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School of Economics and Management

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Development Friendly Competition Policy?

Implementing Competition Policy in the EPAs

Daniel Gustafsson

Abstract

This thesis examines the connection between competition policy, international competition policy and economic development. There are at least two important movements in world trade today: the recognition of competition policy, both domestic and international, for economic growth and development, and the proliferation of bilateral trade agreements. Increasingly, new trade related issues are being brought into bilateral trade negotiations, competition policy being one such issue. There is little doubt that competition policy is important, particularly for developing countries, but under pressure from industrial countries, developing countries may lose focus of their particular development needs, ultimately losing influence over their own policy choices. This thesis finds that there is such a thing as development friendly competition policy. Although there are potential areas of conflict, the Economic Partnership Agreements could help facilitate the implementation of such competition policy in the developing countries, and by way of gradualism, flexibility and competition advocacy redirect growth from the informal to the formal economy.

Keywords: Competition Policy, Developing Countries, Economic Partnership Agreements, Informal Economy, International Competition Policy

Abbreviations

ACP	Africa Caribbean Pacific
AML	Anti-Monopoly Law
CU	Custom Union
ECOWAS	Economic Community of West African States
EDF	European Development Fund
EPA	Economic Partnership Agreements
FDI	Foreign Direct Investment
FTA	Free Trade Area
GATT	General Agreements on Tariffs and Trade
ICA	International Competition Authority
ICN	International Competition Network
IGO	Intergovernmental Organization
ITO	International Trade Organization
JFTC	Free Trade Commission of Japan
M&A	Mergers and Acquisitions
MACP	Multilateral Agreement on Competition Policy
MNC	Multinational Corporation
OECD	Organization for Economic Co-operation and Development
OPEC	Organization of the Petroleum Exporting Countries
RTA	Regional Trade Agreement
SADC	Southern African Development Community
SSA	Sub-Saharan Africa
UNCTAD	United Nations Conference on Trade and Development
WGTC	Working Group on the Interaction between Trade and Competition Policy
WTO	World Trade Organization

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1 Introduction

Since 1947, tariffs on trade have fallen dramatically around the world, from 40% to less than 4%. The success is attributed to the General Agreement on Tariffs and Trade, GATT. Starting with only 23 members, the membership in GATT's follower the World Trade Organization, WTO, has now risen to over 140 countries.¹

But in later years, following the Uruguay Round of multilateral trade negotiations, which began in 1986 and saw the creation of the WTO in 1995, trade negotiations have come to involve issues other than tariff reductions.² The leading principles of the GATT/WTO negotiations are *Reciprocity* and *Most Favored Nation*. The first is that offers of reducing tariffs by one part are met by concessions of doing the same by another and the second that tariff reductions offered to one part were automatically valid for all others.³ But although these principles is very efficient means of facilitating trade liberalization in the form of tariff reductions, they are less useful in tackling new issues in trade talks.

The Uruguay Round did reach conclusion, but its successor, the Doha Round, has dragged out in time, with no end in sight. The stalemate has largely been due to confrontation between industrial countries and developing countries over five new issues: investment, labor standards, the environment, intellectual property rights and competition policy.

Competition policy presents a paradox. While many developing countries staunchly object to its inclusion into the WTO, very few, if any, economists will discredit the role played by competition and competition policy for economic growth and development.

Following the stalemate, the new WTO issues have found their way into bilateral trade negotiations outside the WTO, where competition policy has proven particularly important. But, can a development friendly competition policy withstand the pressures from this new, international competition policy?

¹ Bagwell & Staiger 2003:1

² Hoekman & Kostecki 2001:49

³ Bagwell & Stagier 2003:18

1.1 Issue and purpose

The main issue of this thesis is the current EPA negotiations, particularly in reference to competition policy.

The purpose of this thesis is entering the two concepts of competition policy and international competition policy into the dual contexts of developing countries and Regional Trade Arrangements (RTAs). The overall goal is to evaluate if international competition policy can co-exist with the needs of the developing countries. Therefore, the question to be answered by this thesis is: *How can competition policy be implemented in the EPAs while simultaneously ensuring development gains?*

1.2 Method and Material

This thesis will be extensively based on economic literature, primarily in the form of scientific articles. The articles have been chosen and utilized based on their neutrality and credibility. However, some sources could be described as pro-developing countries, while others as pro-industrial countries. This has been taken into special consideration when utilizing these sources.

I will also draw from two empirical sources; a survey on anti-competitive behavior and another on the business climate, both in reference to SSA. The conclusions drawn from these studies are exclusively my own, in an attempt to incorporate the findings into the development friendly competition policy concept.

The method used has been to first lay the theoretical foundations and to provide the setting. Then I have emphasized a more practical, but not fully theoretically developed, concept, and analyzing this against the contextual backdrop of Economic Partnership Agreements.

1.3 Disposition and structure

This thesis is divided into five chapters. First, in order to provide a theoretical framework, I will discuss the concept of competition policy. Here, competition policy will be defined, its main purpose and objectives explored and its common aspects and components examined. This will be followed by a brief outline of the history and evolution of competition policy in three major industrial countries: the US, the EU and Japan.

The next chapter will entail a closer look at the international aspects of competition policy. With the competition policy discussion in mind, this chapter will, apart from defining the concept of *international competition policy* itself, outline the particular rationale behind it. Focusing mainly on the debate within the WTO, I will examine the progress made both there and in other forums and the current status of the debate.

The third chapter of the thesis will cover the fairly new, and in literature not yet well established, concept of *development friendly competition policy*. Drawing from the theory of competition policy itself and the conditions within, and experiences of, developing countries, the chapter will attempt to outline what could constitute development friendly elements of competition policy. The chapter will tackle three major miss-conceptions regarding competition policy in developing countries. First, that competition policy is not needed for developing countries. Second, that competition policy and industrial policy cannot co-exist and that the latter is far more important for developing countries and, finally, the misconception that developing countries should simply replicate the competition policies of industrial countries.

The fourth chapter will focus on competition policy within some of the newer RTAs, the EU/ACP EPAs. Starting with a brief outline of EU/ACP relations, the chapter will then examine the reason behind creating EPAs. Finally in this chapter will follow a general assessment of the competition policy provision found in the EPAs, with particular focus on SSA.

The fifth and final chapter will constitute the analysis, where the feasibility of development friendly competition policy within the confines of the EPAs will be assessed. Essentially, the goal is to examine the possibility of establishing a sustainable situation where development friendly competition policy and international competition policy can co-exist.

2 Competition policy

This chapter is aimed at providing a theoretical framework for competition policy. First, I will discuss the role of competition and its gains on efficiency and welfare. Second, competition policy will be defined and its general principles and objectives described. Following this will be a description of common aspects and components of competition policy. Finally I will briefly outline history and evolution of competition policy in three industrial countries each having a slightly different competition policy background: the US, the EU and Japan.

2.1 The role of competition

There are two general types of competition: price competition and non-price competition. As the name implies, price competition takes place over prices. In markets characterized by limited competition, such as monopolies or oligopolies, firms are price-setters. But in competitive markets, firms become price-takers, meaning that the market determines the price at which firms are either forced to sell or to exit the market. While price competition certainly is an important part of competition, one which we easily can distinguish in our immediate economic surroundings, non-price competition might be of even greater importance. Most commonly, we see non-price discrimination in the form of advertising and research and development (R&D). These two are generally employed by firms in attempts at avoiding price competition by differentiating their products from those of other firms.⁴ A good example is over the counter pharmaceuticals, for instance painkillers, where the established brands seek to avoid price competition with generic producers by the means of extensive advertising campaigns. Advertising is hard to perceive as improving efficiency or driving innovation. On the contrary, efficiency improvement and innovation are the explicit goals of R&D. The results include new improved products or increased productivity.

⁴ Pepall 2005: 502, 507

2.1.1 Market power, efficiency and welfare

Market power gives rise to *allocative inefficiencies*, which in turn result in welfare losses.⁵ Competition on the other hand can help achieve welfare efficient outcomes, shown by the two *Theorems of Welfare Economics*.⁶ Whereas firms holding substantial market power have lower incentives to innovate, firms in competitive markets are forced to compete by raising their productivity, either by means of increased investment, innovation or more efficient business practices.⁷ The end result is improved efficiency and improved welfare.

2.1.2 Maximum versus Optimum competition

Though competition is important, perfect competition is virtually unattainable, and even undesirable, in real world economics. The rationale is that adding more competition to an already competitive market is not necessarily efficient. For each new firm entering the market, the market share of other firms decrease, lowering the concentration in the market. This is supported by *The Schumpeterian hypothesis* which states that the possibility for technological progress is greater in concentrated, yet still competitive, markets than in those with many small firms.⁸ Therefore, since maximum competition is not generally desirable, there must be some level of optimum competition. The question, however, is how to find that level and how to attain it. This is where competition policy becomes important.

2.2 Competition policy – definitions, objectives and common components

As discussed above, competition between companies encourage them to innovate and to improve their productivity, becoming more efficient. The results are better products, more varieties and lower prices. Although *perfect competition* may be unattainable, efforts to ensure that markets work properly and are free from competition distorting practices are essential to virtually every single industrial country. The shape and form of these efforts may vary from one country to another, but they all have in common their underlying goals and their general principles.

⁵ Motta 2004:40

⁶ Perloff 2004:326

⁷ Motta 2004:56-7

⁸ Pepall 2005:502

According to a common definition, competition policy is “... *the set of policies and laws which ensure that competition in the marketplace is not restricted in way that is detrimental to society.*”⁹ In this definition there is a clear distinction between competition policy and competition law. This is not always the case and, in fact, sometimes competition law and competition policy are used synonymously. Competition law refers to the set of *legal rules* established aimed at maximizing the national welfare by ensuring that competition is not distorted¹⁰, and are, just as the name implies legally binding provisions. Competition policy, on the other hand, is a much broader concept, outlining “... *the set of measures and instruments used by governments that determine the ‘conditions of competition’ that reign on their markets.*”¹¹ It might not be directly derivable from the two aforementioned definitions, but competition law can be distinguished from competition policy as targeting only private firms, whereas competition policy may target both the private sector and the government.¹² Naturally, competition laws can exist in themselves without being enforced. Enforcement requires the establishment of a competition authority, which by law is granted powers of investigation and prosecution. Though there could be made a distinction between the competition law and competition policy, in many cases the latter is used to encompass also the former. In this thesis, I will do just that, effectively using the term *competition policy* as consisting of both competition law and policy.

