international markets.

However, the sustainability and benefits that accrue from the competitive process are not solely dependent on the business conduct of enterprises. They also depend on the business environment or investment climate in which they operate, including the legal and regulatory framework, barriers to entry and exit, and prevailing conditions in markets for labor, land, finance, infrastructure services, and other productive inputs. Moreover, even if most of the problems that enterprises often confront in these areas—especially in developing countries—were mitigated, competition is not necessarily ensured. The process of competition is not automatic. Vested interest groups, incumbent large monopolistic firms, and other stakeholders can dampen, distort, or capture the benefits of market-oriented economic reforms such as trade and investment liberalization, privatization, and deregulation. Empirical studies and case examples indicate that while such economic reforms are pro-competition, they are insufficient. Even in advanced industrial economies, consumers have fallen victim to domestic and international cartels and related anticompetitive business practices—despite the presence of fairly flexible and deep markets for labor, finance, and various other inputs, diverse sources of commercial information, and well-developed market support institutions and business infrastructure. The consumers in these cases were not only ordinary citizens but also enterprises whose competitiveness was undermined by artificially rigged prices.

The competitive process needs to be maintained, protected, and promoted. Herein lays the critical role and importance of an effective competition law-policy. A well-designed and effectively implemented competition law-policy aims at reducing or eliminating impediments to competition that unnecessarily arise from public policy interventions as well as private sector restrictive business practices. Such a law entails both enforcement actions against illegal business conduct and "competition advocacy" to encourage government to reconsider the design and necessity of regulatory and other barriers to competition. It provides for mechanisms whereby injured parties can seek relief against anticompetitive business practices. It also promotes better public and private sector market governance through promoting greater compliance with the law and adoption of sound business ethics. In addition to helping realize the benefits of competition, competition law-policy fosters broader and shared economic development by reducing barriers to entry and competition, increased accountability and transparency in government-business relations, and limiting opportunities for rent-seeking and corruption.

However, there are differing views whether developing countries need to adopt competition law-policy early on in the sequencing of their economic and regulatory reforms, or even to have a specific competition law and institutions. The case against enacting competition law-policy rests primarily on arguments that economic deregulation, trade and investment liberalization will result in increased import competition and entry of new

firms which will erode any excess profits and market power of incumbent firms. Actual experience suggests otherwise. Domestic markets can remain insulated from external competitive pressures due to high transportation costs, non-tradable products and services, exclusive and restrictive distribution contracts, and domestic and international cartels and market sharing agreements. In recent years, even industrialized countries with well established competition regimes have fallen victim to international cartels in markets such as food additives, steel, large transformers and pharmaceutical products. Developing countries that had not adopted or lacked effective competition law-policy were found to pay higher prices for these products.

Another line of argument is that developing countries lack strong supporting institutions such as independent judiciary, good governance, independent media, and professional, well paid civil service. This increases the risks that the law may get misapplied and become a vehicle for unnecessary intervention in markets, corruption and bribery. These risks are undeniable but they also equally apply to other important areas of government services such as customs, tax collection, education, health and safety among others. Instead of avoiding these responsibilities of government, it is important to assist countries in creating and building effective institutions with capable staff and appropriate system of checks and balances. This process can be "jump-started" with provision of technical assistance from more experienced countries, facilitated by multi-and bi-lateral donor organizations.

During the past two decades, more than 100 countries have enacted or significantly revised and strengthened their competition legislation—including many developing nations. However, the adoption of competition laws varies across regions. Proportionately fewer countries have embraced competition law-policy in sub-Saharan Africa, the Middle East and North Africa, East Asia and Pacific, and South Asia regions relative to countries in Europe and Central Asia and Latin America. In all these regions, the least-developed countries (International Development Association [IDA] member nations, which are eligible for grants and low-interest loans) have been especially slow in adopting competition law-policy. There is a wide variation in the institutional design and implementation of these laws. In many of these countries, there are widespread allegations of anticompetitive practices in markets for goods and services such as bakeries, cement, cotton, fertilizers, fish processing, freight transportation, insurance, school textbooks, seeds, steel, staple food products (rice, sugar, vegetable oil), and telecommunication services. Anticompetitive practices in the pricing and supply of many of these products have a particularly adverse impact on the poor. Also on the growth of small and medium sized enterprises which are often subjected to monopsonistic practices by large firms that out-source various intermediate products and services. Nonetheless, there are case-specific examples of anticompetitive practices that have been successfully addressed through the application of competition law-policy. Investigations of anticompetitive business practices under competition law-policy are primarily "demand driven" in response to complaints registered by individual consumers and business enterprises. For example, the Competition Commission of India registered its concerns and contributed to the shelving of a proposal by the Department of Post & Telegraph to extend its postal monopoly to include packages and letters weighing less than 300 grams. Had the proposed regulation been adopted, it would have destroyed the vibrant competitive private courier indus-

try. In Kenya, the Monopolies and Prices Commission has been instrumental in adoption of competitive-bidding policy in government procurement, which has resulted in significantly lower prices for drugs, hospital and school supplies, and road transportation services. It has also investigated alleged cartels in retail gasoline, insurance, Internet services, and various agribusiness product markets. Often the initiation of the investigations has had a deterrent effect on the anticompetitive behavior and resulted in lower prices even if no cases were prosecuted.

There remain, however, significant challenges in fostering competition in most developing countries. These stem in part from the lack of political will, inadequate financial and staff resources, and lack of requisite knowledge and expertise. There are also widespread misconceptions about the beneficiaries of competition, on which vested interest groups capitalize by marshalling fears of unemployment and need for supporting "national champions." A survey by the International Competition Network (ICN) found that strongest support for competition advocacy comes from consumer associations, academics and the media; less from entrepreneurial and professional associations, legislators, and least from political parties, labor unions and local governments. The least supportive or opponents to competition have the most economic and/or political power.

Moreover, international organizations, including the World Bank Group and donor community, have paid relatively scant attention to and provided little sustained technical assistance to foster competition law-policy. This represents a missed opportunity to help developing countries address some of the most egregious and persistent economic development and governance problems associated with high ownership and product market concentration levels, existence of dominant firms, and high barriers to entry and investment in these economies. These factors also result in "missing middle"-size firms, closed and often opaque government-business relations, entrenched vested interest groups, favoritism and corruption in government procurement, and a wide range of anticompetitive practices that undermine productivity and competitiveness. Drawing on published data, this paper indicates that:

- Higher levels and rates of growth in per capita gross domestic product (GDP) are associated in countries that have high intensity of competition in local markets. The IDA countries tend to have low levels of competition intensity in local markets, and low levels of per capita GDP.
- High intensity of competition in local markets is associated with greater effectiveness of competition law-policy. Again, IDA countries have low effectiveness in the application of competition law-policy.
- The higher the effectiveness of the application of competition law-policy, the lower is the prevalence of market dominance by few firms, and higher the ranking in the "business competitiveness index." The IDA countries have a correspondingly greater degree of market dominance, and rank lower in the business competitiveness index.

The levels and growth in per capita GDP, extent of market dominance, and intensity of competition and business competitiveness are determined by numerous other factors as well. However, the maintenance and promotion of competition through the effective application of competition law-policy can undoubtedly play an important role in mitigating concerns in this respect. Economies that do not address anticompetitive situations and lower barriers to entry and competition are

not likely to be attractive to investors. Firms that do not compete in their own home markets are less likely to become competitive in international markets.

RECOMMENDATIONS

Several recommendations are put forward which the World Bank Group, in partnership with other development organizations, client country governments, and civil society organizations could engage in to assist developing nations strengthen competition in their domestic economy, and adopt and effectively implement competition law-policy. These are:

POLICY AND DIAGNOSTICS PROJECTS

(i) Extend policy advisory and diagnostics projects aimed primarily at reducing public policy-based barriers to entry-exit, regulatory costs and delays, licensing, etc. to also cover restrictive business practices engaged in by private sector firms, business associations, and those emanating from closed, opaque government-business relations, especially in regard to government as a supplier or purchaser of goods and services.

INDUSTRY/MARKET STUDIES

(ii) Conduct industry/market-specific competition assessments and regulatory impact analysis to identify the principal public policy- and private sector-created barriers to competition as well as "winners and losers," and explore alternative, less-interventionist policy approaches to promote broad-based competitive investment and growth. Priority should be given to sectors that:

–have an impact on the poor (for example, staple food products, local transportation, water-sanitation, energy);
–provide products and basic services that serve multiple upstream or downstream economic activity and bear on industry value-chains and competitiveness (for example, ports, energy, telecommunications, financial services);
–engage in delivery and cost efficiency of government procurement of goods and services to reduce opportunities for corruption, bribery, and favoritism;
–comprise of potentially competitive and distinctive industries and economic activities that could attract foreign direct investment and related technology transfer and new organizational methods.

TECHNICAL ASSISTANCE AND INSTITUTION BUILDING

(iii) Increase capabilities and responsiveness to requests by least-developed countries for technical assistance for:

–drafting new or revising existing competition legislation and regulatory policies, administrative and interpretation guidelines, and related materials for effective policy implementation;
–providing advice and capacity development in skills such as case management, investigative techniques, compliance programs, regulatory interventions, industry/market competition assessments and regulatory impact analysis, and competition advocacy;
–promoting greater intergovernmental cooperation and coordination, and coherency and consistency in the application and formulation of economic

and regulatory policies to be least restrictive of competition;

–facilitating cooperation and exchange programs, sharing of information, and expertise with peer competition authorities in other countries.

Consideration should also be given to encouraging competition authorities in developing countries to focus not only on protecting and promoting competition, but also to play a more active role in supporting regulatory impact analysis. Economies such as Australia, Hungary and Korea among others have carried out radical reforms in which competition authorities played a key role. Other countries could draw lessons from this. In developing countries, with financial and human resource constraints, drawing synergistically on relevant expertise across different parts of government, with over-lapping and/or complementary responsibilities that bear on industries and markets, would result in avoiding unnecessary inter-departmental frictions. And contribute to greater stability, coherency and consistency in competition and regulatory economic policies. Policy instability has been frequently identified by firms as a major deterrent to investment in developing countries.

INFORMATION DISSEMINATION, BUILDING COALITIONS AND CREATING BROAD-BASED SUPPORT FOR COMPETITION POLICY

(iv) Work with consumer associations, nongovernmental organizations, private sector business organizations and trade associations, academic research and policy institutions, and legislators to foster greater understanding and appreciation of the benefits of competition and encourage grassroots ownership and demand for pro-competition policies.

1. INTRODUCTION

A persistent challenge that faces the governments of least-developed countries as well as policy advisors at the Bretton Woods Institutions, the United Nations, and aid agencies is: *how to foster sustainable broad-based economic growth, development, and poverty reduction.* During the past two decades or more, various policy approaches have been explored. In the "first-generation reforms," the World Bank Group and the International Monetary Fund (IMF), among others, focused on promoting the macroeconomic stability and trade integration of countries. Second-generation reforms moved from the broad policy environment to encourage more microeconomic changes, namely, improvements in the administrative, legal, and regulatory functions of the State. Of late, particular emphasis has been placed on the role of the public sector in establishing an "investment climate" conducive to promoting private sector-led investment, growth, and poverty alleviation.

The quality of a country's investment climate determines the risks and transaction costs of investing in and operating a business. These risks and costs are in turn determined by the legal and regulatory framework, barriers to entry-exit, and conditions prevailing in markets for labor, finance, infrastructure services, and other productive inputs. Essentially, the quality of the investment climate will determine the mobility and speed with which resources can be redeployed from lower to higher productive uses. For this to occur effectively, the nature and degree of competition in markets plays a pivotal role. In this regard, there is significant economic evidence suggesting that private investment has grown faster in countries with better investment climates. Also, economies with competitive domestic markets tend to attract more domestic and foreign direct investment, have higher levels and rates of growth in per capita gross domestic product (GDP), and lower rates of poverty.[1]

Promoting effective competition is often argued on grounds that it spurs firms to focus on efficiency and improve consumer welfare by offering greater choice of higher-quality products and services at lower prices. However, it also promotes greater accountability and transparency in government-business relations and decision making, and contributes to reducing corruption, lobbying, and rent-seeking behavior. Additionally, by lowering barriers to entry, it provides opportunities for broad-based participation in the economy and for sharing in the benefits of economic growth. Without effective competition, firms are more likely to possess considerable market power, which enables them to earn excess profits and wield political influence to tilt public policy in their favor. There are also likely to be distorted price and profit signals and increased risk of misguided investment and output decisions, which can lead to economy-wide repercussions.

The merits and benefits of fostering open and competitive markets have been recognized in many countries that have adopted various macro- and microeconomic reforms. However, there is wide variation in the economic growth and development of nations. Casual observations indicate that there is also a wide variation in the nature and extent of competition prevailing within and across countries. Moreover, notwithstanding the merits and benefits of competition, there is no consensus or widespread support for promoting competition within and across countries—especially developing nations. This stems in part from the lack of understanding or appreciation of what effective competition can

1. See ensuing discussion in Section 2 and World Bank 2005 and 2003.

tangibly contribute to the betterment of the lives of ordinary citizens, and in part from ideological differences and the influence wielded by vested interest groups in both government and the economy at large. Although the differences in the economic growth and development of nations cannot purport to be explained by the differences in the prevailing degrees of competition, this paper argues that it is one of the important, if not critical explanatory factors. It is well established that least-developed economies are encumbered by limitations of human and physical capital, governance and institutional structures, and other resource constraints. But they are also prevented from achieving their potential by various types of public policy-based and private sector anticompetitive business practices. The primary message of this paper is that these countries need to take concrete, consistent, and coherent measures to integrate and promote effective competition policy as part of their overall government economic and regulatory framework. An effective competition policy should be viewed as the "fourth cornerstone" of this framework—along with sound monetary, fiscal, and commercial (international trade) policies.