To the original figure below by Sengupta and Dube has been added a further distinction to competition policy. Apart from merely eliminating barriers of entry and exit, competition policy may also encompass work to actively encourage competition, here referred to as *competition advocacy*. More precisely what such measures may entail will be discussed further in the Development Friendly Competition Policy chapter.

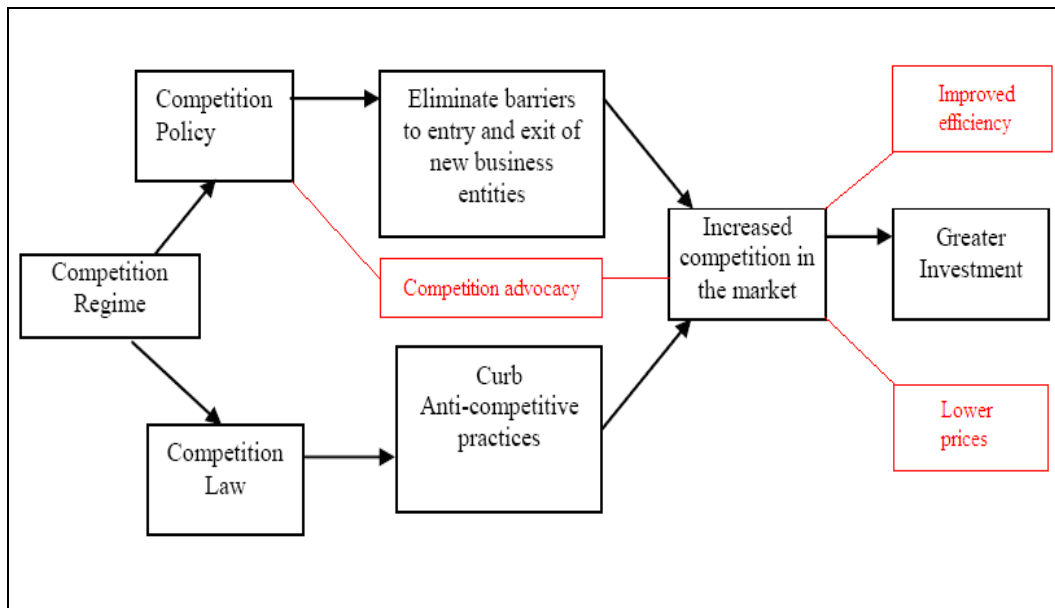
⁹ Motta 2004:30

¹⁰ Hoekman & Holmes 1999:2

¹¹ Ibid

¹² However, in some countries competition law may target the public sector as well. In the EU, for instance, the distortion of competition through state aids to firms are prohibited by Article 87 of the EC Treaty.

Figure 1: *The taxonomy of competition policy and law.*



Source: Sengupta & Dube 2008:4

The ultimate goal of competition, according to Sengupta and Dube, is greater investment.¹³ This certainly holds true, but may be seen as somewhat limited. The desired end result of increased competition is a better functioning market, which in turn *should* result in improved efficiency via increased productivity and innovation and lower prices. Improved efficiency is always a goal within economics which should also translate into lower prices. Of course, efficiency may still improve absent competition, but will then not necessarily translate into lower prices. With the objective of lower prices in mind, one may tend to think of competition policy as consumer protection, but this is only partly true. When recalling the definition of competition policy, avoiding detrimental effects on society and maximizing national welfare only means avoiding dead-weight losses. This, in turn, does not take into consideration transfers between consumer surplus and producer surplus.

2.2.1 Common aspects and components

Competition policy is an elusive concept, making generalizations on its precise content difficult. However, at a bare minimum, one can identify three important components of virtually any competition policy: rules on *collusion*, *abuse of dominance* and *mergers*.

¹³ Serupta & Dube 2008:4

Generally, collusion is co-operation between otherwise would-be competitors. The goal of collusion is practically always price setting. In a competitive market, firms are price takers, whereas a monopoly firm is a price setter. Through explicit price setting, firms may set prices which are close to the monopoly price.¹⁴ The same outcome may be reached if colluding firms divide up the market amongst each other, allowing a firm to act as a monopolist in its assigned market segment or area. Colluding firms are usually referred to as members of *cartels* or *trusts*, the most famous and still active is OPEC. Fighting collusion has been on the top of the agenda of competition authorities in many industrial countries.

Abuse of dominance, or dominant position, is different from collusion in the sense that it normally entails one firm acting alone. Typically, the behavior of individual firms is not targeted by competition policy, but by consumer policy, environmental policy and/or labor policy. Individual firms are under ideal circumstances disciplined by the market itself. But when a firm is large enough, which is usually determined by its market share, its actions may go unchecked. The character of the dominant firm's practices, or abuses, is either *exclusionary* or *exploitative*. The goal of exclusionary practices is to exclude competitors either from entering the market or forcing them to exit, or both. *Predatory pricing* and *tying*, for instance, fall into this category. Exploitative practices are essentially practices where a dominant firm uses its position to extract higher prices from customers, which typically can be achieved via price discrimination. Price discrimination is not illegal per se. In fact, it is common practice in many markets.¹⁵ Normally, price discrimination can be countered by re-sale or parallel imports. But when a dominant firm price discriminates, it could use its market position to enforce non-re-sale clauses with its customers, effectively preventing parallel imports.¹⁶

While rules on fighting collusion and abuse of dominance are applied *ex-post*, investigating and prosecuting observed behavior; merger regulation is *ex-ante*. This means that the *potential* or *expected* effects of mergers are evaluated. Essentially the goal of merger regulation is to prevent concentration, or even monopolization. For instance, a competition authority may block mergers where the market share of the resulting firm is high enough to consider the firm dominant.

¹⁴ Motta 2004:138

¹⁵ Airlines are particularly skilled, and dependent, on price discrimination.

¹⁶ Motta 2004:125

2.3 Competition policy in the industrial countries

While competition has been recognized as important for centuries, competition policy is quite young. In the U.S., competition policy is more commonly referred to as *anti-trust policy*. The 19th century was characterized by a massive American economic expansion. But much of the economic activities in such important areas as oil, steel, railroads and finance were influenced by extensive collusion. In 1890 the federal government passed the *Sherman Act*, aimed at stopping the anti-competitive behavior of the cartels and trusts. The Sherman Act prohibits anti-competitive practices and attempts at monopolization. Since the Sherman Act lacked provisions on mergers, the federal government passed the *Clayton Act* in 1914.¹⁷ Since their inception, these acts have been amended repeatedly, but remain the source of American competition policy.

Much of the practical work in the field of competition policy takes place in two places: the courtroom and the academic world, each of course influencing the other. A later development in the academic world, which has come to influence American anti-trust case law substantially, is the emergence of the *Chicago School* of economics. Its main proponents, such as Robert Bork, believe government intervention in the field of anti-trust is both unnecessary and potentially harmful and that cooperation and mergers can have substantial gains in terms of efficiency.¹⁸ American competition policy has thus come to be characterized by less of a *per se illegality* approach, instead emphasizing *rule of reason*.

European competition policy has two dimensions: firstly that of the member countries individually and secondly that of the Union as a whole. Although historically important, the national competition policies of the EU member states are now of less importance, since they are now expected to conform to EU competition policy. Furthermore, for competition issues relating to the common European market, EU competition policy has supremacy over national competition policy. The Treaty of Paris, signed in 1951, gave birth to the EU competition policy.¹⁹ Since then, the EU competition policy provisions have been adopted in the Treaty of Rome, signed in 1957. Due to their broad nature, the provisions were left to interpretation by the European Commission, under supervision of the European Court of Justice. This has meant that case law has played a pivotal role in the evolution of EU competition policy. Aside from the traditional, economic objectives of competition policy, EU competition policy

¹⁷ Motta 2004:1-5

¹⁸ Bork 1993

¹⁹ Motta 2004:13

adds the objective of market integration.²⁰ Today, the EU competition provisions are found primarily in articles 81 (collusion) and 82 (abuse of dominance) of the Treaty. In addition to these rules, mergers are governed by the Merger Regulation 139/2004.²¹

There are two major differences between EU and U.S. competition policy. First, the assessment of dominance where, in the EU, a firm is said to be dominant when having 40-50% of the relevant market compared to over 60% in the U.S. Secondly, the EU has kept a rigid per se illegality approach, while the U.S., as previously mentioned, has increasingly moved towards rule of reason.

While U.S. and European experiences with competition policy are similar, the path chosen by Japan has until recently been quite different. Prior to World War II, the Japanese economy largely favored co-operation over competition. The economy was dominated by the *Zaibatsu*, massive, vertically integrated industrial and financial conglomerates.²² Following Japan's defeat in 1945, efforts were made aimed at dismantling the *Zaibatsu*. But instead, new vertically or horizontally integrated business alliances emerged, the goals of which were to restrict market access in order to protect domestic Japanese firms from foreign competition. The years to follow are described as the *Dark-Ages of Japanese competition policy*²³, even though the Antimonopoly Law (AML) and its enforcement agency, the Fair Trade Commission of Japan (JFTC) were established during that period. Japan turned to extensive industrial policy as a tool for economic development. However, since 1972, Japan's position has moved towards coherence with western norms of competition and competition policy. Even more recently, Japan has cooperated with the U.S. on competition policy, gradually adopting more and more of the U.S. approach.²⁴ This could be seen as a result of repeated clashes between the two countries over competition and market access issues.

²⁰ Steiner & Woods 2003: 397-398

²¹ Korah 2004:338

²² Schwindt & McDaniels 2007:43-46

²³ Schwindt & McDaniels 2007:57

²⁴ Schwindt & McDaniels 2007: 45, 58, 62-68

3 International competition policy

This chapter, building upon the previous chapter, will expand the concept of competition policy into the international field. The chapter will discuss the ongoing debate on international competition policy, primarily within the WTO, outlining the underlying rationale for this debate as well as examining the stance of the different players. In addition, this chapter will explore the international policy debate within other, less formal forums, such as the UNCTAD and the OECD.