Competition policy refers to those government measures that directly affect the extent of rivalry between enterprises and the structure of industry. Competition policy typically includes both policies that enhance competition in local and national markets (such as liberalized trade policy, relaxed foreign investment and ownership requirements, and economic deregulation) and competition law (also referred to as antitrust or antimonopoly law) designed to prevent anticompetitive business practices by firms and unnecessary government interventions in the marketplace.[2]

The lending and nonlending advisory services of the World Bank Group (and IMF) have paid relatively scant attention to promoting competition law-policy in client countries. While many of the suggested policy measures such as trade and investment liberalization, simplification and reduction of the costs of regulation such as "Doing Business" reforms,[3] and privatization are pro-competition, they are insufficient. These measures primarily change the role of the public sector in the organization and conduct of economic activity, and they appropriately pave the way for an increased and less-encumbered role for the private sector. But these measures do not address the restrictive business practices and rent-seeking behavior of the private sector. The latter can have an adverse impact on the benefits that flow from the competition that other regulatory reforms promote.

Some "schools" of thought and commentators question the need to enact a specific competition law and argue that private sector firms cannot engage in anticompetitive business practices if open competitive markets are promoted by lowering barriers to trade, investment, and entry. Any rents that incumbent firms earn will be quickly eroded by the emergence of new competitors seeking to also earn high profits. There are intertemporal and cross-section industry studies that indicate that with tariff reductions and resulting increased import competition, the profit (price-cost) margins of domestic firms decrease. However, case- and industry-specific studies indicate that domestic firms and markets can remain insulated from international competitive pressures due to factors such as high transportation costs, nontradable products and services, perishable goods, and business strategies such as exclusive dealing, foreclosure of important sources of inputs and distribution channels,

2. See Khemani and Dutz (1996). Presently, more than 100 countries have competition legislation. More than half of these nations have adopted or strengthened such policies since the early 1990s, but effective implementation varies because of factors such as inadequate resources, administrative capacity, and political support. See also the discussion in Section 5.
3. World Bank (2007 and earlier years) "Doing Business" reports are at http://www.worldbank.org and http://www.doingbusiness.org.

product standards, various domestic regulations, and international cartels. Moreover, the business environment prevailing in least-developed countries is fraught with problems that raise barriers to entry: lack of enabling physical and business infrastructure, underdeveloped financial (debt-equity) markets, informational asymmetries and the like, as well as anticompetitive practices and lobbying by large incumbent firms, which often have close connections to government and politicians. There is an inherent tendency among firms—whether in advanced industrial or developing economies—to avoid the inconvenience of competition and monopolize markets to earn higher profits wherever possible. Such tendencies need to be curbed to promote merit-based competition.

While economic deregulation and lowering of barriers to trade and investment fosters competition, the competitive process also needs to be *protected and promoted*. This is the role of an effective competition law-policy. It provides for a system of checks and balances so that businesses are free to pursue legitimate commercial interests, consumers including other business firms are not exploited, and both government and business adopt good "market governance" principles. An effective competition law-policy includes a set of instruments that buttress a healthy investment climate, thereby contributing to investment, productivity, and broad-based economic development. To further elaborate on these points, the ensuing discussion is organized as follows: Section II discusses the implications of high product market and ownership concentration, governance, and institutional characteristics frequently observed in developing countries that have an impact on competition. Section III presents empirical information on the pro-growth and pro-poor benefits that arise from increased competition. Section IV discusses constraints that business faces in operating in developing countries. Section V describes the nature and type of alleged anticompetitive business practices encountered in developing countries, and Section VI concludes the discussion and offers some recommendations that the World Bank Group, in partnership with other international organizations and donors, could consider in strengthening and promoting effective competition policy in recipient countries.

2. INTERPLAY AND IMPLICATIONS OF HIGH PRODUCT, OWNERSHIP AND FINANCIAL MARKET CONCENTRATION

Most developing and transition market economies (including the previously high-performing nations in East Asia) have a number of common structural, institutional, and governance characteristics that include the following:

- High levels of domestic product market concentration, barriers to entry and trade, and a low degree of interfirm rivalry-competition. While the liberalization of markets for goods and services is on the rise, the inherent structural features of high product market concentration tend to change slowly due to past government policies and interventions such as industrial policy, tariff protection, licensing, preferential procurement, and the like, as well as the relatively small size of domestic markets in most developing economies and underdeveloped capital markets.
- High levels of ownership concentration and inadequate corporate governance regime. In many developing and emerging market economies, major corporations are family owned or controlled by small group of influential investors. They also tend to have conglomerate holdings with extensive direct and indirect (pyramid) ownership structures, buttressed by non-voting shares and interlocking directorates. Outside shareholders tend to have minority positions, without recourse to adequate information disclosure requirements, security regulations, and related safeguards for their investments. The family or closely held enterprise groups loom large not only in specific markets but across the economy as well, resulting in high levels of aggregate concentration.[4]
- "Missing middle"-size firms. Industries and markets tend to be dominated by a few large firms, and many small-size (marginal) firms that rarely survive and grow to medium/larger sizes. The missing middle is attributed to a range of factors, such as lack of access to financial and managerial skills, and anticompetitive business practices by large incumbent firms.
- Lack of an effective "market for corporate control," that is, the process by which inefficient firm management is displaced through mergers and acquisitions. This is due in part to policy-based restrictions against foreign ownership and "reserved" lists of economic sectors, and in part to high levels of ownership concentration.[5]

4. See Prowse (1998) and Claessens (1998). Various studies relating to developing and emerging market economies indicate the concentration of wealth and industry. In Pakistan during the 1960s, 22 mainly family-owned businesses controlled 66 percent of industrial assets and 87 percent of the banking and insurance assets. Forty-three families closely owned and/controlled 53 percent of the companies listed on the Karachi Stock Exchange, and the average four-firm concentration ratio was 70 percent in the 82 industries that accounted for the bulk of industrial production (see CUTS [Consumer Unity and Trust Society] [2002]). In the Philippines, 22 family-controlled groups account for 63 percent of the stock market capitalization, and purportedly dominate the congress and government economic policies (see Coronel [2004]). In Indonesia, former President Suharto and his extended family along with selected politicians and businessmen controlled virtually every significant financial and industrial sector in the economy. Until the economic-financial crisis in the late 1990s, the top 30 Korean chaebols (conglomerates) dominated every sector of the economy except agriculture. They owned or controlled roughly two-thirds of the 100 largest manufacturing firms and about 40 percent of manufacturing GDP, 16 percent of total GDP, 50 percent of exports, and 15 percent of commercial bank loans (see Yoo [1998] and Yoo and Lim [1997]). In nine East Asian economies, for example, a survey of nearly 3,000 firms indicates that more than 50 percent are controlled by a single shareholder. High levels of industry, aggregate, and ownership concentration also exist in Argentina, Brazil, Chile, and Mexico, as well as the formerly socialist and recently privatized industrial sectors in economies such as in Russia. Although more up-to-date information on concentration and ownership is not easily obtainable, studies of other countries suggest that such structural patterns change very slowly over time, and these and other developing and emerging market economies are likely to be still highly concentrated.

5. Restrictions on foreign ownership and contested (hostile) takeovers remain in several developing countries. In many spheres of economic activity, firms require government permission or licenses to enter or conduct business. As the World Bank's *Doing Business* reports indicate, starting and registering a business, dealing with licenses and labor laws, enforcing contracts, obtaining credit, etc., impose inordinate delays and costs—especially in the least-developed economies.

While the direction of causality between these sets of factors is open to debate, they tend to be *mutually re-enforcing* and give rise to inflexible, inefficient, and anticompetitive industrial and financial/capital market structures.

In a number of economies, high levels of industry or product market concentration may be the result of the small size of the domestic market relative to efficient scale of production, so that there is room for only a few firms. It could also be attributable to lack of an effective competition law-policy that prevents monopolistic business practices and mergers and acquisitions. Aggregate and ownership concentration may have initially arisen due to market and institutional failures and gaps such as absence of well-developed markets for credit and other inputs; paucity of relevant information and intermediaries; and an inadequate legal system for protection of property rights, resolving disputes, and enforcing contracts. This would necessitate enterprises to internalize many of these functions to minimize transaction costs and risks.[6] High industry and ownership concentration levels may have also arisen due to preferential treatment by and industrial policies of government. Regardless of these underlying explanatory factors, which vary across economies, the observed high levels of concentration create "incumbency benefits" for firms and make markets less easily contestable by new entrepreneurs.

High levels of product market concentration and weak competition generally result in high (monopoly) prices and profits. With easy, if not assured profits and preferential treatment by governments, incumbent firms have little or no incentive to use resources efficiently. At any given time, firms insulated from competition generally incur costs that are higher than what would be sustainable under the best technical and managerial practices. Over time, these losses are compounded by the misallocation of resources and "x-inefficiencies" stemming from monopolistic output levels, and managerial and organizational slack. However, in spite of these costs, these firms may still produce satisfactory operating and financial results, and attract foreign investment and joint ventures as they know local market conditions and may have greater access to policy decision makers than do new domestic firms. High prices and profits can mask high costs and poor investment decisions.[7]

High profits also provide increased incentives for entrenching the observed high levels of ownership concentration.

> *Why would owners give up ownership control when on a risk-adjusted basis they can earn higher returns (that is, rents) in markets insulated from competitive pressures?*

VESTED INTERESTS THWART COMPETITION

While some argue that high ownership concentration is conducive to resolving or minimizing the "principal-agent" problem, that is, ensuring corporate management (agents) acts in the best interests of a firm's owners

6. In this regard, a stream of theoretical and empirical studies examine different hypotheses. See, for example, Khanna and Palepu (2000a and 2000b) and various citations therein.
7. Glen et al. (2003) examine the persistence of profits of large firms across seven developing countries (Brazil, India, Jordan, Korea, Mexico, Thailand, and Zimbabwe) over the period 1980–1995 and draw some comparisons with results relating to advanced industrial countries. Counterintuitively, they find that both short- and long-term persistence of profits is lower, suggesting competition is equally if not more intense than in advanced countries. However, the sample is restricted to analysis of only 339 firms across the seven economies for which time-series data could be obtained, and the firms differ across countries in their industrial composition. Moreover, there is a selection bias in that the analysis does not cover firms that may have entered and exited during the period of analysis. The results, while interesting, cannot be interpreted as characterizing competition in the least-developed countries, most of which do not have functioning stock markets.

(principals) by maximizing shareholder value, this argument applies only when ownership and management are separate. When owners actively manage the firm, they can exploit minority shareholders or outside investors, engage in moral hazard behavior by passing on the risks and costs, and pursue various non-economically viable objectives such as catering to their prestige and egos. In addition, high levels of ownership concentration entrenches owner-managers and limits the extent to which the market for corporate control can act as a disciplinary force on their performance. In these circumstances, it is difficult to change ownership and control of a corporation through mechanisms such as mergers and acquisitions so as to redeploy resources from lower- to higher-valued uses. It also undermines the development of a separate cadre of professional managers, as owner-managers appoint extended family members to key management positions.[8] Such situations provide little incentive for domestic and foreign direct investment. They also preclude the benefits that tend to accrue in terms of diffusion of new knowledge, technology, organizational methods, product innovation, productivity, and competitiveness.

The commercial advantages of large, closely held incumbent firms are not lost on banks and other financial institutions, which play a predominant role in financial intermediation in developing countries. Banks maintain cozy relationships with established and often well-connected businesses—a natural outcome in a protected and profitable business environment in which both the borrowers and the lenders operate. In some countries, commercial firms also own and control major domestic banks, creating business conglomerates with "in-house" sources of easy financing for themselves. For example, some of these practices contributed to the high leverage of leading firms in East Asia, as well as the widespread corporate distress and banking failures during the financial turmoil of the late 1990s. More generally, preferred access to bank credit significantly reduces the need of incumbent firms to rely on securities markets where external financiers often demand transparency and accountability of corporate insiders. And when outside nondebt capital is required, restricted or nonvoting and preferred shares are issued.[9]

Inadequate competition limits access to capital by new or small businesses. The lack of fair competition results in lower profits and retained earnings as internal sources for financing growth. Lenders and investors understandably prefer more-established firms with significant business advantages. Over time, the industrial structure may become skewed, with a few large conglomerates dominating the economy and a large number of small firms struggling to overcome scant prospects for growth. There emerges the missing middle that is observed in the size distribution of firms in many developing economies. A report by the United Nations Conference on Trade and Development (UNCTAD) points out many of the difficulties that small firms face in least-developed economies; these include business networks that provide support for insiders and make it more difficult for outsiders to enter particular activities or markets; networks

8. In Korea, 29 of the 30 chaebols were (and most still are) family controlled. In many cases, chaebol owners are interlinked via marriages, interlocking directorates, cross-holdings, and investments. Marriages also cement links with senior government officials. Cummings (1997) points out that fully one-third of chaebol owners' sons or daughters were married to high-ranking government officials. In India, most of the 50 largest industrial groups are family owned according to Pramal (2003). See World Bank "Doing Business" reports, op cit.
9. Singh (2003) finds that stock markets in developing countries grew rapidly between 1980 and 1995 and contributed significantly to corporate growth through issuance of primary stock; this growth diminished in the post-1995 period. However, the analysis is based mainly on large economies such as India, Korea, and Thailand, which have reasonably well-functioning stock markets, and the findings do not apply to the least-developed countries, the focus of this paper.

that limit competition and lead to unproductive entrepreneurial activities; and inability to tap into capital markets or to face very high rates on borrowing.[10]

As indicated above, owners of incumbent firms have an incentive to retain control of profitable domestic operations. They may chose to remain private or go public without giving up control by retaining a controlling stake or issuing nonvoting shares. Available data suggest that a higher share of leading firms remain private in less-competitive markets. Even within the group of publicly traded companies, a higher proportion of closely held firms are observed in less-competitive economies.[11]

Regulatory and private restraints on the competitive process have deeper ramifications. Because existing firms tend to be relatively large in size and few in number, they have definite organizational and financing advantages in influencing the government's legislative and regulatory agenda. In more advanced countries, where there is a depth of informed opinions, competing interests, and independent media, powerful commercial interests may not always prevail. In most developing countries, competing opinions are more limited. In this context, interest groups are more likely to succeed in furthering their own agendas.

The close connection between economic power and political influence is generally recognized. Incumbent firms often use their political influence to entrench their market and ownership positions. For example, domestic bankers in many countries have successfully resisted introduction of competition and entry by new domestic and foreign banks. Even in the stress of a financial crisis, major conglomerates in East Asia were able to water down unfavorable reforms and stretch out the onset of implementation. Public sector enterprises are no exception. Difficulties in privatization programs have been encountered over a wide range of cultural and economic environments, for example, from Ghana to India and Thailand.

Another concern is that, with distorted prices that guide business decisions, the pursuit of profits may be detrimental to social welfare. Operations that are profitable when based on domestic prices may actually produce a loss when the inputs and outputs are valued at world prices. This certainly has been the case with many commodity monopolies in Africa and politically connected conglomerates in East Asia.

Rajan and Zingales (2003) state that:

> *"The corrupt version of capitalism—when powerful corporations deliberately try to eliminate healthy competition to preserve their privileged position—generates economic inefficiencies and social injustice, thereby undermining political support for the free-market based system…."*[12]
> *They also observe that: "…while everyone benefits from competitive markets, no one in particular makes huge profits from keeping the system competitive and the playing field level….Without a strong political constituency supporting them and under the continuous pressure of vested interests markets are always too restricted, never too free."*[13]

10. See UNCTAD (2006).
11. See Khemani and Leechor (2000).
12. See Rajan and Zingales (2003).
13. In Crown Business Books (2003: 311), the authors argue that access to competitive financial markets is perhaps the most critical factor to sustainable economic development. Vibrant financial markets threaten the sclerotic corporate establishment and increase corporate mobility and opportunity, which translates into personal freedom and economic development for more people. Elites restrict access to capital and severely limit not only economic development but also that of individuals. In the end, such vested interests backfire as the excuse for suppressing competition to reduce risk, and they result in lack of innovation and exposure to market downturns.

Among the major impediments to development identified by the authors is access to competitive financial markets.

Access to finance as a major constraint to the operations and growth of firms was also identified in the World Bank's assessment of the investment climate across countries and regions around the world—especially in Africa and South Asia.[14] Other constraints included anticompetitive business practices, which tended to have greater impact on small- and medium-size firms.[15] The importance of the role of effective competition law-policy becomes heightened in the context of the economic structural, governance, and other characteristics prevalent in the developing countries discussed above.

14. See Batra et al. (2003).
15. Ibid: Chapter 2.

3. PRO-POOR BENEFITS OF COMPETITION AND ECONOMIC GROWTH[16]

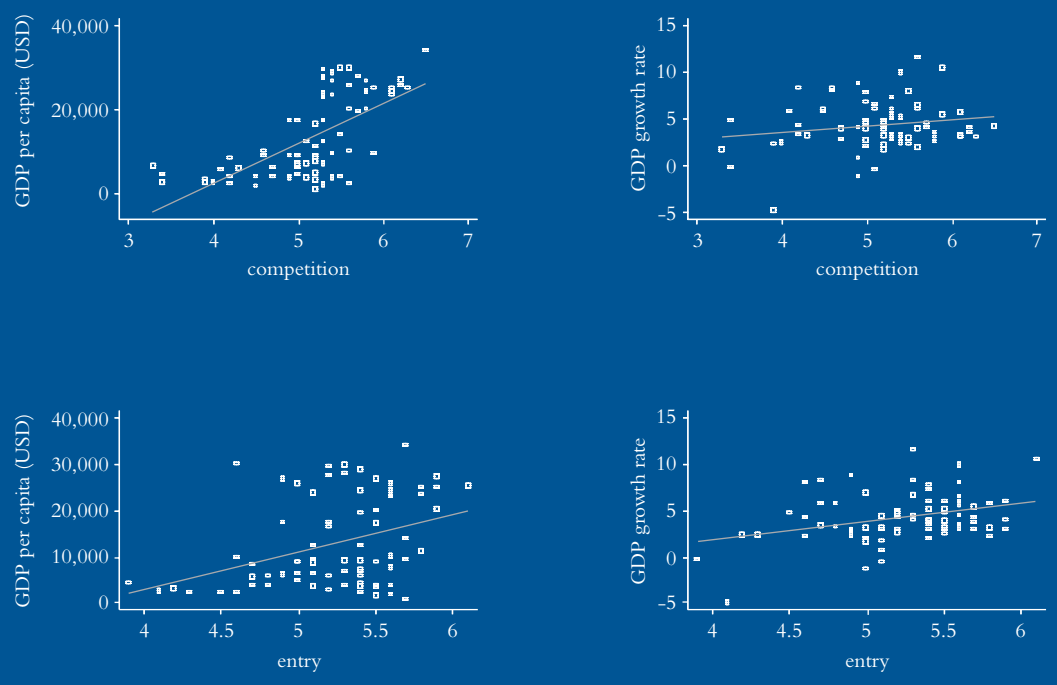
The World Bank's Global Economic Prospects Report (2003) points to the pro-growth and pro-poor benefits of competitive markets. Research conducted for the report indicates that economies with competitive domestic markets generally tend to have higher levels and rates of growth in per capita income. Entry of firms plays an important role in the competitive process (see figure 3.1). These economies also have lower rates of poverty and attract more domestic and foreign investment. This research is consistent with the broad empirical finding that barriers to competition impede innovation, growth, and prosperity.[17]

In a complementary fashion based on the detailed study of individual industries and companies worldwide, William Lewis and his colleagues at McKinsey & Company document how undistorted competition in product markets is the most important long-run determinant of productivity, and hence prosperity. Neither education nor lack of capital appears to be a binding constraint on productivity. Direct investment by top-class companies can readily overcome obstacles such as low levels of education or scarce local capital and allow workers to reach world-class productivity levels if allowed to do so through open markets and a level playing field where efficiency and innovation are appropriately rewarded.[18] The emergence of India as a major global center for automotive design as well as manufacture of cars and components in a short number of years as the result of an explicit set of policies to promote competition in this sector is illustrative of the potential productivity benefits of competition (see box 3.1).[19]

The increased competition and investment have also given rise to increased employment in the automotive and other sectors such telecommunications, consumer durables, domestic airline services, and IT (information technology) software industries in India.[20] More generally, the increased employment and lower prices that result from increased competitive pressures expand markets and make goods and services more affordable. Indeed, various studies suggest that, when there are

16. The discussion in part is derived from Dutz and Khemani (2007).
17. See among others Baumol (2002), Easterly (2001: Chapter 9), and Klein (2003).
18. See Lewis (2004).
19. It should be noted that while India liberalized investment and entry into the automotive sector, it continued to maintain high levels of tariffs and instituted domestic content regulations. However, such policies did not limit competition in the domestic market given its large size relative to efficient scale of production, new entry and the number of competing firms, and pent-up high demand for better-quality vehicles. While such "industrial policy or strategy" may be possible for large economies such as India, the same options are not available for economies with smaller domestic markets. In this regard, Malaysia and its troubled state-supported automobile manufacturer Proton would be an example. Also, large domestic market size does not necessarily ensure success. According to McKinsey & Company, Brazil's car industry stagnated until the mid-1990s due to tariff protection and lack of competitive rivalry between firms. With gradual reduction in tariffs, productivity increased on average by 16 percent per year. A policy of tariff reductions is also recommended for the Indian automotive sector in order to reap the full benefits of competition. If followed, the Indian automotive sector could reach 80 percent of the U.S. benchmark productivity levels by the year 2010 (see McKinsey & Company [2001]). Economies with relatively small domestic markets can also have internationally competitive industrial firms. A case in point would be Sweden with such firms (among others) as Saab, Sandvik, SKF, and Volvo that have based their success on reputation for high quality, durability, and well-engineered products. Productivity gains in these firms were garnered through competition in export markets.
20. That increased competition can also result in unemployment is not questioned. Analysis by Auer Islam (2007) points out that there is a tendency for employment intensity to decline with economic growth; it varies across industries, in magnitude, and over time, and no specific sectors need to be targeted for special measures. However, the analysis recommends a mix of general policies for employment security including investment in training. Such approaches are not in friction with competition policy.

FIGURE 3.1: COMPETITION, ENTRY, AND ECONOMIC GROWTH



Sources: World Bank Economic Forum and World Bank SIMA Indicators. "Competition" is the average response in each country to the question "In most industries, competition in the local market is (1=limited and price-cutting is rare, 7=intense and market leadership changes over time)." "Entry" is the average response to the question "Entry of new competitors (1=almost never occurs in the local market, 7=is common in the local market)."

unnecessary regulatory impediments and insufficient competition, the poor often pay higher prices and receive lower-quality goods and services than the more affluent segments of society.[21]

Not all countries in the sample in figure 3.1 necessarily have adopted specific competition law-policy. Moreover, recent legislation enacted in countries as diverse as Egypt, India, Malawi, and Mongolia (among others) has yet to come into full effect. As indicated earlier, measures such as trade and investment liberalization and deregulation can give rise to competition in the domestic economy, whether or not specific competition law-policy is in place. And enactment of competition law does not necessarily result in competition. However, having a

21. See for example the World Bank (2004) report that there was improved quality and delivery of food grains at lower prices when competitive market-oriented measures were introduced in the state-dominated food distribution system. Other studies by the World Bank Group and various development organizations also point out that the poor pay more or receive lower quality for such services as water, sanitation, electricity, and even primary school education than do residents in the formal city.

BOX 3.1: THE BENEFITS OF INCREASED COMPETITION: THE CASE OF INDIA'S AUTOMOBILE INDUSTRY

Notwithstanding their partial nature, India's 1991 economic reforms and subsequent sectoral liberalization fostered increased domestic and foreign investment, growth, and competitiveness. Nowhere is this more evident than in the automobile industry, which as of 2002 permitted foreign direct investment up to 100 percent for the manufacture of automobiles and components, with no minimum capital investment required for new entrants. Once characterized by the Economist as producing outdated 1940s' models referred to as "fossils on wheels," today the automobile industry accounts for:

- **Four percent of GDP, up from 2.8 percent in 1992–93.**
- **More than $13.5 billion in investments.**
- **More than 1.12 million automobiles produced annually, compared with 264,000 in 1994–95.**
- **More than $21.6 billion in annual turnover of automobile sales.**
- **Direct employment of half a million workers and indirectly 10 million, compared with less than 100,000 before.**

While two decades ago Indian automobile customers waited for up to five years or more, today they have a plethora of models to choose from in all price ranges, from economy to luxury cars. Abroad, the Maruti Alto hatchback, manufactured in collaboration with Suzuki, accounts for 19 percent of the small cars sold in the Netherlands. India also has become a significant exporter of automotive parts.

The benefits of intensive competition and increased investment have also stimulated innovation. Mahindra & Mahindra spent only $120 million to develop its fast-selling Scorpio model—one-fifth of what it would cost in Detroit. Similarly, Tata Motors developed its Indica model for $340 million, compared to a global development benchmark cost of $1 billion. As a result, India has emerged as major global center for automotive design as well as manufacture of cars and components.

Source: Evalueserve 2006

competition law in place signals to firms and markets that certain business behaviors and commercial practices, as defined in the law, are illegal. It confers rights and obligations on transacting parties and provides for due process to resolve disputes and obtain relief from anticompetitive practices.

In this connection, cross-country analysis by Dutz and Hayri (1999) found that "perceived" effectiveness of competition policy helps to explain differences in economic growth beyond the variables conventionally used in models of economic growth. Dutz and Vagliasindi (2000) found that effective implementation of competition law-policy in transition market (former centrally planned) economies of Europe and Central Asia have a robust positive relationship with expansion of more efficient private sector firms.