3.1 The debate at the WTO

The fundamental rationale behind establishing an international competition policy is the breakdown of trade barriers. Through the negotiations within GATT, and subsequently the WTO, tariff trade barriers have been steadily reduced. Although inducing free trade, the tariff reductions have highlighted the existence of other, non-tariff, trade barriers. These have in common that they are *behind the border* and thus falls under the jurisdiction of the sovereign state. Such practices may have indirect effects on trade, constituting *policy spillovers* created by domestic policy.²⁵ Many of these behind the border practices may be employed to such an extent that they could replace the tariff barriers, consequently eroding the gains from trade liberalization.²⁶ The debate in the WTO has revolved largely around three key concerns: behind the border practices, most notably in the form of export cartels and international cartels, the potential abuse of market power by large multinational corporations and, finally, the global merger movement.

The behind the border practices can, depending on their type, be employed by either the private business sector or by the government. For business practices such as collusion to work, the government, via its national competition policy, must condone that behavior. This can only mean one of two things: either the national competition authority looks the other way, disregarding the cartel's negative effect on domestic welfare, or the effects of the cartel are not felt in the home country. Even though strong interest groups, for instance representing the country's perceived key industries, may influence the national competition

²⁵ Hoekman & Saggi in Evenett & Hoekman 2006:439

²⁶ Bilal & Olarreaga 1998:4-6, Hoekman & Mavroidis 2003:2.

authority, the most credible answer is that the observed anti-competitive practice has no home market effect. Since national competition policy only aims to maximize *national* welfare by preventing market distortions, the national competition authority will neglect the effects of its policies on the welfare of the rest of the world.

3.1.1 Export cartels and international cartels

Export cartels are an example of policy spillovers. Export cartels are “... *agreements between competitors that are designed to exploit market power on foreign markets...*”²⁷. Since export cartels produce only for exports, thus not having any effect on the home country’s welfare, national competition authorities have no real incentive to discipline such cartels. An export cartel can increase producer surplus at home, without lowering consumer surplus, thus being welfare enhancing at home. Instead, the rest of the world will bear the burden of reduced welfare.²⁸ There is generally nothing that stops national competition authorities from using domestic competition policy to stop export cartels, but it requires both will and technical ability. Developing countries, particularly, lack the technical ability.²⁹ It is therefore the role of international competition policy to either explicitly ban export cartels, to force national competition authorities to discipline them or to in some way induce the home country to internalize the effects of the export cartels. This role could be played by a Multilateral Agreement on Competition Policy (MACP).

International cartels are not the result of policy spillovers per se, but they do cause spillover effects. An international cartel can be said to consist of firms from different countries, having anti-competitive effects on the same market.³⁰ While export cartels certainly are international by nature, international cartels do not have to be export cartels. An export cartel operates in at least two distinct geographical markets, essentially producing in one market and selling in another. To illustrate, think of OPEC, the Organization of the Petroleum Exporting Countries. The OPEC can be described as a cartel in the sense that its members are cooperating over output rationing of crude oil production, which in turn leads to price maintenance. The effects of this are felt globally, even on the domestic markets of the OPEC members³¹. Consequently, OPEC is an international cartel, but not an export cartel. Though developing countries may want to endorse export cartels within their own countries, international cartels can have severe

²⁷ Hoekman & Mavroidis 2003:10

²⁸ Bilal & Olarrega 1998:2, 6-7

²⁹ Evenett & Hoekman 2006:439

³⁰ Hoekman & Mavroidis 2003:11

³¹ However, the domestic petroleum prices can be subsidized by using the monopoly profits from the cartel. Venezuela, for instance, has the world’s lowest gas price at \$0.04 per liter.

consequences for developing countries, both in terms of prices, in foreclosure and exclusion of domestic firms and in exploitation of consumers. It is exceedingly difficult to measure the *global* impact of international cartels, but in the U.S. alone, the OECD estimates that in overcharges and economic waste, ten international cartels alone cost the American economy well over \$2 billion.³²

3.1.2 Cross-border abuse of dominance

Where international cartels create strong market power, this can also be achieved without inter-firm cooperation. The growth, and subsequent behavior, of large multinational corporations is a source of concern for many developing countries.³³ Although the abuse of market power, dominance, can be targeted by national competition policy many countries, even industrial countries, lack the resources to successfully investigate and prosecute such behavior.³⁴ A particular source of concern is the inability to exchange information across borders. This information is crucial when determining the potential dominance of a firm. It is exceedingly difficult for a domestic competition authority, lacking such information, to assess the level of dominance of a firm on foreign markets.³⁵

3.1.3 Cross-border mergers

The third concern ties in with the market power issue. In 1999, cross-border mergers and acquisitions (M&A) made up almost 80% of global foreign direct investment (FDI).³⁶ The growth of M&A has been such that some economists speak of a global merger wave.³⁷

Mergers between large transnational corporations can create cross-border effects. Specifically, domestic competition authorities want to be able to control mergers which create strong market power for the combined firm, especially if the firm is of foreign origin. Mergers with international spillovers are a source of conflict between different competition authority jurisdictions. A situation could arise where one competition authority approves a merger in its jurisdiction, while another does not. There have been several such examples between the competition authorities of the EU and the U.S., for instance the Boeing/McDonnell Douglas

³² Winslow 2001:120

³³ Singh 2002:22

³⁴ Hoekman & Holmes 1999:15, Singh 2002:23

³⁵ Normally, dominance is required on the affected market. But following cases in the EU, such as Tetra Pak II, it has been established that dominance can be *transferred* from one market to another.

³⁶ World Investment Report 2000:117

³⁷ Singh 2002:15

and GE/Honeywell mergers.³⁸ Where the competition authorities of industrial countries can clash over such mergers, developing countries generally cannot. An MACP could alleviate the aforementioned problems, but that would entail evaluating the *global* effects of a merger. This, in turn, would require reaching an agreement on clear standards for merger assessment.³⁹ The inconsistency of such standards is at the very root of the aforementioned U.S./EU merger conflicts, so reaching an agreement may be very difficult.

These concerns have gradually been introduced into the world trading system. In fact, they date back to the Havana Charter of 1948, where the drafts on the creation of an International Trade Organization (ITO) included a section on competition policy. But since the charter was left unratified and focus subsequently shifted towards tariff reductions, the prospects for an international competition policy slipped away.⁴⁰ Not until 1996, with the Singapore Ministerial Meeting, did the issue once more reach the top of the agenda.

3.1.4 Progress

The Singapore Ministerial Meeting resulted in the so-called Singapore Issues. These issues included non-tariff related trade barriers in the areas of investment, competition, government procurement and trade facilitation.⁴¹ Another more concrete result of The Singapore Ministerial Meeting was the establishment of a working group to study the interaction between trade and competition.⁴² This working group, The Working Group on the Interaction between Trade and Competition Policy (WGTCP), was encouraged to draw upon existing work carried out in the field, particularly by within the UN.⁴³ The group's discussions, based upon submissions by WTO members, has touched upon the possibility of achieving harmonization among national competition policies, for instance by member states' agreeing on competition policy core principles.⁴⁴ The group has also discussed the use of the WTO's dispute settlement mechanism to settle competition policy disputes between member states and the feasibility of establishing a supranational, International Competition Authority (ICA). The WGTCP failed to reach any conclusive results in any of these fields and largely due to the failure of the Cancun multilateral trade talks, competition policy was dropped from the Doha Round agenda and the work of the WGTCP was suspended.

³⁸ Hoekman & Holmes 1999:8, Hoekman & Mavroidis 2003:2.

³⁹ Hoekman & Holmes 1999:9, Hoekman & Evenett 2006:447

⁴⁰ Bilal & Olarrega 1998:1, Paasman 1999:29.

⁴¹ Evenett & Hoekman 2006:154

⁴² Davidow & Shapiro 2003:56 footnote 59

⁴³ Singapore Ministerial Declaration, 1996, article 20.

⁴⁴ Hoekman & Mavroidis 2003:5

Much could be said of the varying positions held by the WTO members on international competition policy. But in general terms, international competition policy is supported by industrial countries and largely opposed by developing countries. However, this has not always been the case. Initially, developing countries' concerns over the potential behavior of large multinationals lead these countries to advocate an agreement on international competition policy. Since then, however, tables have turned.⁴⁵ The most avid supporter of international competition policy is the EU. The EU position can be traced back to the findings of the Van Miert Report in 1995. First of all, the report acknowledges the effects of globalization on competition policy, for instance shown by the increasing number of large cross-boarder mergers. The EU recognizes that, although desirable in itself, globalization creates problems that go beyond national borders, such as export cartels.⁴⁶ The EU also recognizes that most WTO members already have competition policy, or are in the process of developing it, but a growing number of competition policy authorities, with different goals and policy choices have the potential of creating new problems. While the EU has successfully carried out bilateral competition policy cooperation with the US, the EU points out the difficulties in doing so with the growing number of competition authorities. To remedy this, the EU believes competition policy cooperation should be carried out on the multilateral level also. The proper forum would be the WTO.⁴⁷ The EU supports establishing an ICA, although realizing that the outlook for the creation of such is quite bleak.

The U.S. too must be considered being in overall support of international competition policy, but the U.S. hesitation and go-slow approach has contributed to the faltering of the issue. The U.S. concern is primarily with delegating the powers of its national competition authority to an international authority, thus losing sovereignty over its competition policy.⁴⁸ This concern ties in with the fear that multilaterally agreed rules, which will take precedence over national rules, will be inferior to existing national rules. Consequently, the U.S. argues foremost for unilateral action or bilateral coordination and cooperation, but not explicitly for an MACP.⁴⁹

The most unwavering opponents against international competition policy are the developing countries. Few people would question the importance of a national competition policy for developing countries, but the issue of the need for international competition policy for developing countries is far from settled.⁵⁰ There is a general reluctance among developing countries to introduce further disciplines of non-tariff trade barriers into the WTO. The experiences from TRIPS

⁴⁵ Singh 2002:31

⁴⁶ Van Miert Report 1995:3-4

⁴⁷ Speech by Jean-François Pons, DG Competition, 2002:3-4.

⁴⁸ Hoekman & Holmes 1999:3-4, Bilal & Olarrega 1998:13.

⁴⁹ Paasman 1999:40.

⁵⁰ Hoekman & Holmes 1999:15.

have proven to developing countries that they lack both the experience and the institutional structures to handle such agreements.⁵¹ However, though generally opposed, many developing countries still recognize the need for international rules on competition. Developing countries are primarily worried, like the EU, with the aforementioned cross-border abuse of dominance by multinational corporations and the observed global merger wave.⁵²

3.2 Other forums for debate

Parallel to the WTO, and for a longer period of time, the UN has dealt with competition policy under the auspices of the United Nations Conference on Trade and Development (UNCTAD). In 1972, the UNCTAD established an expert group in order to study the topic. The main results were twofold. Firstly, the group formulated a set of principles and rules to control anti-competitive behavior. These rules were adopted by the UN General Council in 1980. Secondly, the UNCTAD took into special account the situation of developing countries, acknowledging their need for special and differential treatment.⁵³ Currently, the work of the UNCTAD focuses on how a potential MACP, or ICA, might affect developing countries. The UNCTAD is exploring three venues for ensuring development gains, the first being how a developing country should model its own national competition policy. Secondly, influencing the design of the MACP/ICA itself. And finally, building technical and institutional capacity to implement and enforce both domestic competition policy and an MACP/ICA.⁵⁴ The UNCTAD's main function, however, has been that of a forum for discussion, where, unlike in the WTO, issues can be raised and discussed without risking potential repercussions in negotiations in other areas.⁵⁵ The influence of the UNCTAD should not be underestimated, even though its results are non-binding and non-enforceable within the UN context.

The Organization for Economic Co-operation and Development (OECD) has also carried out work on international competition policy, the focus of which traditionally has revolved around domestic competition policies within its member states. More recently, however, the OECD has also ventured into the field of international competition policy. The OECD's work has largely dealt with the concept of *contestability*. This concept relates to the entry and exit barriers of a market. The idea behind contestability is that firms in a contestable market are

⁵¹ Singh 2002:31

⁵² Paasman 1999:41-2

⁵³ Paasman 1999:30-31.

⁵⁴ See for instance Note by UNCTAD Secretariat, 2007.

⁵⁵ When the Doha round dragged on and Cancun failed, members wanted to put trade negotiations back on track by removing the newly added areas of for instance competition policy.

disciplined by the mere threat of entry. And where entry is a distinct possibility, even dominant firms will refrain from employing anti-competitive behavior.⁵⁶ Recently, the OECD also has started discussing capacity building in developing countries. In doing so, the OECD recognizes the importance of not only competition policy in developing countries, but also of competition advocacy. According to the OECD capacity building and technical assistance in developing countries requires not only funding, but also coordination of the different organizations involved in the capacity building process.

Apart from the WTO, the UNCTAD and the OECD, there are more informal settings for discussing international competition policy. One such setting is the International Competition Network (ICN). The ICN was started in 2001 by competition policy officials from 14 countries, including both the EU and the US. Similar to the UNCTAD, the ICN functions as a venue for communication between competition authorities of the different countries. Rather than making rules, the ICN working groups makes recommendations and leaves up to the competition authorities to decide upon them.⁵⁷ Finally, it is also worth mentioning intergovernmental organizations (IGOs) dealing with international competition policy. One such is the South-Centre, an IGO serving as a think tank for developing countries.⁵⁸ The focus of the South-Centre is exclusively the impact of competition policy, domestic and international, on developing countries. Though interesting, it must be emphasized that the work of IGOs, such as the South-Centre, is by nature biased. But with this in mind, the work of the South-Centre provides excellent insight into the reservations and the demands but also the optimism of the developing countries' view on competition, competition policy and international competition policy.

⁵⁶ Paasman 1999:35

⁵⁷ <http://www.internationalcompetitionnetwork.org/index.php/en/about-icn>

⁵⁸ http://www.southcentre.org/index.php?option=com_content&task=view&id=13&Itemid=80

4 RTAs, EPAs and Competition Policy

This chapter explores the role of competition policy in Regional Trade Agreements (RTAs). The dramatic increase of RTAs in recent years has brought into question the future of multilateral trade negotiations. The bilateral nature of RTAs makes them a far more accessible path for countries seeking to bring non-tariff, behind the border policy-related trade issues onto the negotiating table. This chapter will address RTAs, starting with a brief outline of what RTAs are and why we are seeing a recent proliferation of such agreements. The next section will provide an example of RTAs which has drawn major attention; the Economic Partnership Agreements (EPAs) between the EU and the African, Caribbean and Pacific (ACP) countries. In this section, I will first discuss the relationship between the EU and the ACP countries followed by a brief description of the EPAs themselves and their *raison d'être*. Finally, competition policy will be brought into the RTA/EPA context. The intention is to provide a general understanding for the role of competition policy in RTAs and to identify specific competition policy provisions in the EPAs.

4.1 RTAs – Regional Trading Agreements

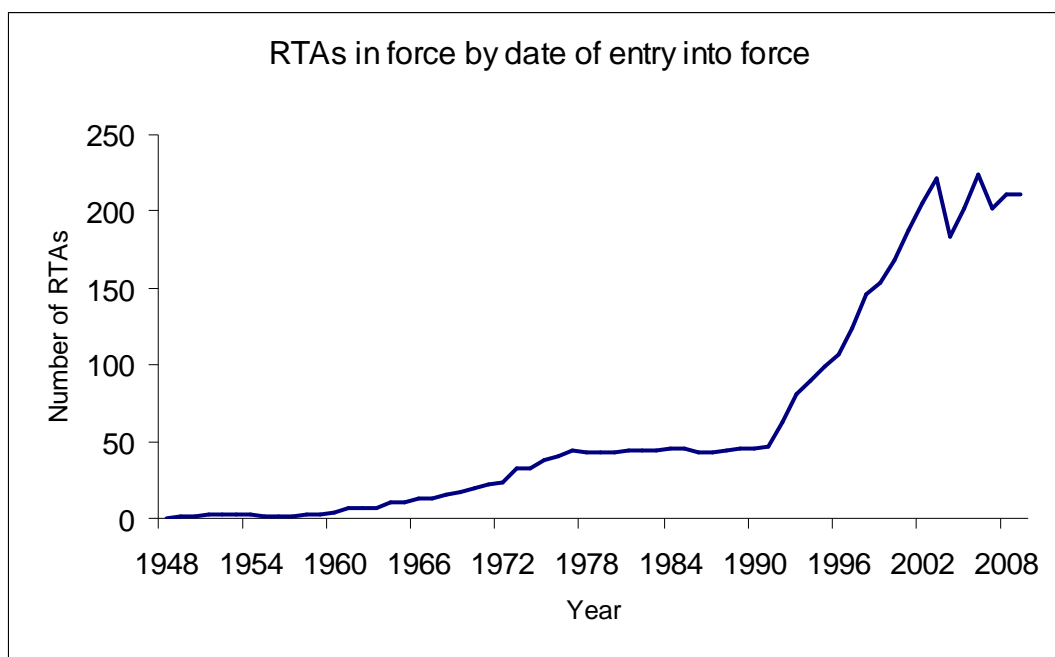
RTAs are by nature *preferential trade arrangements*, meaning agreements granting preferential trade status between participants. RTAs, therefore, are major departures from two major WTO principles: the *Most Favored Nation* and the *Non-discrimination* principles.⁵⁹ However, the WTO recognizes the need for RTAs and has opted to allow them within the multilateral trade framework, with the condition that such agreements between members must be reported to the WTO. Even so, there are growing concerns that “...*regionalism is causing harm to multilaterally-based trading relationships.*”⁶⁰

In recent years, there has been a substantial proliferation in reported RTAs, as shown in the chart below. But first, before any attempts at explaining this recent RTA-growth, I will provide a brief definition of the RTA concept.

⁵⁹ http://www.wto.org/english/tratop_e/region_e/regrul_e.htm

⁶⁰ Speech by WTO Director-General Pascal Lamy, 2007
(http://www.wto.org/english/news_e/sppl_e/sppl67_e.htm)

Figure 2: *The proliferation of RTAs.*



Source: WTO (http://www.wto.org/english/tratop_e/region_e/regfac_e.htm)

Preferential trade arrangements are generally of bilateral nature, but could also be multilateral. As opposed to the preferential treatment previously offered under the Special and Differential Treatment principle of the WTO, RTAs are by nature reciprocal, meaning that preferential market access is enjoyed by all the signatories.⁶¹ There are two general types of RTAs; Free Trade Areas (FTAs) and Custom Unions (CUs), the former being of greater interest for this thesis and in fact the more common of the two making up almost 60% of total RTAs.⁶² RTAs can also be seen as a tool for regional integration. Regional integration, in turn, is generally driven by motives of trade liberalization, but it could also create inter-country legal instruments and institutions, or even, as is the case of the EU, supra national bodies.

In the last ten years alone, the number of active RTAs has grown from 146 to 211 and in a longer time perspective, the increase of RTAs is even more dramatic.⁶³ Beside the reasons of regional integration and the subsequent creation or strengthening of regional economies⁶⁴, the proliferation of RTAs may be the result of the impasse in the WTO multilateral negotiations. For countries wishing to move forward more swiftly in areas other than tariff reductions, the bilateral

⁶¹ Special and Differential Treatment in the WTO meant preferential, non-reciprocal access to industrial countries' markets for the Least Developed Countries (LDCs)

⁶² http://www.wto.org/english/tratop_e/region_e/regfac_e.htm

⁶³ http://www.wto.org/english/tratop_e/region_e/regfac_e.htm

⁶⁴ Whalley 2008:529-31

arena may prove more suitable. Also, as mentioned above, some of the increase of RTAs may be explained by a greater will for regional integration. A murkier motive for creating an RTA is protectionism, which in RTAs could take two forms. First, although bilateral trade agreements liberalize trade *internally*, they are by nature exclusionary for non-participants. Second, bilateral trade agreements can be filled with exemptions, protecting sensitive sectors or even whole industries.⁶⁵ As I will show, the EU/ACP EPAs are being created in response to WTO rules, which partly could explain the increase in numbers of RTAs.