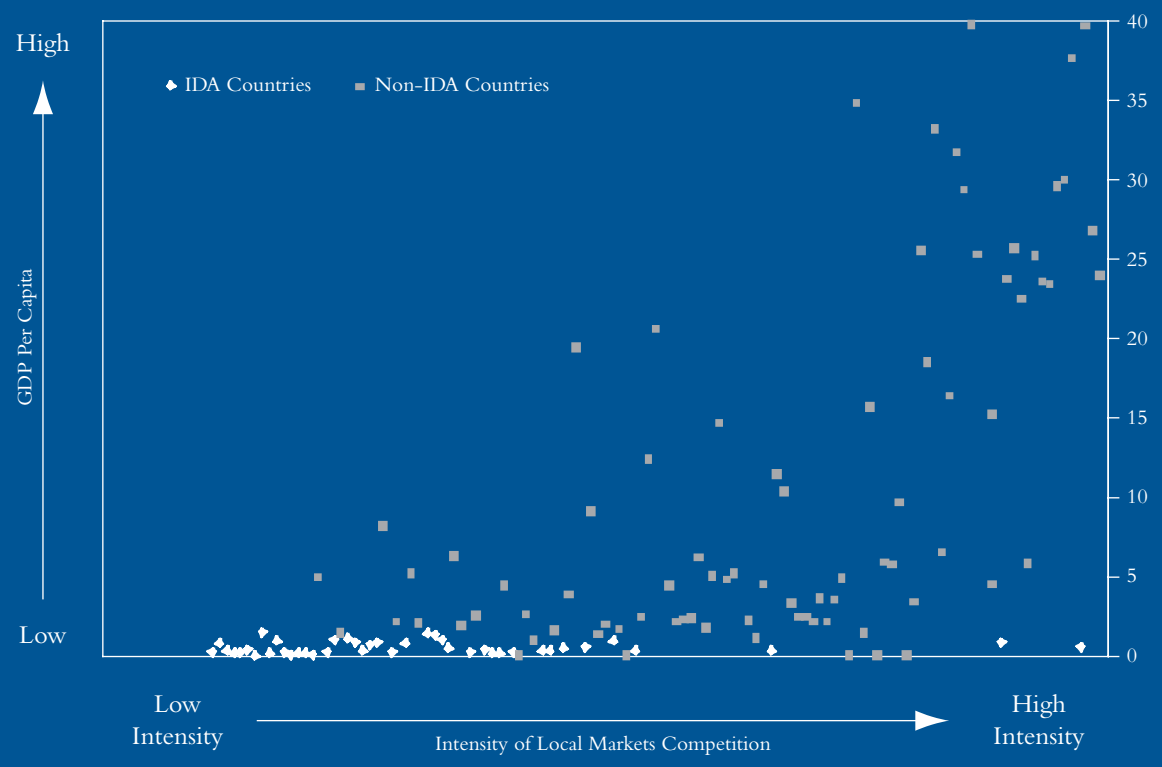
Data derived from the World Economic Forum's *The Global Competitiveness Report 2006–2007* provide further evidence of the importance of competition, and competition (antitrust) law-policy, in fostering higher incomes,

broad-based markets (less-dominant firms) and global competitiveness (see figures 3.2 to 3.5). The data are derived from "perception surveys" of opinions of policymakers, business executives, and various officials in public and private sector organizations, including academia. The responses, collated and computed into various indicators, do not actually measure factors such as volume of trade, magnitude of intensity of local competition in terms of prices and firm turnover, and effectiveness of competition (antitrust) law-policy implementation in terms of number of cases handled and resolved, etc. Nonetheless, the indicators are useful, as they are based on the views of key individuals who are aware of the array of issues that have an impact on competitiveness in their respective countries.[22]

Figure 3.2 indicates that the least-developed (based on International Development Association [IDA] ranking) countries,[23] which tend to have low levels of per capita GDP, also have low intensity of competition in local markets.[24] The majority of these countries tend to cluster together. While a few have a higher degree of local market competition, this does not necessarily translate into higher per capita incomes, probably due to other constraints in their business environment. In recent years, many least-developed countries have experienced higher rates of economic growth. However, various reports point out this growth is fragile and primarily commodity driven. It has not led to creation of productive capacities and industrial upgrading. Figure 3.3 indicates that these countries also tend to have less-effective competition (antitrust) law-policy,[25] which probably explains why local markets are dominated by few large firms. These economies also rank lower in terms of the business competitiveness index (figure 3.4), which is positively associated with effectiveness of competition (antitrust) law-policy. Finally, figure 3.5 suggests that the intensity of competition in local markets and effectiveness of competition (antitrust) law-policy tend to be positively correlated. As the discussion in the preceding section postulates, these characteristics of least-developed economies result from the interplay and mutual re-enforcement of market dominance of large firms, weak state of competition in local markets and resulting lack of business competitiveness. The data pertaining to non-IDA countries, where these factors tend to have higher correlations, suggest that this cycle could be broken by an effective competition (antitrust) law-policy.

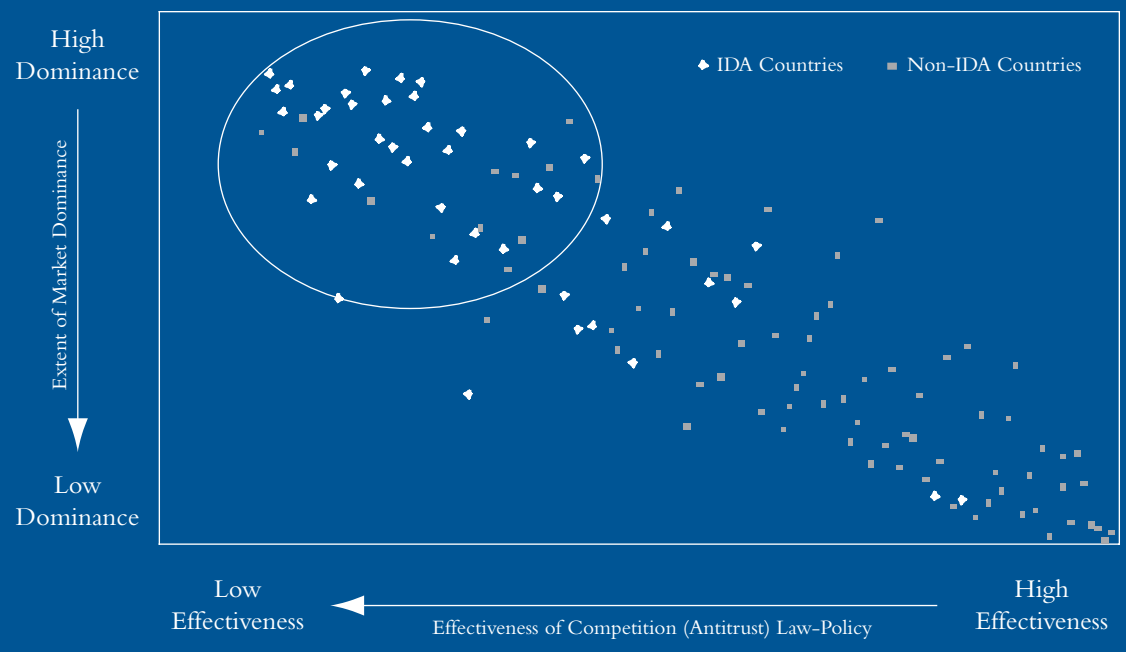
22. For further information on the construction of these indicators, including the Global Competitiveness Index see Auer and Islam (2007: Chapter 1.1).
23. IDA provides interest-free (credits) and grants to the poorest developing countries in order to boost their economic growth and improve living standards. The list and regional distribution of these countries is in the appendix, table A-2.
24. In this and subsequent figures, the main outlier countries are India, Indonesia, and Kenya. This may be the result of the perception bias of the respondents. For example, India currently does not have an effective antitrust law—the Competition Act amendment bill is before Parliament and has yet to come into full effect. However, there is a markedly high intensity of competition in local markets, in part because of the relative large size of the domestic economy and number of firms. Indonesia has had a new competition law in force since 2000, with an autonomous competition commission that has investigated a number of cases in the fertilizer, cement, retail, paper, insurance, and other sectors. Its domestic economy is also relatively large, which sustains a number of rival firms, though the competition commission has confronted difficulties in areas such as getting information and collection of fines. In 1990, Kenya updated and replaced earlier legislation on prices and related matters with a Restricted Trade Practices and Control of Monopoly Prices. Commentators have pointed to the need for Kenya to have a well-resourced, independent competition authority and greater harmonization with overlapping sector-specific laws that are less pro-competitive. Even so, the Monopoly and Prices Commission has investigated and prosecuted a number of cartels, other types of restrictive business practices, and merger-and-acquisition transactions.
25. See UNCTAD (2006).

FIGURE 3.2: INTENSITY OF LOCAL MARKET COMPETITION AND PER CAPITA GDP



Source: Global Competitiveness Report 2006–2007 and World Bank DDP, 2005

FIGURE 3.3: EFFECTIVENESS OF COMPETITION (ANTITRUST) LAW-POLICY AND THE EXTENT OF MARKET DOMINANCE

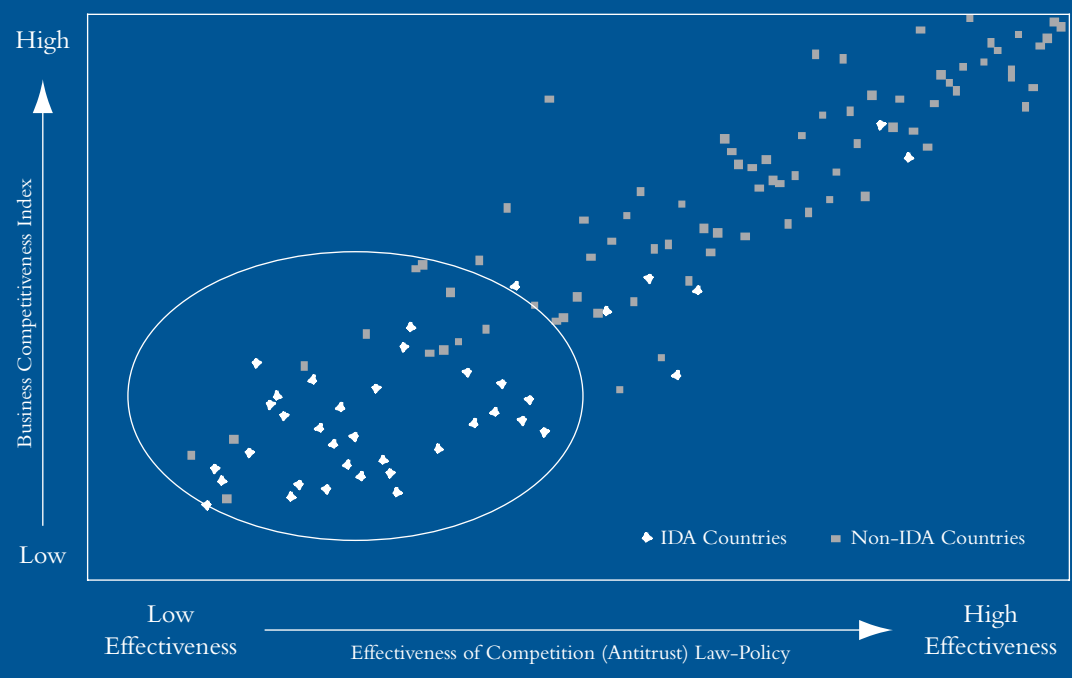


Source: Global Competitiveness Report 2006–2007

RANK CORRELATIONS

IDA	n = 43	rs = - 0.7201
Non-IDA	n = 82	rs = - 0.8626
All countries	n = 125	rs = - 0.79866

FIGURE 3.4: BUSINESS COMPETITIVENESS INDEX AND EFFECTIVENESS OF COMPETITION (ANTITRUST) LAW-POLICY

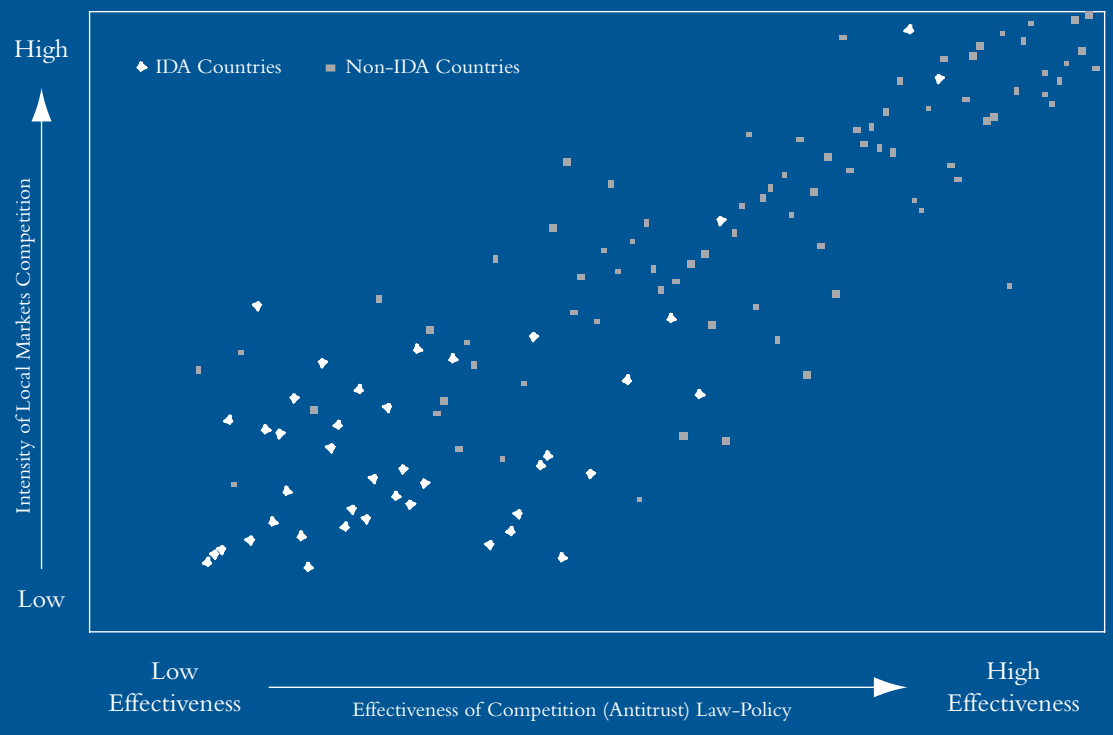


Source: Global Competitiveness Report 2006–2007

RANK CORRELATIONS

IDA Countries	n = 39	rs = 0.61
Non IDA	n = 80	rs = 0.90
All Countries	n = 119	rs = 0.92