4.2 The Economic Partnership Agreements (EPAs)

The relationship between the European states and the African, Caribbean and Pacific (ACP) countries far outdates the EU. Historically, many European states have had special bonds with their former colonies. Over time, and with the inception of European regional integration, these special bonds were formalized via the Treaty of Rome in 1957. The first specific agreements were signed in the sixties, first *Yaoundé I* in 1963, followed by *Yaoundé II* in 1969. In 1975 *Yaoundé II* was replaced the *Lomé Agreement*, a more extensive agreement than the previous two. The preferential market access that was granted the ACP countries via the first two agreements remained in the *Lomé Agreement*. However, further attention was afforded to development aid through the European Development Fund (EDF). *Lomé* also saw the formal creation of the ACP group of countries.

4.2.1 The EPAs - what and why?

Although having preferential access to the European markets, the ACP countries' share of European imports actually fell, from 5.1% in 1970 to 1.5% in 2003.⁶⁶ This can be attributed to increased trade liberalization in the European countries, whereas the ACP countries have kept a stricter trade policy. Any hopes of continuing the *Lomé Agreement* was effectively extinguished by the WTO ruling that the preferential nature of the agreement was non-compatible with the WTO framework.⁶⁷ These factors have led to the inception of the Cotonou Agreement, which outlines EU/ACP co-operation in terms of political, trade and development dimensions.⁶⁸

⁶⁵ Trakman 2008:373

⁶⁶ Bormann et al 2005:169-170

⁶⁷ Bormann et al 2005:169 and GATT 1994 Article XXIV

⁶⁸ See http://ec.europa.eu/development/geographical/cotonou/cotonou2000_3_en.cfm

The Cotonou Agreement has two major impacts on the ACP countries. Firstly, trade between the EU and the ACP countries, which previously were non-reciprocal, are now to be of reciprocal nature. That is, in order to comply with the WTO regulations, the ACP countries must open their markets to EU trade. This will entail abolishing existing tariff barriers, which in turn will mean tariff revenue losses for the ACP countries. Some estimates put the losses as high as 40-60%⁶⁹ and with complete elimination of tariffs this could amount to an annual revenue loss of \$2.9 billion in Africa alone.⁷⁰ This creates a delicate, but substantial problem for the ACP economies, in that tariff revenues typically represent a significant part of total revenues. Secondly, other non-tariff related issues are put on the negotiating table, such as those of services, investment, procurement, intellectual property, labor, environment and last but not least competition policy.

4.2.2 Competition policy in the RTA/EPA context

RTAs increasingly contain competition policy related provisions. The taxonomy of these, however, varies substantially between different agreements. The provisions range from those on co-operation and dispute settlement to direct rules concerning anti-competitive practices and anti-dumping. However, a general division can be made in terms of provisions on anti-competitive behavior and those relating to co-operation and co-ordination. The Cotonou Agreement contains three articles on competition policy. The first, article 45, reads:

"The Parties agree that the introduction and implementation of effective and sound competition policies and rules are of crucial importance in order to improve and secure an investment friendly climate, a sustainable industrialisation process and transparency in the access to markets."

The subsequent articles provide specific guidance. Article 46 stipulates that *competition law* is to be implemented and broadly which types of practices that are to be targeted, in other words in the characteristic style of the anti-competitive behavior provisions that many RTAs have in common. Finally, article 47 specifies, although in broad terms, co-operation and co-ordination on competition policy issues.

As seen, the provisions on competition policy in the Cotonou Agreement are quite general in scope and limited in specifics. However, the Cotonou Agreement

⁶⁹ Kennan & Stevens 2005:4

⁷⁰ Perez & Karingi 2007:1880.

is a framework agreement, serving as a base for the more specific negotiations of the EPAs.

4.2.3 Competition policy in the SADC EPA

Since negotiations of most of the EPAs have currently not yet reached conclusion, it is difficult to provide a clear picture of the agreements' competition policy contents. Here, however, I will provide an example of EPA competition policy by describing the competition policy provisions of an EPA currently under negotiation: the EPA between the EU and the Southern African Development Community (SADC).

The draft⁷¹ from June 2007 of the EU/SADC EPA contains competition policy provisions somewhat more specific than those of the Cotonou Agreement, but not by much. The draft starts by outlining the general principles of competition and competition policy, with special reference to collusion and abuse of market power.⁷² This text is very similar to the provisions found in articles 81 and 82 of the Treaty of Rome, particularly in the sense that both lack exhaustive lists of what behavior amounts to collusion and abuse. The second article stipulates the implementation of national competition laws. Nothing is said of either how these laws are to be designed or how they are to be implemented. The article does, however, provide a timeframe for the implementation. The third article relates to co-operation and exchange of information. There seems to be particular focus on the latter, affording the competition authorities the right to exchange information. Co-operation is further covered by article five, which establishes the importance of *capacity building* and *technical assistance*. This co-operation is to cover four areas: assisting in drafting legislation, exchanging experts, training personnel and ensuring the proper functioning of the competition authority.

An interesting observation is that the draft contains no explicit references to international competition policy concerns, such as export cartels. Yet, there is nothing in the broad wordings of the articles that excludes international competition policy related issues. What is more surprising is the lack of reference to mergers. In all, the draft contains only one area of specific concern for developing countries: the difficulties and costs of efficient implementation of competition policy. These limitations are not unique to the SADC draft; the EPA draft for the Economic Community of West African States (ECOWAS) contains virtually identical provisions.⁷³ The implication, of course, is that there will have to be considerable negotiations before any comprehensive competition policy can be agreed upon.

⁷¹ This draft is the EU proposal which serves as basis for negotiation

⁷² SADC EPA draft 05.06.2007.

⁷³ ECOWAS EPA draft 04.04.2007

4.2.4 Possible negotiation outcomes

It is exceedingly difficult to speculate on the specific outcomes of such negotiations. But it is possible to generalize over the potential outcome, in the sense that there are three general types of an EPA competition policy agreement.

The first type is an agreement characterized by harmonization. The main component of such an agreement is the identification for common competition law principles, ensuring a minimum standard of sort.⁷⁴ Harmonization means bringing two systems closer together. But in the case of harmonizing an extensive system with a limited one it is highly plausible, if not for certain, that the limited system will have to grow far more than the extensive system will shrink. In fact, the U.S. position on competition policy in the WTO highlights this, in that the major reservation the U.S. has towards international competition policy agreements is that the agreed principles will be inferior to existing national ones. Similarly, it is hard to imagine the EU allowing its own competition policy principles and laws being replaced by less extensive or even inferior ones. The conclusion thereof is that harmonization of EU and ACP competition policies will entail more than a fair share of competition policy *exports*. This, as I will explain in the next chapter, can have substantially adverse effects on a developing country.

A second type of agreement could consist of a co-operative framework. Such an agreement usually entails the signatories agreeing to utilize its domestic competition policy to target certain practices deemed undesirable from a competition point of view. This would in other words mean so-called *best endeavors*, where countries agree *what* to pursue, but not necessarily *how* to do it. This is more in line with the provisions in the Cotonou Agreement, than is harmonization. The third path is purer co-operation agreements. Here, general co-operation is emphasized over harmonization or best endeavors. The co-operation could take on a variety of shapes, for instance information exchanges, technical assistance in creating a domestic competition policy and capacity building to implement it.⁷⁵

Clearly there is a wide range of negotiation outcomes, which in turn are affected by negotiating power and the general understanding of competition and competition policy. It is likely that the limited expertise in the ACP countries will limit their ability to ensure a development favorable outcome. That is, if there actually is such a thing.

⁷⁴ Okediji 2006:11

⁷⁵ Okediji 2006:12-3

5 Development friendly competition policy

As seen in the previous chapter that the competition policy provisions of the EPAs are broad and do not offer much in terms of the particular design of the competition policies of the ACP countries. But this offers room to discuss the competition policy needs of developing countries, essentially what can be referred to as *development friendly* competition policy.

Therefore, this chapter will address competition policy from a developing country perspective. In line with the previous chapter, the basis will be the ACP countries, particularly those of Sub-Saharan Africa (SSA). This chapter begins with the pivotal question: Do developing countries need competition policy? Then I will discuss the concern of competition policy potentially preventing the use of industrial policy. The third section will cover the spread of industrial country style competition policy among developing countries. Having laid the foundation for the developing countries' need for competition policy, and alleviating some of the more theoretical concerns, the final section of this chapter will discuss the preconditions for establishing competition policy in developing countries, particularly the obstacles, *and* opportunities, that present themselves when attempting to do so.

5.1 The need for competition policy

Clearly, as shown in the previous chapters, there is mounting pressure on the developing countries to establish competition policy. In fact, many developing countries have already done so, either unilaterally or under influence by industrial countries. Many developing countries do have competition laws, but the question must be raised whether these laws are working, or for that matter, if they are at all enforced. Hence, there is room for a debate on the role of, and even the need for, competition policy in developing countries.