FIGURE 3.5: INTENSITY OF LOCAL MARKETS COMPETITION AND EFFECTIVENESS OF COMPETITION (ANTITRUST) LAW-POLICY



Source: Global Competitiveness Report 2006–2007

RANK CORRELATIONS

IDA Countries	n = 42	rs= 0.42
Non IDA	n= 82	rs= 0.84
All Countries	n = 124	rs= 0.86

Michael Porter, in *The Competitive Advantage of Nations* (1990), observed that:

> *Few roles of government are more important to the upgrading of an economy than ensuring vigorous domestic rivalry. Rivalry at home is not only uniquely important to fostering innovation but benefits national industry…In fact, creating a dominant domestic competitor rarely results in international competitive advantage. Firms that do not have to compete at home rarely succeed abroad. Economies of scale are best gained through selling globally, not through dominating the home market.* (page 662)

The role of government in promoting competitive rivalry has been and continues to be debated among policy makers and advisors, academic researchers, and others—especially in regard to the degree of protection and direct support that governments should accord to business. A commonly cited example is the success of the East Asian "miracle" economies of Japan, Korea, Malaysia, and Singapore, where governments provided "administrative guidance" and departments such as Japan's Ministry of Trade and Industry encouraged cartels and mergers and granted export credits to stimulate productivity and dynamic efficiency. However, even proponents of fostering competitiveness and economic growth recognize that maintaining oligopolistic rivalry instead of concentrating resources and subsidies on a single or few selected "national champions" was a critical part of the industrialization strategy.[26] Porter along with Japanese researchers revisited the "government-led model" by examining in-depth a sample of 20 internationally competitive sectors and seven uncompetitive ones in terms of the nature, timing, and extent of government interventions. They found that the government-led model with major subsidies was almost entirely absent and found little evidence of interventions in competition.[27] Indeed, even casual observations in products such as electronics, automobiles, and consumer durables indicate that there is vigorous interfirm rivalry between Korean and Japanese firms in their respective home markets as well as abroad. And in recent years, in both these economies as well as Singapore, vigorous enforcement of competition law-policy has become central to reviving their economies.

Recently, Porter et al. has reiterated the importance of interfirm rivalry and competition in domestic markets, among other dimensions of the business environment such as quality of infrastructure, removal of trade barriers, protection of property rights, and regulatory standards for promoting competitiveness and economic growth.[28] These and other microeconomic factors combined are found to account for more than 80 percent of the variation in per capita GDP (on a purchasing power parity basis). Decomposing the Global Competitiveness Index and applying bivariate analysis, Porter reports several other interesting results. The intensity of local competition accounts for about 42 percent (adjusted R-squared) of the variation in GDP; effectiveness of competition (antitrust) law-policy 65 percent, and complementary factors such as presence of demanding regulatory standards 78 percent, property rights 72 percent, judicial independence 59 percent, and trade 33 percent. Clearly, while competition and competition (antitrust) law-policy are important, so are other factors—which combined form the physical and business infrastructure of a modern economy. As one would expect, variation

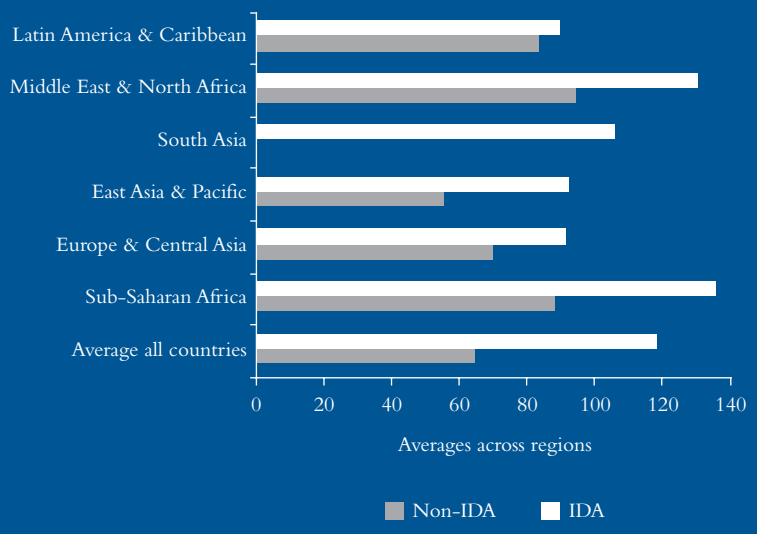
26. See, for example, Amsden and Singh (1994).
27. See Porter et al. (2000).
28. See Porter et al. (2007).

exists across countries depending on their income and stage of economic development. Analysis of country/economy groups conducted by Porter et al. indicate that factors such as intensity of local competition, effectiveness of competition (antitrust) law-policy, trade, efficiency of legal framework, and presence of demanding regulatory standards are insignificant in low-income countries, less so in middle-income countries, and not at all in high-income countries. These results should not be interpreted as indicative of the unimportance of policies (and institutions) relating to competition, but rather the opposite. As discussed earlier, the inherent ownership, industrial and financial market, and governance structures in least-developed countries coupled with inadequate physical and business infrastructure makes it difficult to foster competition. Also, as the discussion below suggests, effective implementation of competition law-policy in least-developed economies is lacking. The process of competition is not automatic, and takes time to develop—even in more-developed economies. It is dependent on both business environment and institutional factors.

4. INVESTING AND "DOING BUSINESS" IN DEVELOPING COUNTRIES

The degree to which business environments allow entrepreneurs to engage in profitable and productive economic activity varies considerably across countries. A survey of the investment climate conducted by the World Bank (2003) found that across nations, whether they are Organisation for Economic Co-operation and Development (OECD) members or developing countries, enterprises identified the principal constraints to investing and conducting business as taxes and regulations, financing, policy instability and uncertainty, and inflation. Enterprises in developing countries also ranked corruption and inadequate infrastructure among the leading constraints. There were also salient regional differences: In South Asia, respondents identified street crime as a constraint; in Africa, respondents identified infrastructure. About 46 percent of survey respondents also indicated anticompetitive policies and business practices as an important constraint. The highest percentages of respondents mentioning this were in Bangladesh (58 percent), Indonesia (62 percent), Krygyz Republic (72 percent), Pakistan (57 percent), Philippines (66 percent), and Turkey (62 percent).[29]

FIGURE 4.1: EASE OF DOING BUSINESS RANK, 2006



Source: Source: World Bank (2007) "Doing Business Report."
Note: Higher ranking implies greater difficulties in doing business. All countries in South Asia are IDA members.

More recent World Bank surveys indicate that it is easier to do business in developed, industrial countries than in developing countries. The Ease of Doing Business Index is computed using a number of factors, namely, the time (days), costs, and number of procedures that it takes to start a business, deal with licenses, get credit, export and import, close a business, employ and fire workers, and deal with other business-related issues.[30] Figure 4.1 and tables A-1 and A-2 in the appendix present information on the average rankings of selected indicators across regions and globally for IDA and non-IDA countries. A higher rank indicates greater difficulty. For example, figure 4.1 indicates that on average it is almost twice as difficult to do business in IDA countries than in non-IDA ones. Also, doing business is more difficult in the poorer regions of South Asia, sub-Saharan Africa, and the Middle East and North Africa.

Tables in the appendix suggest that some of the factors underlying these averages, namely, the time, number of procedures, and costs of meeting the various regulations, range widely across countries and regions. For example, in Equatorial Guinea, 20 procedures need to be com-

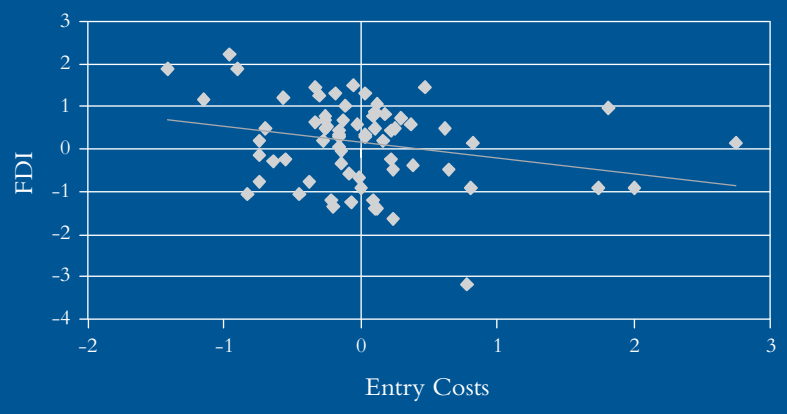
29. See Batra et al. (2003).
30. Refer to World Bank (2007) *Doing Business* for more information. These measures are also described in the notes to tables A-1 and A-2 (in appendix) of this paper.

pleted to start a business whereas Australia, Canada, and New Zealand require only two. In Suriname, it takes 694 days to complete business start-up procedures; in Australia it takes two days, and in many other advanced industrial countries between two and eight days. Developing countries also tend to require more licenses to conduct even general activities. The number of procedures for obtaining licenses is highest in Sierra Leone (48), Taiwan-China (32), and Egypt (30). Hiring and letting go of workers, and closing a business also can be difficult and costly: In Egypt, laid-off workers receive 186.3 weeks of wages, and in Zimbabwe, 446.3 weeks. Closing a business in Chad and India can take up to 10 years.

As Figure 4.2 indicates, difficulties in obtaining licenses and permits discourage foreign direct investment. Related research suggests that strong rule of law, which would include among others competition law, attracts foreign investors. And barriers to entry become barriers that adversely affect productivity and impose real costs to the economy.[31]

The difficulties of doing business in developing countries, which generally arise from ill-conceived or unnecessary government (public policy) interventions, deter not only domestic and foreign direct investment but also the mobility of resources so that they can be utilized in the most productive way. They also induce distortions and rigidities into the economy and weaken the countries' ability to withstand economic shocks and further integrate into the global economic system. The "Investment Climate Assessments" and "Doing Business" indicators published by the World Bank have raised the awareness of national governments on the urgent need to reduce the time delays and regulatory burdens that they impose on business. There is increased demand for technical advisory programs at both the national and subnational levels. Countries in Europe and Central Asia and high-income OECD members are among those undertaking reforms, followed by sub-Saharan Africa. South Asia ranks low in initiating such reforms.

FIGURE 4.2: HIGH ENTRY COSTS INHIBIT FDI INFLOWS



Source: World Bank 2003.
Note: y= -0.5937x + 0.1851. Partial correlations control for market size, human capital, macroeconomic stability. The entry cost measure used in this figure refers to the costs of obtaining the necessary permits and licenses and other procedures required to set up a new establishment. See Djankov et al. (2002).

31. See World Bank (2003): 66, 90–92.

5. NATURE AND TYPE OF ANTICOMPETITIVE BUSINESS PRACTICES IN DEVELOPING COUNTRIES

Currently more than 100 countries (not including regional blocs) have enacted initial or significantly updated competition legislation. Most of these countries—mainly developing and transition market economies—enacted competition laws during the 1990s. The adoption of competition law-policy has been driven by a wide range of factors, including economic liberalization and deregulation, loan and policy conditions of the World Bank/IMF, regional and multilateral trade agreements, and aspirations to join the European Union. The competition laws in most developing countries mirror and contain the core provisions found in such legislation in industrial countries.

Table 5.1 indicates the number of countries by region, including IDA member countries that have enacted competition law-policy. Countries in the Latin America and Caribbean and Europe and Central Asian regions (the latter of which includes many former centrally planned economies) have included competition laws as part of their economic and regulatory policy framework. Relatively few countries in the Middle East and North Africa region have done so. In all regions but most notably in Africa, many countries have yet to adopt competition law. As indicated above, some countries, most notably India and Malawi, have enacted laws but have not established the requisite administrative machinery to implement them. Reasons range from the legislature's overloaded agenda to higher economic and political priorities and possible capture by vested interest groups.