The first stepping stone is the sentiment that developing countries do not need competition policy. Some studies do show that competition in developing countries is potentially as healthy as in industrial countries.⁷⁶ But lacking concrete

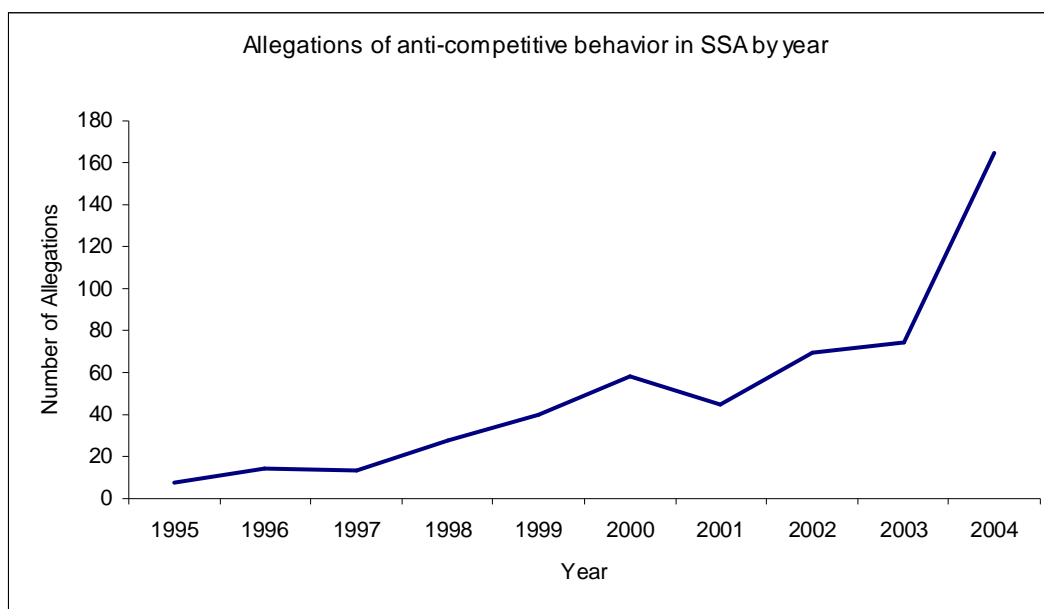
⁷⁶ Singh 2002:7

empirical evidence, and considering the relatively poor functioning of the formal economy, claiming that developing countries do not need competition policy is a stretch. Also, even if competition *currently* is healthy in these countries, failing to safeguard this competition may have dramatic consequences in the future. This connects with the notion that forthcoming domestic privatizations and trade liberalization will have a profound influence on developing countries' economies. And ultimately, even though competition may exist, so it seems do anti-competitive practices.

5.1.1 Evidence on anti-competitive practices

An empirical survey by Evenett, Jenny and Meier examines the occurrence of *alleged* anti-competitive practices in SSA. The survey makes a number of interesting observations. First, there is an increasing trend in alleged anti-competitive practices. Second, the increase has been particularly dramatic over recent years. Third, the number of allegations increases for both domestic and foreign firms. Finally, the sample also shows that the most common anti-competitive practices in SSA are collusion, anti-competitive mergers and abuse of dominance (including monopolistic practices and predatory pricing).⁷⁷ The figures below show the number of allegations of anti-competitive behavior by year and type respectively.

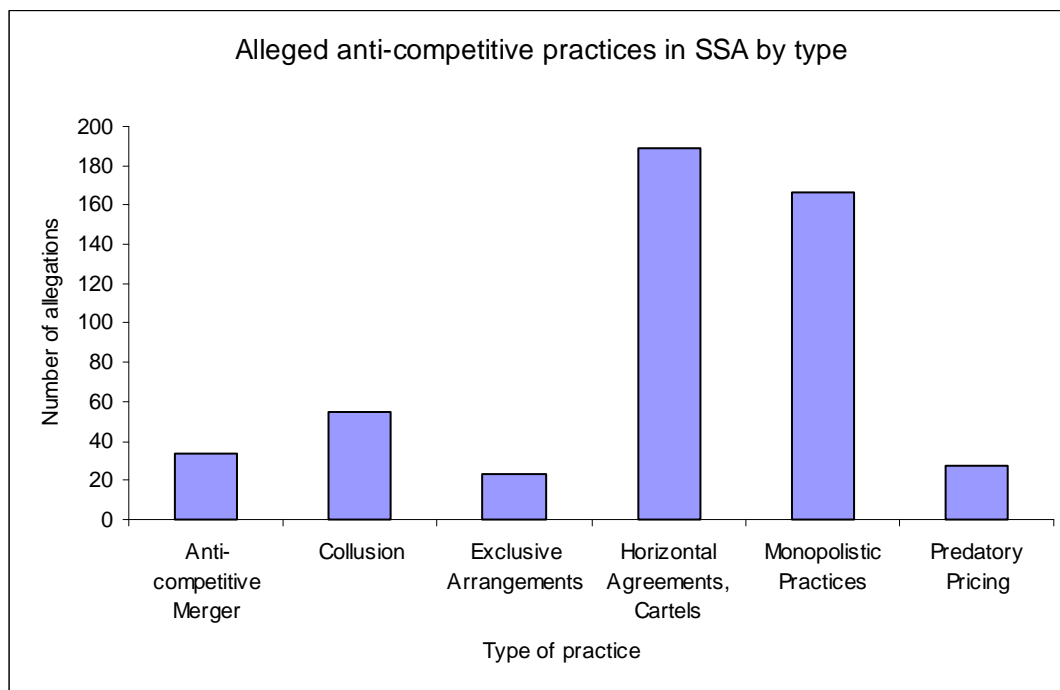
Figure 3: *Allegations of anti-competitive practices in SSA*



Source: Constructed from Evenett et al 2006:13

⁷⁷ Evenett et al 2006:12

Figure 4: Common types of anti-competitive practices in SSA



Source: Constructed from Evenett et al 2006:12

One of several conclusions that could be drawn from this survey is that there is a *perceived* increase in anti-competitive practices. But whether this increase stems from a *real* increase in anti-competitive practices or from improved awareness, it is hard to say. Another conclusion is that the dramatic increase over recent years could be explained by greater openness of the SSA countries' economies. The conclusion of greater openness is supported by the presence of alleged anti-competitive practices by foreign firms. The number of alleged anti-competitive practices involving foreign firms has actually increased more than those involving domestic firms.⁷⁸ This openness may cause, or be the effect of, privatization and liberalization and consequently greater participation on the SSA markets by foreign firms. Finally, the three most common types of alleged anti-competitive behavior can all have the international dimension mentioned in the international competition policy chapter. The overall conclusion from the survey is that there are indeed anti-competitive practices in developing countries and thus that there is a real need for competition policy.

⁷⁸ Evenett et al 2006:9

5.1.2 Liberalization and privatization

The study has several implications for developing countries. Firstly, privatization of formerly state owned firms and monopolies, particularly those in utilities, may run the risk, absent enforced competition policy, of creating *private* monopolies. This could possibly explain the increase in monopolistic practices observed by the survey. Such practices could spoil much of the gains from privatization, if not directly for the government itself then at least for domestic consumers. Second, liberalization of trade policies, such as that incurred by RTAs, makes countries more susceptible to international influences.⁷⁹ Such influences may come in many forms and have diverse effects, detrimental or beneficial. Many developing countries had small, closed economies, often controlled by the government. This was achieved by either state monopolies or by direct intervention.⁸⁰ True, with the possibility of direct intervention there is little need for an explicit competition policy. But at the same time it is evident that the mere possibility of direct intervention does not serve well to attract investment, domestic or foreign.

Although it could be argued that some such economies worked, at most, decently, no one will argue that they were efficient and growth oriented. With growing democratization, carrying with it increased liberalization, the option of using direct government intervention is shrinking. Also, when previously closed economies are getting more and more open, becoming players in today's global economy, they are also subject to mounting pressures from their environment. This is made evident by the rise in RTAs. Where these countries formerly had preferential market access to industrial countries' markets, but with the ability to limit access to their own, they must today open up for market access for their RTA trading partners. Of course, it would be reckless to argue that this is overall a bad thing, since this by all accounts is what globalization and trade liberalization seek to accomplish.

5.1.3 Three areas of concern

For developing countries, there are mainly three types of competition related and potentially detrimental effects stemming from trade liberalization. The first is collusion, in the form of cartels, the numbers of which are increasing in SSA according to the survey. These can have severe adverse effects on a developing country's economy. While such arrangements would find themselves hard pressed against the well established competition policies of the industrialized world, even

⁷⁹ Hoekman & Mavroidis 2003:7

⁸⁰ Singh 2002:11

these, faced with *international* cartels, may fall short.⁸¹ Hence the need for international competition policy, but this, in turn, would require developing countries to have a competition policy of their own. Furthermore, developing countries will need competition policy to address the problem created by both domestically harmful cartels as well as their own export cartels. Of course, as previously mentioned, a competition authority can opt to disregard the effects of export cartels since they are only felt abroad. But the indirect effects, in the form of reduced confidence on behalf of their trading partners or worse yet, the utilization of such counter-measures as anti-dumping, may prove substantially harmful. While the enforcement of national competition policy cannot guarantee that trading partners refrain from using anti-dumping measures, there is still some evidence that it *may* be successful. For instance, between the EU member states and between New Zealand and Australia, competition rules have completely replaced anti-dumping provisions.⁸²

A second potential problem for developing countries is cross-border abuse of dominance. Large, powerful multinational corporations (MNCs) may prove a challenge for developing countries. Under well established and well enforced competition policy, the behavior of such firms is checked and disciplined. Attempts at monopolization, exploitation or exclusion can be discouraged or prosecuted when necessary. A developing country with a non-existent, barely enforced or poorly functioning competition policy is not well versed for taking on the exclusionary or exploitative practices by domestic firms and particularly not those of dominant MNCs. With attracting foreign direct investment as an ever more cited device for economic development, growth and competitiveness, the will to by other means target the anti-competitive behavior of large MNCs is conceivably even less among the country's leadership. The only plausible national safeguard: a well established competition policy, enforced by a committed and independent competition authority, combined with international agreements on competition policy co-operation and information exchange.

Finally, as has been discussed to greater lengths in the international competition policy chapter, there is the international dimension of mergers and acquisitions.⁸³ Although the survey results do not say so explicitly, it is plausible to conclude that, for the most part, the anti-competitive mergers include foreign firms, either merging with each other or with a domestic firm. Here there are two main discernable risks for developing countries. Firstly, closely related to abuse of dominance, the massive entities created by the recent wave of mergers are likely to achieve substantial, if not dominant, market power. This, in turn, could be wielded to exclude existing or potential competitors, particularly in the developing countries. Secondly, budding, prosperous developing country firms

⁸¹ For instance OPEC, a quantity setting cartel which works remarkably well anywhere in the world.