OBJECTIVES AND PRINCIPAL FOCUS OF COMPETITION LAW-POLICY

As has been noted above, most countries enact competition law primarily to maintain and promote competition to encourage economic efficiency and increase consumer welfare through provision of greater choice of goods and services at lower prices. However, some countries have the broader goal of promoting the "public interest or benefits," which encompasses eco-

TABLE 5.1: NUMBER OF COUNTRIES WITH COMPETITION LAWS

	Sub-Saharan Africa	East Asia and Pacific	Latin America and Caribbean + North America	Europe and Central Asia	Middle East and North Africa	South Asia
No. of countries in the region	47	32	31	57	21	8
No. of countries with CL	17 (including 3 regional integrations)	13	19 (including 2 regional integrations)	47 (including 1 regional integration)	7	3
No. of IDA countries (with CL)	39 (11)	13 (4)	9 (3)	10 (8)	2 (0)	8 (3)

nomic efficiency and consumer welfare goals but also other social-economic and political objectives such as regional development; employment; protection of small- and medium-size enterprises; and expansion of exports, equity, and fairness. Not all of these entire and at times conflicting goals can be quantified or reduced to a single economic measure. However, they reflect society's wishes, culture, history, institutions, and other values that cannot nor should necessarily be ignored. It should be noted that most jurisdictions recognize the importance and need to protect and promote the competitive process and not individual competitors—though the implementation of competition law-policy often raises the issue of the impact of competition on competing incumbent domestic firms and labor.

While details vary by country, an effective competition law-policy essentially comprises four sets of instruments aimed at preventing anticompetitive business practices and market situations that *substantially lessen or prevent competition*. These are:

(i) Measures to prevent business firms from colluding or forming cartels to limit competition by entering into explicit or implicit agreements to fix prices, restrict output, allocate markets and customers, and rig bids or tenders. Typically such interfirm agreements or arrangements are strictly prohibited. The penal codes of some jurisdictions treat these practices as crimes.

(ii) Preventing dominant firms from abusing their market position by engaging in predatory prices; foreclosing markets for inputs or distribution channels; setting discriminatory prices and terms of service; using tied selling, which forces customers to buy other products and services as a condition of purchase of a particular product or service; and engaging in other forms of egregious monopolistic behavior.

(iii) Reviewing and preventing mergers and acquisition activity, joint ventures, and other interfirm agreements that exceed a certain size threshold, to ensure that transactions do not result in significant "market power" and lessen competition substantially. If transactions do this, they must have offsetting benefits, such as increased economic efficiencies and consumer welfare or attainment of other public interest objectives.

(iv) "Competition advocacy" directed at existing or proposed public policies and regulations that unnecessarily limit competition and entry, when alternative approaches that are less restrictive of free-market forces may be feasible. Competition advocacy also entails conducting competition assessments or market studies relating to the competitive dynamics at the industry level. These often provide insights into binding constraints to public policy and private sector restraints to competition and growth.[32]

It should be noted that competition law has certain exceptions and exemptions, most notably relating to collective bargaining activities of workers, setting of standards, research and development cooperatives, and development and exchange of statistics and other information, with the proviso that these activities do not result in anticompetitive business practices. Many jurisdictions grant exemptions or differential treatment to the financial sector (insurance, banking), professional services (lawyers, doctors, organized sports, etc.), regulated industries (utilities, telecommunication), and state enterprises. The economic rationale for exempting or treating these sectors differently is

32. See also Palmade (2005).

BOX 5.1: WHO ADMINISTERS COMPETITION LAW-POLICY?

Competition law-policy is generally administered by a specialist agency; this could be an independent body, subject to certain checks and balances and accountable either to a government ministry or department or to the legislative body. Alternatively, a competition agency could be a division or department within a designated government ministry, reporting to the minister in charge. Because competition law is a generally a law of general application that applies to all sectors and entities engaged in commercial economic activity, it is preferable to have an agency that is independent and insulated from political interference and influence of major interest groups/stakeholders in the economy.

A 2002 ICN report indicates that 62 percent of competition agencies are independent authorities, 32 percent are within a ministry or department, 2 percent are in an area ministry, and 4 percent are specialized tribunals. Though having an independent competition authority is favored for reasons such as increased likelihood of being insulated from bureaucratic and political interference, no particular model or approach can be deemed superior to the other. The United States has two competition agencies, both widely regarded as being independent from such influences: the Federal Trade Commission and the Department of Justice's Antitrust Division.

See also Dutz and Khemani (2007), World Bank (2000), and Kovacic (1997) for further discussion on such institutional design issues.

increasingly questioned,[33] in part because of developments and new learning in industrial organization and regulatory economics, as well as the introduction of new technologies in such fields as finance, telecommunication, transportation, and energy. It also is because most exemptions are the result of lobbying and preferential treatment of selected sectors. It is worth noting that because industrialized countries began enacting competition laws much earlier than developing countries—for example, Canada and the United States first enacted competition laws at the end of the 19th century—they tend to have more exemptions.[34]

Competition law-policy tends to be weaker in developing, particularly low-income countries. The reasons include lack of political will, limited staff and financial resources, institutional design issues such as slow and inefficient courts, and insufficient knowledge and experience. In jurisdictions where exemptions are granted, they tend to raise barriers to competition by creating an uneven playing field between private sector firms and state enterprises, and preferential treatment of politically connected firms. Moreover, promoting broad-based grassroots support and business culture supportive of fostering effective competition requires time, commitment, and resources. Frequent change of governments, and political and policy instability that characterizes many developing economies are not conducive to building and sustaining effective competition law-policy regimes.

33. See Khemani (2003) for further details.
34. Ibid.

Views differ as to whether developing countries need to adopt competition law-policy early on in the sequence of their economic and regulatory policy reforms, or even to have a specific competition law-policy. One line of argument is that trade and investment liberalization and economic deregulation will create conditions for entry of new firms, and increased domestic and foreign competition will erode any excess profits and dominant market position of an incumbent. However, as actual experience and related research indicates, while these policy measures are complementary, they are not sufficient to ensure effective competition. Domestic markets may be still insulated from external competitive pressures due to high transportation costs, non-tradable products and services, exclusive and restrictive distribution contracts, and domestic-international cartels and market-sharing agreements, among other factors.[35] For example, international cartels have spanned such products as vitamins, steel-graphite rods, large transformers, and food additives (lysine). These cartels included both domestic and international firms, and jurisdictions that enforced competition laws had lower price overcharges.[36] Moreover, lower tariffs and increased import competition do not necessarily result in increased productive capacity of domestic firms and new product and process development.[37]

A second line of argument is that developing countries lack strong supporting institutions such as an independent judiciary, good governance, independent media, and well-paid and capable public servants. New laws and institutions will fail to meet their goals, and could be costly and become yet another vehicle for corruption and interference in an emerging market economy. Undeniably these risks exist. But they also apply to other important areas of government services such as customs, tax clearance, public health, safety, and education, and governments do not avoid attempting to create effective institutions to improve delivery of such services. Competition can succeed with proper policy formulation, institutions designed with systems of checks and balances, accountability and transparency, and sufficient resources. International development organizations and donors, with their experience and resources, can help jump-start this process.

In this context, Clarke and Evenett have noted that about a quarter of the documented competition law enforcement actions in developing countries involve bid-rigging against state purchasers. If effective application of competition law deterred just 1 (one) percent of the value of the state contracts and resulted in price reductions of 15 percent, the cost savings would amount to between 3 percent (in Zambia) and 170 percent (in India) of the budget of the competition authority.[38] The resultant savings, which do not include economic fines that are normally imposed, would release resources for other development priorities.

Finally, it should be noted that the application of the main provisions of the first three sets of competition law instruments mentioned above (namely, dealing with cartels, abuse of dominant market position, and mergers and acquisitions) are primarily "demand driven." That is,

35. See industry- and country-specific examples cited in Khemani and Dutz (1996), Evenett et al. (2001), and Evenett (2004).
36. See Clarke and Evenett (2003a).
37. See UNCTAD (2006) and Clarke (2004). Clarke finds the net effect of lower tariffs on new product and process development to be negative but small, and for the most part cancelled out. In contrast, stricter competition laws and better enforcement of those laws appear to increase the likelihood of new product and process development, especially when competition is treated as endogenous to the economy.
38. See Clarke and Evenett (2003b).

business firms seeking relief from alleged anticompetitive market situations register complaints with the competition authorities. If these complaints are considered valid, the law generally requires the competition authorities to investigate and resolve the matter. This legal obligation has an important bearing on the degrees of freedom with which the competition authorities can deal with the multitude of case, sector, and systemic matters that arise in an economy—especially in a developing economy. The challenge for competition authorities in such an environment, with limited staff and financial resources, lies in finding an appropriate balance between the choice of instruments at their disposal, and the competition issues they can reasonably address.

EXAMPLES OF ALLEGED ANTICOMPETITIVE PRACTICES IN SELECTED COUNTRIES

Box 5.2 illustrates different types of complaints and allegations of anticompetitive business practices in selected developing economies. Several of the (alleged) complaints relate to intermediate products such as cement, steel, banking, and transportation (trucking and shipping), as well as products for export such as cotton and fish. These practices raise the costs of business and undermine competitiveness in domestic and international markets. For example, in Morocco, a trucking cartel operated in the transportation of cut flowers for export, a major source of employment and foreign exchange earnings in that economy. A database compiled from various newspapers and other publications relating to sub-Saharan African countries indicates that many of the alleged private anticompetitive practices pertain to intermediate products.[39] About one-third of the alleged abuses of dominant market positions or monopolistic practices referred to foreign-owned or -controlled firms. Foreign firms also appear to take advantage of weak or lack of competition law-policy and anticompetitive market situations. Parenthetically, it is also worth noting that the majority of competition cases in advanced industrial countries also relate to complaints registered by business firms alleging cartels and other forms of anticompetitive business practices by firms supplying inputs that increase the costs and undermine domestic and international competitiveness. As noted above, some recent examples include graphite steel rods, cement, paper, transportation services, and food additives.

In summary, competition can be generated and increased through various policy measures such as trade and investment liberalization. Enactment of competition law-policy does not necessarily result in competition. However, as competition arises in existing or new market economies, it needs to be protected and promoted. The principal objective of an effective competition law-policy is to maintain and promote competition. It is to safeguard and foster the competitive process and not existing competitors. In doing so it becomes an important if not critical vehicle for empowering entrepreneurs and investors, creating conditions for entry of new and expansion existing businesses, and increasing consumer welfare—be they individuals or firms that purchase inputs for production processes. It provides for relief from anticompetitive business practices whether these emanate from government enterprises and public policies or incumbent private sector firms. Liberalization of trade, investment, and regulations are complementary measures and not substitutes for an effective competition law-policy.

39. See Evenett et al. (2006).

BOX 5.2: EXAMPLES OF ANTICOMPETITIVE PRACTICES IN SELECTED COUNTRIES IN SUB-SAHARAN AND SOUTH ASIA REGIONS

Allegations of price-fixing, market-sharing, bid-rigging, transnational cartels and agreements, and abuse of dominant market position are reported.

Kenya
Fish processing, Lake Victoria: Fishermen, government officials, and local chiefs allege fish processors/exporters have formed a cartel to exercise monopsonistic market power. Fish sold at 2.5 times the purchase price paid to fishermen and "make a fortune and invest nothing back to improve the welfare of the people living around the lake."

Malawi
Cotton: There are very few buying companies, and they collude to exploit over terms and prices offered to cotton growers.
Bakeries: While there are many bakeries, a few giant ones dominated the Master Bakers Association. Until government action in response to consumer complaints, the association fixed the prices of baked goods.
Freight transport: The Transport Operators Association, consisting mainly of a few large firms (Trans African Transport, Central African Road Services, Zagaf, Welsons, Fersons, and others) set high transportation rates and include foreign trucking firms as members.

Ethiopia
Fertilizers, seed: Alleged domestic and import cartels formed by "party-statals" (firms owned mainly by the political party in power) with market-sharing agreements covering different farming regions have exploited and raised the costs to farmers, and the price of products.

Kenya/Tanzania
Beer: Transnational market-sharing agreements and anticompetitive mergers and acquisitions.
Insurance: Price-fixing.

East African Cement Producers Association
Cement: Consolidation and monopoly control of markets in Kenya, Tanzania, and Uganda; coordinated measures to prevent import competition from Egypt.

West Africa
Shipping: Europe-West Africa Trade Agreement and Europe-West Africa Shipping Conference coordinate and significantly increase shipping tariffs, which is detrimental to exports.

Nigeria
Telecom services: Attempted monopolization alleged by Mobile Telecommunication Services against incumbent MTN Nigerian Communication.

Bangladesh
Staple foods (rice, potatoes, sugar): Widespread allegations of uniform prices/cartels.
Industrial products/inputs: Cartels in cement, fertilizers, and corrugated steel markets.
Intercity passenger bus services: Price-fixing and route-sharing agreements.
Government procurement: Bid-rigging and illegal manipulations in the purchase of aircraft for domestic airline services, and in the electric power sector.

India
Airline fuel surcharge: Domestic airlines meet to agree and fix the level of fuel surcharges to be added to passenger ticket costs. Meeting facilitated by Ministry of Aviation.
Staple products: Cartelization of supply of sugar, food grains, and vegetable cooking oil.
Industrial products/inputs: Price fixing of cement, steel, trucking, banking; mergers to reduce competition in cement.

Vietnam
School textbooks, uniforms: Tied selling.

Sources: Evenett et al. 2006, DFID (Department for International Development) 2006, and various reports and email newsletters by CUTS, Joint World Bank-DFID field investigations, Bangladesh, October 2005.