⁸² Whalley 2003:55 footnote 48

⁸³ Singh 2002:14-15

may be vacuumed up by MNCs, in efforts to gain market access, to limit competition when already on the market or to gain access to technology. While there are positive aspects to this, such as technology transfers, it could also have adverse effects on the degree of competition as well as on jobs. Furthermore, it is important for developing countries to achieve growth of their small enterprises, if not into large corporations, but at least into medium-size employers.

5.2 Competition policy versus Industrial policy

There seems to be a growing concern among developing countries that competition policy may limit their ability to employ industrial policy.⁸⁴ One could even discern a belief that competition policy *contradicts* industrial policy and that the latter is more important for developing countries. There is some truth to this; industrial policy has proved pivotal for the economic growth of most industrial countries. This connects with the *infant industry argument*, that protecting domestic industry will in time allow it to grow competitive. This might be true in the short-run, but in the long-run, only through fully exposing domestic industry to competition can full competitiveness be developed.⁸⁵ For instance, proponents of the infant industry argument commonly point to Japan and Korea, where co-operation was initially favored over competition. Over time, competition has grown more and more important, as indicated by the revitalization of Japanese competition policy. The Korean government too favored co-operation over competition, but competition still proved to be fierce with substantial inter-firm rivalries.⁸⁶

But in recent years, the use of industrial policy and co-operation has gained some momentum, particularly in public-private endeavors, so-called *cluster initiatives*, formed to create agglomerations. Economic theory and empirical evidence point to agglomerations as a driving force for competitiveness by way of innovation and increased productivity. Since developing countries today compete primarily through low labor costs and natural resources, government supported cluster initiatives are seen by many as the best way towards economic growth and development for poor countries. Though cluster initiatives to some extent must involve co-operation, clustering and inter-firm co-operation is not equivalent to collusion. In fact, competition is vital for the survival of a cluster.⁸⁷ Furthermore, co-operation in clusters usually take place *vertically* between firms, that is, between firms upstream and downstream, not horizontally. In many

⁸⁴ Bhattacharjea 2006:297-8

⁸⁵ UNCTAD 2004:324

⁸⁶ UNCTAD 2004:324

⁸⁷ Porter 1998:79-80, 86

industrial countries, vertical co-operation between firms can be targeted by competition policy. Developing countries' choice of competition policy could, and perhaps should, therefore provide some leeway for public-private cluster initiatives as well as, to a certain extent, other forms of vertical co-operation.

5.3 Exporting competition policy

The competition policies of the industrial countries are well established and successful, thus the likelihood that industrial countries will seek to export their successful competition policies to developing countries. This is precisely what harmonization *could* amount to. It may be tempting for many developing countries to adopt the competition laws of the industrialized world and be done with it, possibly even receiving some aid in return. But this is a dangerous path. Introducing competition laws, which may be compatible with the level of development of the industrialized world but not with that of the developing world, is likely to make enforcing them exceedingly difficult. And, as found by the World Bank “*Merely adopting some other country’s laws and formal regulations is no guarantee of achieving the same institutional performance*”⁸⁸. This point of view is drawn upon the fact that many developing countries lack the institutional capacity to both implement and enforce such extensive and advanced competition policy.⁸⁹ What is more, developing countries may miss the particular development oriented aspects of competition policy, that is, gradualism in its implementation flexibility in its enforcement and, finally, *competition advocacy*.

5.4 Preconditions, obstacles and opportunities

Implementing competition policy in developing countries is subject to a range of preconditions, obstacles and, not to forget, opportunities. This section will address this with focus on three major issues: *institutional capacity*, *the informal economy* and *competition advocacy*. Note that it is not clear which of these adhere to which issue. In fact, each of them could be said to be concerned with preconditions, obstacles and opportunities.

⁸⁸ World Bank 2005:5

⁸⁹ Okediji 2006:14

5.4.1 Institutional capacity

There is a real concern among developing countries regarding the difficulties and the costs associated with the implementation and enforcement of competition policy. There has therefore been identified a real need for technical assistance and capacity building. The first could be said to relate primarily to assistance in drafting the competition laws and designing the enforcement bodies, or competition authorities.⁹⁰ Capacity building too ties in with the establishment of the competition authorities, but it covers a broader area than that. Successful competition law enforcement requires more than a competition authority. It requires first and foremost a functioning judicial system and additional, supporting governmental agencies. For instance, the competition authority could, and probably should, liaise with consumer protection agencies and development agencies to ensure a balanced outcome. Hence, capacity building can never merely be about establishing a competition authority, which, if other fields are not taken into account, will soon find itself impotent and incapable of fulfilling its purpose.

Building capacity and offering technical assistance is of course important, but will it be sufficient? Even with massive capacity building and technical assistance the strain on a developing country's institutional environment may turn out excessive. So instead of simply focusing on offering help to implement competition policy, there must be some considerations of how implementation can be best achieved. Here there are two key concepts: *gradualism* and *flexibility*. Gradualism means that everything is not implemented at once. Implementing everything at once is a real prospect when developing countries are induced to import industrial countries' competition policy. There is a distinctly possible path for the implementation of competition policy in establishing first the ultimate goals of competition, such as an efficient, productive and competitive market. The next step would be settling on broad, fundamental principles on what types of behavior are considered harmful. Gradualism then means increasing the level of enforcement as well as expanding the principles. Flexibility on the other hand means taking into account the special circumstances surrounding developing countries, for instance allowing, to a certain degree, the use of industrial policy.

With gradualism, competition policy in developing countries can be allowed to *mature*, much like it has done in the industrialized world. As competition policy matures, flexibility ensures that it does not counter-act the effects of other policies or reforms. But institutional capacity, capacity building, technical assistance, gradualism and flexibility cannot alone guarantee a successfully implemented competition policy. In many ACP countries, particularly those in SSA, the large informal economy constitutes a significant hurdle, but, perhaps, also an opportunity.

⁹⁰ OECD 2003:13

5.4.2 The informal economy

A major concern for developing countries is their large, and growing, informal economies. On the African continent it is estimated that the informal economy makes up approximately 60-70% of all non-agricultural and urban employment. Further, more than nine of ten new jobs are created in the informal economy. Counting agriculture, these numbers are even substantially larger. In the OECD countries, by comparison, the corresponding figure is 17%.⁹¹ For SSA in particular, and rather in terms of the informal economy's share of GNI, the average size of the informal economy is over 40%. The figures range from the lowest in South Africa, with below 30%, to the highest in Nigeria, Tanzania and Zimbabwe, all reaching almost 60%.⁹² The direct implications of a large informal economy are of course loss of potential tax revenues and lack of market regulation. But why do these countries display such large informal economies, and what are their impacts on competition policy?

There are a number of factors that affect the size of the informal economy, such as lack of infrastructure, institutions etc. For competition and competition policy, however, it is interesting to study the ability to enter the *formal* economy. A healthy economy is symbolized by the ability of firms to enter the market, to struggle and compete, and to exit when they cannot. Naturally, market entry decreases market concentration and increases market competition. In a market, entry and exit is determined by the ability to make long-term profit. There will almost always be entry costs in the form of sunken capital, but the decision to enter the market is made on the basis that these can be recovered long-term and that variable costs are covered short-term. But with *barriers* to entry, the potential entrants are faced with additional sunk costs that must be recovered. Exit also matters in a firm's decision to enter the market. When exiting a market, a firm can recover some of its entry costs. But with barriers to exit, the costs of exit increases and thus the ability to recover entry costs decreases. But how does this apply to developing countries? Beside all the difficulties adhering to physical infrastructure, market entry and exit appear more difficult in developing countries than in industrialized ones, whether due to bureaucracy or corruption, or both. Consequently, it is interesting to study the size of some important factors affecting entry and exit.

The World Bank annual report *Doing Business* compares countries over a range of factors, determining the investment climate and, simply, the climate for doing business. The 2005 report *Doing Business 2005: Removing Obstacles to Growth*, offers special attention to SSA. In reference to entry, two factors are particularly important: How long does it take to start a firm and how much does it

⁹¹ Xaba et al 2002:3 and Dessy & Pallage 2001:1 (taxes, inequality and size of the informal sector)

⁹² Verick 2006:5

cost? Exit is not as straightforward: how long does completing a bankruptcy take and how much can be recovered?

Starting with entry, it takes on average 63 days to start a business in SSA, costing on average 224% of the BNI per capita. The lowest corresponding figures in the industrialized world are 2 days (Australia) and 0.0% (Denmark).⁹³ The measurement gives a solid indication: starting a business in SSA is expensive and time consuming. The picture for exit is similar. It takes long to complete a bankruptcy and the recovery rate is low. In SSA it takes on average 4 years to complete a bankruptcy, compared to 0.4 years in Ireland, the lowest in the industrialized world. The average recovery rate in SSA is 19%, compared to Japan's 92.4%. So in SSA, it takes a long time to get out and when you do, you have lost approximately 81% of your investment.⁹⁴

Yet, if market entry is low and market exit is low, can that not mean existing firms actually *are* competing? Yes, but if they were to face the risk of new entrants, spurred by the ease to enter, and exit if need be, they would have to compete even harder and to innovate more to stay ahead and to become even more efficient. This perception of the role of competition policy is widely supported, for instance by the UNCTAD, which hails eliminating barriers to entry as one of the most important roles of competition policy.⁹⁵ The OECD too considers this, in connection with its often cited *contestability* approach.

What then are the risks of trying to implement competition policy with such a strong informal economy? Firstly, the enforcement of competition policy will be confined to the formal economy and the effects on the economy as a whole will thus be limited. Even worse, imposing new rules and enforcing competition policy in the formal economy may result in large transfers to the informal economy. As shown earlier, the growth of the informal economy is already substantial and the apparent ease by which it grows indicates that transfers from the formal economy may be a distinct possibility. Therefore, it is important that the ease of entry, ease of exit and the benefits from remaining in the formal economy are strengthened. This is best achieved by removing barriers to entry, barriers to exit and by coordinating the policies of various domestic agencies. This in turn should constitute the expanded role of a domestic, development oriented competition policy.