COMPETITION ADVOCACY

In many jurisdictions, competition authorities are authorized to engage in "competition advocacy," that is, to review and comment on various public policies and regulations that unnecessarily restrict competition. Instead of creating new government entities such as economic or regulatory reform units, some governments have opted to use competition agencies to review, vet, and suggest alternative approaches to policies and regulations that restrict competition, economic efficiency, and consumer welfare—while balancing other socio-economic-political objectives. In Australia, Korea, and Russia, government ministries and other agencies are required to consult competition authorities in this regard. In Canada, the head of the Competition Bureau has a statutory right to appear before parliamentary committees, commissions, and regulatory authorities to put forward pro-competition proposals and arguments. In the United Kingdom, and increasingly in other countries including several developing nations such as South Africa, competition authorities and sector-specific regulators have memoranda of understanding and other formal and informal mechanisms that guide their coordination and consultation on regulatory matters that may have an impact on competition. This does not necessarily imply that the views and recommendations are binding or always factored into the final decisions of the relevant regulatory bodies, but it introduces greater accountability and transparency in formulation of regulatory policies.

The International Competition Network (ICN) survey indicates that 36 percent of the competition authorities reported their opinions on sector reform proposals are always sought, 23 percent participated "ex-officio," and 30 percent were occasionally consulted. Only 11 percent stated they were only informed. The last statistic pertains primarily to developing countries. Of the agencies that were always or frequently asked to provide input, 65 percent were involved at an early stage, and 16 percent were involved throughout policy formulation process. Most successful advocacy activities were reported in the telecommunications, electricity, and transportation sectors, fewer in financial services, retail trade, and ports. Most successful participation related to privatization processes (40 percent of respondents), removal of price regulations (22 percent), licenses and permits (22 percent), and concessions (16 percent).[40]

The ICN survey also indicates that the strongest support for the advocacy role of competition authorities comes from groups such as consumer associations, academics, and media; less from entrepreneurial and professional associations, legislators, and nongovernmental organizations (NGOs), and least from political parties, labor unions, and local governments. These results are not surprising: Legislators and political parties worldwide are noted for "pork-barrel" spending to win financial support and votes. Several industrial organization economic studies indicate that labor is paid higher wages in industries with monopolistic market structures that insulate them from competitive pressures. Labor in such situations becomes a willing partner of business in lobbying against pro-competition reforms.

To counter such challenges, competition authorities can forge strategic alliances with other competition advocacy groups. For example, lobbying for duties and increased tariff protection against imported steel can be countered

40. See ICN (2002).

through studies that show the anticompetition repercussions of such policies and mobilizing support from the users of steel such as the automobile and construction industries, as well as consumer groups that ultimately will bear the higher costs of those products. These activities also raise awareness of the benefits of competition and promote a competition culture in society. Appreciation of competition is markedly lower in developing countries than in advanced industrial economies, not only in general society but also in the courts and within government itself.[41]

Experience shows competition authorities are most successful at advocacy when they eschew a confrontational approach, and instead work cooperatively with other government departments and regulatory bodies, for example, offering alternative recommendations and proposals that are sensitive to the mandates of the other organizations. In other words, "first best" solutions may not always be workable; compromise that is least damaging to the competitive process may be needed. Nor should competition advocacy be directed solely at government entities and competition-constraining policies—the business practices of industry and trade associations and large firms may also be candidates for reform. A balance must be struck between enforcement of, and fostering compliance with, competition law-policy, for litigation is costly to both government and business. Through information dissemination programs such as publication of administrative and policy implementation guidelines, business advisory opinions, and speeches and conference proceedings, competition authorities can reduce uncertainty, and promote good commercial practices and business ethics in the marketplace.

APPLICATION OF COMPETITION LAW-POLICY

Examples of application of competition law-policy are:

India

Due to a legal challenge and amendments in parliament, the full force of the Competition Act (2002) has yet to come into effect. However, in the interim, the Competition Commission of India (CCI) has been active—among other activities, it has conducted 38 advocacy and awareness building programs with leading industry, trade, and professional associations and civil society; conducted a number of market studies/research projects; drafted regulations and interpretation bulletins on matters relating to cartels, bid-rigging, predatory pricing, and intellectual property and other rights; held consultations and met with state governments on jurisdictional and interstate competition matters; provided input and opinions on various policy and regulatory proposals; drafted a curriculum for competition courses in law and economic programs in collaboration with academic institutions. One notable example is that the CCI registered its concerns and opposition to a proposal by the Department of Post & Telegraph to extend monopoly control on all letters and packages up to 300 grams. Had the proposed policy been adopted, it would have ended the competitive private courier service. The CCI also indicated that a meeting between airlines to fix fuel surcharges, facilitated in part by the Ministry of Aviation, violated the cartel provisions of the competition act. The CCI is engaged with other government departments and advisory bodies in drafting a "National Competition Policy" to foster greater coherency and consistency in government policy formulation and decision making as it relates to competition.[42]

41. Ibid.
42. See www.competition-commission-india.nic.in, and discussions by the author with CCI officials.

Kenya

Kenya's Monopolies and Prices Commission (MPC), a unit of the Department of the Treasury, administers the Restrictive Trade Practices, Monopolies and Price Control Act. The law has had limited success, in part because of institutional design flaws—for example, it contains provisions that could allow reinstitution of price controls that in effect have been decontrolled since 1994—and because of factors that impede its effective application, including inefficiency and corruption in the public and private sector, lack of adequate human and financial resources, a judiciary inexperienced in competition law and economic matters, and limited public support. In addition, the MPC is not an independent authority. Nevertheless, it surveils markets, receives complaints, and investigates matters to ensure competition rules are upheld. From 1989 to 2005, the MPC fully investigated 234 cases relating to a wide number of business practices and industries. It also has succeeded in introducing competitive bidding and eliminated single-sourcing in government procurement, resulting in significant reductions in prices of drugs and other supplies to hospitals, and road transportation services. It initiated cartel cases in the retail gasoline, insurance, Internet service, and selected agribusiness products—which even while legal proceedings were pending resulted in price reductions. As a consequence of MPC's actions, several merger-and-acquisition transactions that could have resulted in significant reductions in competition have been restructured in markets such as food processing, pharmaceuticals, car rental services, and beer.[43]

Tunisia

The Competition Council enforces the competition law in Tunisia. In a case involving abuse of dominant market position by a giant poultry firm, Poulina, the Council imposed a fine of approximately 240,000 dinars (approximately US$194,000). While there were about 1,500 small producers of chickens and eggs, Poulina dominated the market in not only the downstream market but also the provision of inputs. It imposed unfair conditions including exclusive dealing contracts on distributors, foreclosing participation in the market by smaller producers.[44]

Zimbabwe (and Zambia)

The National Breweries Ltd. (NBL) has a market share of 90 percent of the beer sector with a nationwide distribution network. Nesbitt Breweries entered the market, but confined its entry to the town of Chiredizi. NBL countered by launching a sales promotion campaign in Chiredizi, offering T-shirts, free snacks, luck-draw prizes, and lowering its beer prices to partly absorb normal transportation costs. The promotion campaign was not held in other markets. The Zimbabwe Competition Commission found this behavior to constitute predatory pricing with the intent of driving out Nesbitt, and issued a cease and desist order.[45]

The commission has also investigated and resolved various cases relating to cement, poultry, soft drinks, and tobacco products. Merger-and-acquisition transactions, most related to foreign takeovers of local or subsidiary firms, have generally been permitted to proceed, with certain restructuring, performance, and other conditions, to safeguard competition while not discouraging foreign investment.

43. See Njorge (2006).
44. Cited in Chakravarthy (2007).
45. Ibid, and UNCTAD (2002).

The experience in neighboring Zambia is parallel, and has in some cases related to the same firms and product markets.[46]

Similar examples on the successful case- and sector-specific application of competition law and policy can be obtained from the Web sites and publications of various competition authorities.[47]

Despite theses successes, there still are obstacles to the effective implementation of competition law and policy worldwide but especially in least-developed countries, namely, lobbying by vested interest groups, lack of political support, human and financial resource constraints, and lack of relevant expertise in the judiciary.

46. See Lipimile (2004).
47. These websites can be accessed from www.internationalcompetionnetwork.org

6. CONCLUSIONS AND RECOMMENDATIONS

The preceding discussion has highlighted the benefits of promoting competition in domestic markets in developing economies. The adoption and effective implementation of competition law-policy fosters static and dynamic economic efficiency, increases consumer welfare by spurring firms to produce greater variety and more affordable goods and services, reduces market dominance by large incumbent firms, contributes to greater accountability and transparency in government-business relations, and thereby reduces opportunities for corruption and bribery. Effective competition improves and buttresses the investment climate and makes it more attractive for investment by domestic and foreign entrepreneurs. It also facilitates integration of developing economies into global markets, and sustains broad-based economic growth and poverty reduction.

Competition law-policy has a broad interface with other government economic and regulatory policies. To enhance coherency and consistency in these policies, competition law-policy needs to be integrated as a central platform. This will require increased efforts to foster better understanding of the instruments, requirements, and benefits of promoting competition—in government policy formulation and in the private sector and civil society at large. It also will require reorienting the policy advisory and support programs of the World Bank Group toward longer-term engagements with client governments to conduct country- and sector-specific analysis, institution building, and development of local capabilities.

REBALANCING OF POLICY ADVISORY AND DIAGNOSTIC PROJECTS

For the past two decades or more, the World Bank Group and other development organizations have encouraged developing and emerging market economies to adopt pro-competition measures such as trade and investment liberalization, privatization, and economic deregulation. These initiatives have been aimed primarily at reducing *public sector* policy-based barriers to entry, regulatory costs, and delays that unnecessarily constrain private sector economic activity. Giving priority to these reforms and the overall positive impact they have had on productivity and competition are not questioned. They are, however, insufficient—they are complementary to but do not substitute for an effective competition law-policy. They do not address the *private sector* restrictive business practices that can significantly impede competition. Unchecked, anticompetitive practices by dominant and politically connected firms and vested interest groups can capture or significantly reduce the benefits that accrue from competition. The freedom of economic action of new investors, entrepreneurs, and firms can be severely constrained unless there are avenues for legal recourse to obtain remedial relief. An effective competition law-policy is a vehicle for such relief and for curbing anticompetitive practices by both government and business. Competition does not arise or sustain itself automatically. The competitive process needs to be *maintained, protected,* and *promoted* to strengthen the development of a sound market economy.

There are misconceptions, doubts, and questions about competition in the minds of policy makers and the general population in many developing countries; in particular, they ask "who are the main beneficiaries?" To focus on public policy-based barriers to competition without simultaneously addressing private sector anticompetitive business practices helps competition's detractors, who argue first that market liberalization reforms are aimed at benefiting the well-connected families that own/

control large dominant firms and other vested interest groups, including multinational enterprises, and second that competition law-policy is yet another manifestation of the "Washington Consensus" policies to open developing country markets and take advantage of emerging opportunities without necessarily investing in and creating indigenous productive capacities.

Such views need to be dispelled. It is critical to promote better understanding, appreciation, and local support for competition law-policy as an instrument to do the following: (a) Foster competition in the *domestic* industries and markets to create opportunities for *domestic firms and entrepreneurs* to participate in their *own economy.* In other words, competition law-policy aims primarily at removing constraints impeding efficient functioning of domestic markets and not necessarily at opening them to international competition—that can happen later, as capable domestic firms emerge. (b) The application of competition law is mainly demand driven, in response to complaints by customers that have been victims of actual or alleged anticompetitive practices. Indeed, the great majority of complaints and cases in countries with competition law-policy regimes relate to intermediate inputs, the high costs of and restricted access to which undermine competitiveness of downstream firms. (c) Competition law-policy is essentially about empowerment. It is aimed at removing unnecessary restrictions imposed by government policy-based *and* artificial private sector business firms' barriers to entry and competition.

(A) It is recommended that the World Bank Group, in partnership with other development organizations, client country governments, and especially civil society organizations (NGOs) should engage in a systematic program of:

(i) Information dissemination and knowledge sharing on effective implementation and beneficial impact of competition law-policy—particularly in terms of the domestic economy.
(ii) Country- and industry-specific competition assessments and diagnostic projects that extend beyond public policy-based impediments to include in-depth analysis of the private sector restrictive business practices. Identify the "winners" and "losers" emanating especially from barriers created by and/or favoring dominant firms and vested interest groups.
(iii) Work with consumer associations, NGOs, and private sector business organizations and trade associations, to create local "voices" for fostering grassroots ownership and demand for pro-competition measures in government policies.

Priority Sectors

Competition law is of general application—it applies to all sectors and agents engaged in commercial economic activity. Few sectors and activities warrant exemptions. Nevertheless, government policies and regulations, as well as lobbying by industry groups often do result in exemptions, exceptions, and differential treatment of certain businesses.

(B) It is recommended that:

(i) Countries' competition assessments and regulatory impact analysis include an audit of the nature and extent, and underlying economic rationale of the exemptions, exceptions, and differential treatment of various economic activities, taking into account the socio-economic-political objectives.

(ii) Priority be given to economic activities that have an impact on:

–The poor (for example, staple food products, local transportation, water-sanitation, energy);
–Products and basic services that serve multiple downstream economic activities and bear on industry competitiveness (for example, financial services, factor inputs, basic infrastructure);
–Delivery and cost efficiency of government procurement of goods and services to reduce opportunities of corruption, bribery, favoritism;
–Potentially competitive industries that could attract and benefit from foreign direct investment.

(iii) The appropriate role, coverage, and possible application of instruments of competition law-policy be defined relative to sector-specific policies and regulations such as in financial services and provision of basic infrastructure services.