⁹³ Doing Business 2005:6

⁹⁴ Doing Business 2005:19

⁹⁵ UNCTAD 2004:326

5.4.3 Competition advocacy

Competition advocacy is important for developing countries in the sense that industrial countries already display a healthy culture of competition, whereas this *may* not be as well established among some developing countries. While the role of competition authorities in industrial countries primarily consists of monitoring and disciplining anti-competitive behavior, the role of developing countries' competition authorities must be broader, with added attention to competition advocacy. This role, both teaching people the virtues of competition and coordinating other policy reforms, could easily be overseen when modeling the competition policy after that of the industrialized world.⁹⁶ Competition advocacy can be described as having two dimensions. The first is that of removing existing barriers to competition, such as those described in the previous chapter. The second is creating, reinforcing and/or stimulating competition culture. This, of course, can be achieved by way of a variety of means, but often cited are the use of contests.

In industrialized countries, contests have clearly had an effect on competition. There are numerous examples, but in an effort to connect to the aforementioned clusters, I particularly wish to highlight the use of contests in cluster initiatives. Both Germany and Sweden have utilized this concept, trying to inspire regions to compete over who can present the most competitive cluster. Another way of seeing it is that the contests, which typically offer some kind of subsidy or support as a reward, induces different regions to reveal their competitiveness. I believe the same concept can be employed in developing countries' economies, albeit on a smaller scale. In these countries, such contests could have the dual effect of both encouraging entrepreneurial spirit and providing an incentive to enter a market. Coordinating this policy with industrial policy could *potentially* create substantial growth in the formal economy. The agency best suited to adopt, oversee and coordinate this policy is the competition authority.

5.5 Concluding remarks: fitting development friendly competition policy in the EPAs

This study has covered a vast area in economics, ranging from trade liberalization to competition policy to economic development. Connecting these lines is not an easy task. But this study has attempted to show that there is indeed a connection between competition and competition policy on the one hand and economic development on the other. Constructing a competition policy which is

⁹⁶ UNCTAD 2004:327

development friendly is not effortless, but it *is* possible. But the prospects of doing so in the context of international trade in general and the EPAs in particular are not as straightforward.

The EPAs will have profound impacts on the ACP countries' economies. On the negative side, a substantial part of these impacts will be on tariff revenue, which will effectively be slashed. This will in turn erode the income base for the ACP countries' governments, a major concern for many ACP countries. The result *could* be substantially reduced income *and* substantially increased expenditure, the latter stemming from costly competition policy implementation. However, the distinct possibility of using competition policy to stimulate growth in the formal economy could serve to counteract the revenue loss, replacing *tariff revenues* with *tax revenues*. Increasing tax revenues has long been a goal for developing countries but the tools to achieve this have been lacking.

The EPA context presents an opportunity to establish competition policy, both by means of increased focus on competition, trade and liberalization and also by receiving support from the EU. In line with the importance of gradualism and flexibility in implementing competition policy, the developing countries need to *own* the process. In other words, allowing the EU to dictate the agenda, and the competition laws to be stipulated, will erode the prospects for development friendly competition policy. Not in the sense that the competition policy is *anti-development*, but in the sense that the development friendly aspects are overlooked and forgotten. Selling the concept of gradualism to the EU might actually be quite trouble-free, particularly if the EU is involved in establishing the pace and the timeframe for *full* competition policy implementation. Flexibility is another matter, but could be viable if ensuring that the flexibility does not create what the EU fears the most; export cartels. Nevertheless, with the prospect of reprisals in form of anti-dumping measures, there is little cause for the ACP countries to encourage, or simply ignore, such cartels. In fact, there is a possibility for a trade-off: the ACP countries concede to a direct ban of export cartels, being rewarded by the EU agreeing to exclude the possibility of using anti-dumping measures.

How ever the EPA negotiations may play out, the ACP countries should not lose focus on that competition policy is not only a must, but also a strong tool for development, growth and economic prosperity.

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Edited. Originally sourced from Sengupta & Dube 2008:4.

Figure 2: *The proliferation of RTAs.*

Source: www.wto.org/english/tratop_e/region_e/regfac_e.htm)

Figure 3: *Allegations of anti-competitive practices in SSA.*

Source: Constructed from Evenett et al 2006:13.

Figure 4: *Common types of anti-competitive practices in SSA.*

Source: Constructed from Evenett et al 2006:12

8 Appendix

Anti-competitive practices data

Year	Number of Articles	Percentage	Number of Allegations	Percentage	Number of Different Types of Anti-competitive Practices	Percentage
1995	9	1.40%	8	1.55%	8	1.33%
1996	16	2.48%	14	2.72%	19	3.16%
1997	14	2.17%	13	2.52%	15	2.50%
1998	30	4.66%	28	5.44%	33	5.49%
1999	44	6.83%	40	7.77%	52	8.65%
2000	72	11.18%	58	11.26%	68	11.31%
2001	50	7.76%	45	8.74%	49	8.15%
2002	93	14.44%	70	13.59%	80	13.31%
2003	90	13.98%	74	14.37%	83	13.81%
2004	226	35.09%	165	32.04%	194	32.28%
Total	644	100,00%	515	100,00%	601	100,00%

Source: Evenett, Jenny, and Meier (2006)

Type Anti-competitive Practice	Entire Sample		Entire Example Except South Africa		South Africa		1995-2001		2002-2004		Anti-competitive Practices in which Foreign Firms were Mentioned		Anti-competitive Practices in which Foreign Firms were Accused	
	N	%	N	%	N	%	N	%	N	%	N	%	N	%
Abuse of Dominant Position	39	6.32%	16	3.73%	23	12.23%	15	5.95%	24	6.58%	11	7.80%	10	8.62%
Anti-competitive Merger	33	5.35%	13	3.03%	20	10.64%	19	7.54%	14	3.84%	10	7.09%	8	6.90%
Barriers to Entry	8	1.30%	6	1.40%	2	1.06%	2	0.79%	6	1.64%	2	1.42%	0	0.00%
Bundling	1	0.16%	0	0.00%	1	0.53%	0	0.00%	1	0.27%	0	0.00%	0	0.00%
Collusion	55	8.91%	29	6.76%	26	13.83%	24	9.52%	31	8.49%	12	8.51%	10	8.62%
Contractual Discrimination	4	0.65%	1	0.23%	3	1.60%	2	0.79%	2	0.55%	1	0.71%	1	0.86%
Creation of a Monopoly	3	0.49%	2	0.47%	1	0.53%	2	0.79%	1	0.27%	2	1.42%	2	1.72%
Cross-subsidiation	3	0.49%	1	0.23%	2	1.06%	1	0.40%	2	0.55%	0	0.00%	0	0.00%
Denial of Infrastructure	6	0.97%	1	0.23%	5	2.66%	2	0.79%	4	1.10%	1	0.71%	0	0.00%
Exclusive Arrangements	23	3.73%	9	2.10%	14	7.45%	13	5.16%	10	2.74%	6	4.26%	6	5.17%
Hoarding	4	0.65%	4	0.93%	0	0.00%	0	0.00%	4	1.10%	1	0.71%	1	0.86%
Horizontal Agreements, Cartels	189	30.63%	142	33.10%	47	25.00%	87	34.52%	102	27.95%	35	24.82%	27	23.28%
Minimum Resale Price	3	0.49%	1	0.23%	2	1.06%	1	0.40%	2	0.55%	1	0.71%	1	0.86%
Monopolistic Practices	166	26.90%	155	36.13%	11	5.85%	53	21.03%	113	30.96%	42	29.79%	34	29.31%
Predatory Pricing	27	4.38%	17	3.96%	10	5.32%	9	3.57%	18	4.93%	10	7.09%	9	7.76%
Tying	3	0.49%	1	0.23%	2	1.06%	1	0.40%	2	0.55%	1	0.71%	1	0.86%
Vertical Agreements	7	1.13%	3	0.70%	4	2.13%	2	0.79%	5	1.37%	2	1.42%	2	1.72%
Violation of Merger Control Regulations	5	0.81%	1	0.23%	4	2.13%	0	0.00%	5	1.37%	0	0.00%	0	0.00%
Unspecified Practices	38	6.16%	27	6.29%	11	5.85%	19	7.54%	19	5.21%	4	2.84%	4	3.45%
Total	617	100,00%	429	100,00%	188	100,00%	252	100,00%	365	100,00%	141	100,00%	116	100,00%

Source: Evenett, Jenny, and Meier (2006)

ACP countries

Angola
Benin
Botswana
Burkina Faso
Burundi
Cameroon
Cape Verde
Central African Republic
Chad
Comoros
Congo (Brazzaville)
Democratic Republic of Congo
(Kinshasa)
Cote d'Ivoire
Djibouti
Equatorial Guinea
Eritrea
Ethiopia
Gabon
Gambia
Ghana
Guinea-Bissau
Guinea
Kenya
Lesotho
Liberia
Madagascar
Malawi
Mali
Mauritania
Mauritius
Mozambique
Namibia
Niger
Nigeria
Rwanda
Sao Tome and Principe
Senegal
Seychelles
Sierra Leone
Somalia
South Africa
Sudan
Swaziland
United Republic of Tanzania
Togo
Uganda
Zambia
Zimbabwe
Caribbean
Antigua and Barbuda
The Bahamas
Barbados
Belize
Dominica
Dominican Republic
Grenada
Guyana
Haiti
Jamaica
St. Kitts and Nevis
St. Lucia
St. Vincent and the Grenadines
Suriname
Trinidad and Tobago
Pacific
Cook Islands
Federated States of Micronesia
Fiji
Kiribati
Marshall Islands
Nauru
Niue
Pacific Islands (Palau)
Papua New Guinea
Solomon Islands
East Timor
Tonga
Tuvalu
Vanuatu
Samoa

SADC member states

Angola
Botswana
Democratic Republic of Congo
Lesotho
Madagascar
Malawi
Mauritius
Mozambique
Namibia
South Africa
Kingdom of Swaziland
Tanzania
Zambia
Zimbabwe

ECOWAS member states

Benin
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Cape Verde
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Ghana
Guinea
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Liberia
Mali
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Nigeria
Senegal
Sierra Leone
Togo