Institution Building

Currently at least 104 countries have enacted or significantly updated their competition legislation. The adoption of competition law-policy has been driven by a wide range of factors that include economic liberalization and deregulation, loan and policy conditions of the World Bank/IMF, regional and multilateral trade agreements, and aspirations to join the European Union. Competition laws in most developing countries mirror and contain the core provisions generally found in industrial countries. However, competition law-policy is perceived to be weaker in in those countries, particularly in low-income ones. The reasons for this include limited staff and financial resources, institutional design issues such as slow and inefficient courts, and insufficient knowledge and experience. Their government policies, such as granting exemptions to state enterprises and preferential treatment of politically connected firms, raise barriers to competition and distort markets. This undermines the development of a healthy private sector. In addition, continuous or multi-year technical advisory programs and assistance from the World Bank Group and other development organizations is lacking—notwithstanding the requests of nascent competition regimes. Promoting and building effective competition regimes requires time, commitment, and resources.

(C) It is recommended that the World Bank Group, in partnership with other development organizations, develop a more systematic technical advisory program and a set of criteria for selecting countries that meet certain requirements and show prospects for developing and strengthening a competitive market economy. This technical advisory program should include:

(iv) Assistance in drafting and revising competition legislation and regulatory policies, administrative and interpretation guidelines, and other related materials for effective policy implementation.
(v) Advice and capacity development in case management, investigative techniques, compliance programs, regulatory interventions, industry competition assessments and regulatory impact analysis, competition advocacy, and other skills.
(vi) Promotion of greater intergovernmental cooperation and coordination in the formulation and application of economic and regulatory policies to least restrict market competition, while taking into account other socio-economic-political objectives.
(vii) Facilitation of cooperation and exchange programs with peer competition authorities, including information sharing on transborder matters of mutual interest and staff exchanges.

The Nexus of Public and Private Sector

Competition law-policy operates at the point where the public and private sectors interface and interact. To develop an efficient and competitive market economy, both sectors must take part in its design and implementation. This requires trust, cooperation, and partnership—the application of competition law-policy need not produce tension between sectors, nor among individual firms. Competition law-policy is not inimical to but rather complements other approaches to fostering competitiveness. For example, a modern competition law-policy contains provisions that facilitate legitimate public-private partnerships and cooperative approaches. Competition law-policy plays a benign or facilitative role in many initiatives, such as development of standards, research and development, underwriting and risk-mitigation relating to insurance and finance, and collection and dissemination of statistical information, as long as the initiatives do not become vehicles for engaging in exclusionary and other business practices that substantially lessen competition. Government and business increasingly recognize that enforcement litigation in respect to cartels and other abuses of dominant market position is costly compared to fostering compliance with the law. Even in areas most subject to competition law-policy, such as mergers and acquisitions, joint ventures, and strategic alliances that are primary vehicles for foreign direct investment, the vast majority of transactions proceed unhindered. Indeed, these transactions are facilitated by an effective competition law-policy, as it promotes ethical business behavior by establishing the rules and framework for proper functioning and governance of markets.

APPENDIX: TABLES

TABLE A.1: SELECTED DOING BUSINESS INDICATORS, AVERAGES ACROSS REGIONS (2006)

	Ease of Doing Business Rank		Starting a business		Dealing with licenses	
	Non-IDA	IDA	Procedures (number)	Time (days)	Procedures (number)	Time (days)
Latin America & Caribbean[i]	82.54	88.88	10.2	73.3	15.4	198.7
Middle East & North Africa[ii]	93.53	129.5	10.3	40.9	19.9	206.9
South Asia[iii]	(**)	104.75	7.9	32.5	16.1	226.6
East Asia & Pacific[iv]	54.63	91.33[v]	8.2	46.3	17.6	147.4
Europe & Central Asia[vi]	69	90.54	9.4	32.0	21.4	242.5
Sub-Saharan Africa[vii]	87.77	134.83[viii]	11.1	61.8	17.7	230.2
Average all countries	64.01	117.45				

Source: World Bank 2006.

(**) All countries in the region of South Asia are IDA borrowing countries.

i. Latin America and Caribbean's IDA borrowing countries include Guyana, Haiti, Bolivia, Honduras, Dominica, Nicaragua, Grenada, St. Lucia, and St. Vincent.

ii. Middle East and North Africa's IDA borrowing countries include Djibouti and Republic of Yemen.

iii. South Asia's IDA borrowing countries include Afghanistan, Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan, and Sri Lanka.

iv. East Asia and Pacific's IDA borrowing countries include Cambodia, Indonesia, Kiribati, Laos, Myanmar, Mongolia, Papua New Guinea, Samoa, Solomon Islands, Timor-Leste, Tonga, Vanuatu, and Vietnam.

v. No data available for Myanmar.

vi. Europe and Central Asia's IDA borrowing countries include Armenia, Albania, Azerbaijan, Bosnia-Herzegovina, Georgia, Kyrgyz Republic, Moldova, Montenegro, Serbia, Tajikistan, and Uzbekistan.

vii. Sub-Saharan Africa's IDA borrowing countries include Angola, Benin, Burkina Faso, Burundi, Cape Verde, Cameroon, CAR (Central African Republic), Chad, Comoros, Congo Republic of, Congo DR (Democratic Republic of), Cote d'Ivoire, Ethiopia, Eritrea, Gambia, Ghana, Guinea, Guinea-Bissau, Kenya, Lesotho, Liberia, Madagascar, Malawi, Mali, Mauritania, Mozambique, Niger, Nigeria, Rwanda, Sao Tome and Pr., Senegal, Sierra Leone, Somalia, Sudan, Tanzania, Togo, Uganda, Zambia, and Zimbabwe.

viii. No data available for Somalia and Liberia.

Employing workers		Getting credit		Trading across borders		Closing a business	
Difficulty of hiring index	Firing costs (weeks of wages)	Public registry coverage (% adults)	Private bureau coverage (% adults)	Time for export (days)	Time for import (days)	Time (Years)	Recovery rate (cents on the dollar)
34.0	59.0	7.0	27.9	22.9	27.9	2.6	25.7
29.7	56.9	3.2	7.6	27.1	35.4	3.1	25.7
41.8	71.5	0.1	1.3	34.4	41.5	3.6	19.5
23.7	41.7	3.2	10.1	23.9	25.9	2.4	27.5
34.2	26.2	1.7	9.4	29.2	37.1	3.5	29.5
44.3	71.2	1.5	3.8	40.0	51.5	2.6	17.7

TABLE A.2: SELECTED DOING BUSINESS INDICATORS: BEST AND WORST COUNTRY STANDINGS BY REGION (2006)

				Latin America		Middle East	
Indicator	Non-IDA average	IDA average		Best	Worst	Best	Worst
Ease of Doing Business Rank[ix]	64.01	117.45	Rank(*)	Puerto Rico (19)	Venezuela (164)	Israel (26)	Egypt (165)
Starting a business[x]	72.87	106.68	Rank(*)	Puerto Rico (8)	Haiti (167)	Israel (15)	West Bank & Gaza (173)
			Procedures (number)	Grenada (4)	Paraguay (17)	Israel (5)	Algeria (14)
			Time (days)	Puerto Rico (7)	Suriname (694)	Tunisia (11)	West Bank & Gaza (93)
Dealing with licenses[xi]	75.01	103.21	Rank(*)	St. Vincent (1)	Guatemala (165)	Yemen (39)	Egypt (169)
			Procedures (number)	Grenada (8)	Guatemala (23)	Yemen (13)	Egypt (30)
			Time (days)	Belize (66)	Brazil (460)	Tunisia (79)	Iran (668)
Employing workers[xii]	81.5	97	Rank(*)	Belize (14)	Bolivia (174)	Kuwait (20)	Morocco (156)
			Difficulty Hiring Index	St. Kitts & Nevis (0)	Panama (78)	Egypt (0)	Morocco (100)
			Cost of Firing (weeks of wages)	Puerto Rico (0)	Argentina (138.7)	Iraq (4)	Egypt (186.3)

ix. **Ease of Doing Business**—The table shows the overall ease of doing business ranking for each economy. Economies are ranked on their ease of doing business, from 1–175, with first place being the best. A high ranking on the Ease of Doing Business Index means the regulatory environment is conducive to the operation of business. This index averages the country's percentile rankings on 10 topics, made up of a variety of indicators, giving equal weight to each topic.

x. **Starting a Business**—Bureaucratic and legal hurdles an entrepreneur must overcome to incorporate and register a new firm. It examines the procedures and time involved in launching a commercial or industrial firm with up to 50 employees and start-up capital of 10 times the economy's per capita gross national income (GNI). The indicators shown in the table include all procedures require to register a firm and the average time spent during each procedure. *Rank*—Higher rank values in the table indicate more rigid regulations to start a business including the following indicators (a) procedures required to register a firm, (b) average time spent during each procedures, (c) official cost of each procedures, and (d) the minimum capital required as a percentage of income per capita.

xi. **Dealing with Licenses**—Procedures and time necessary to build a warehouse, including obtaining necessary licenses and permits, completing required notifications and inspections, and obtaining utility connections. They include all procedures to build a warehouse and the average time spent during each procedure. *Rank*—Higher rank values in the table indicate more rigid regulations for building a warehouse and include (a) procedures to build a warehouse, (b) average time to build a warehouse, and (c) the official cost of each procedure.

xii. **Employing Workers**—This indicator measures the flexibility of labor regulations. It examines the difficulty of hiring a new worker as well as the costs involved in dismissing a redundant worker. The table shows two indicators: the difficulty of hiring a new worker (Difficulty of Hiring Index) and the cost of a redundant workers, expressed in weeks of wages (Firing Costs). *Rank*—Higher rank values in the table indicate more rigid regulations for employing workers and include (a) difficulty of hiring a new worker (Difficulty of Hiring Index), (b) restrictions on expanding or contracting the number of working hours (Rigidity of Hours Index), (c) difficulty and expense of dismissing a redundant worker (Difficulty of Firing), (d) an average of the three indices (Rigidity of Employment Index), and (e) cost of a redundant worker, expressed in weeks of wages (Firing Costs).

South Asia		East Asia & Pacific		Europe & Central Asia		Sub-Saharan Africa	
Best	Worst	Best	Worst	Best	Worst	Best	Worst
Maldives (53)	Afghanistan (162)	Singapore (1)	Timor-Leste (174)	Lithuania (16)	Uzbekistan (147)	South Africa (29)	Congo, Dem Rep (175)
Afghanistan (17)	India (88)	Hong-Kong, China (5)	Indonesia (161)	Romania (7)	Tajikistan (166)	Mauritius (30)	Guinea-Bissau (175)
Afghanistan (3)	Pakistan (11)	Tonga (4)	China (13)	Latvia (5)	Belarus (16)	Mauritius (6)	Equatorial Guinea (20)
Afghanistan (8)	Bhutan (62)	Singapore (6)	Lao PDR (163)	Turkey (9)	Belarus (69)	Central African Republic (14)	Guinea-Bissau (233)
Maldives (9)	India (155)	Thailand (3)	Timor-Leste (173)	Estonia (13)	Croatia (170)	Swaziland (16)	Eritrea (173)
Maldives (10)	Bhutan (26)	Vanuatu (7)	Taiwan, China (32)	Estonia (13)	Moldova (34)	Guinea-Bissau (11)	Sierra Leone (48)
Maldives (118)	Nepal (424)	Micronesia (73)	China (367)	Armenia (112)	Russia (531)	Namibia (105)	Cote D'Ivoire (569)
Maldives (5)	Nepal (150)	Marshall Islands (1)	Taiwan, China (154)	Georgia (6)	Estonia (151)	Uganda (8)	Sao Tome (175)
Maldives/Sri Lanka (0)	Bhutan/ Pakistan (0)	Hong Kong, China (0)	Taiwan, China (78)	Belarus (0)	Latvia (67)	Botswana (0)	Tanzania (100)
Afghanistan (4.3)	Sri Lanka (177)	Marshall Islands (0)	Indonesia (108.3)	Romania (3)	Turkey (94.7)	Gambia (8.7)	Zimbabwe (446.3)

xiii. **Getting Credit**—This topic explores two sets of issues—credit information registries and the effectiveness of collateral and bankruptcy laws in facilitating lending. The table includes two main indicators measuring the coverage of public credit registry (Public Registry Coverage as % of adults) and the coverage of private credit bureau(s) (Private Bureau Coverage as % of adults). *Rank*—Higher rank values in the table indicate more rigid regulations for getting credit and includes (a) the coverage of credit information registries and (b) the effectiveness of collateral and bankruptcy laws in facilitating lending.

xiv. **Trading Across Borders**—Procedural requirements for exporting and importing a standardized cargo of goods. Every official procedure is counted—from the contractual agreement between the two parties to the delivery of goods—along with the time necessary for completion. The table shows two main indicators, which are the time necessary to comply with all procedures required to export and import goods. *Rank*—Higher rank values in the table indicate more rigid regulations for trading internationally including (a) the number of all documents required to export/import goods, (b) time necessary to comply with all procedures required to export/import goods, and (c) the cost associated with all the procedures required to export/import goods.

xv. **Closing a Business**—This topic identifies weaknesses in existing bankruptcy law and the main procedural and administrative bottlenecks in the bankruptcy process. The table shows two main indicators: the average time to complete a procedure and the recovery rate, which calculates how many cents on the dollar claimants (creditors, tax authorities, and employees) recover from an insolvent firm. *Rank*—Higher rank values in the table indicate more rigid regulations and include (a) the average time to complete a procedure, (b) the cost of the bankruptcy proceedings, and (c) the recovery rate (cents on the dollar).

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