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# The Objectives of Competition Law

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**Abstract:** *This essay examines the nature of competition law objectives by visiting some of the theoretical and philosophical foundations underlying competition law. The key objectives of competition law are welfare, efficiency, and free and fair competition. There are distributive dimensions in competition law that are related to different notions of welfare (consumer surplus and producer surplus). The different types of efficiencies are subject to trade-offs – within a given time (allocative versus productive) and inter-temporally (static versus dynamic). Theoretical, conceptual, and philosophical frameworks also influence competition law objectives.*

***Keywords*:** Competition, Competition Law
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# 1. Introduction

Competition law has become increasingly prevalent in many countries. Its spread has been accompanied by greater familiarity with many of the objectives associated with competition law. Such objectives are often stated in competition laws. Does this mean that there is a consensus on competition law objectives? Students of competition law may be forgiven for thinking that such objectives are 'common knowledge' and uncontroversial.

The presumption of a universally acceptable set of objectives is the key premise underlying manuals and model competition laws for countries embarking on the implementation of their own national competition laws (World Bank-OECD, 1999; UNCTAD, 2010). These manuals and models provide tailor-made definitions and templates that countries can use to draft their competition laws without (so it was thought) much controversy and at lower cost (time and money). Contrary to these beliefs, competition law objectives can be controversial and can affect enforcement priorities (Brodley, 1987).

Staying mostly within the confines of mainstream economics, it is plausible that Brodley (1987) has just scratched the tip of an iceberg. If license is granted to explore some of the theoretical and philosophical foundations that underpin the 'economics of competition law', additional insights are likely to emerge on the nature of competition law objectives.

The main goal of this essay is to examine the nature of competition law objectives by visiting some of the theoretical and philosophical foundations of competition law. This is undertaken on a step-by-step basis by firstly presenting the 'mainstream' or 'consensus' statements on competition law objectives (Section 2). The question of why these objectives assumed their current form is then examined by relating it to the economic principles underlying competition law. This is followed by an analysis of how competition law objectives and their implications can potentially be altered in the face of alternative and/or more recent theories and empirics in economics (Section 3). Taking this further, an even more fundamental shift in the foundations of competition law objectives is attempted by examining philosophical issues relating to theories of justice (Section 4). How all these stand and relate to the enforcement of competition law is discussed in relation to institutional and political economy factors (Section 5).

## 2. The Objectives of Competition Law

> Few people dispute that antitrust's core mission is protecting consumers' right to the low prices, innovation, and diverse production that competition promises. (Hovenkamp, 2005, p.1).

The raison-d'être of any law or regulation often manifests itself in the form of its objectives. This applies to competition law as well. However, the objectives of competition law are sometimes not explicitly stated either in the law or guidelines. In some cases, the objectives can only be inferred indirectly from statements, speeches, or presentations by representatives from competition law enforcement agencies.

### 2.1. Statement of Objectives

It can be argued that it is important to state the objectives of competition law as these objectives often exert influence on how the law is to be interpreted and enforced (Kaplow, 2014). This is true when there are multiple ways to interpret the objectives that are associated with competition law. For example, given that there are differences between consumer welfare and efficiency, which should be emphasized? This would depend on which objectives are emphasized in a given country's law. Such statements of objectives can become even more important when trade-offs exist between two or more objectives, for example, consumer welfare, efficiency, and equity.

Taking the view from the other side, are there any benefits from not explicitly stating the objectives of a competition law? A competition law that does not contain an explicit statement of purpose perhaps can be considered an 'incomplete law' – a concept highlighted in Pistor and Xu (2003). Such 'omissions' could be unintentional due the poor drafting of the law. It could also be intentional so as to render more flexibility in the interpretation of the law to deal with unforeseen changes in the future. Theoretically, it is impossible to incorporate all possible future states in a law. Irrespective of the reasons underlying incomplete law, such laws are likely to confer more flexibility as well as discretionary powers to the courts which are then said to

have more 'residual law making power' (Pistor and Xu, p.933). In so far as the executive (that is, politicians) have powers to appoint an attorney general and senior judges, such incompleteness provides room for politicians to influence the overall direction of competition law enforcement. Thus, incomplete competition law may influence the 'norms' of competition law enforcement (Kovacic, 2003). The lack of an explicit statement on competition law objectives could also allow politicians to accommodate and pursue more than one objective.

Finally, it is also important to ask whether it matters how and where such objectives are stated, that is, whether formally in the law itself and in the enforcement guidelines, or more informally through speeches and presentations. The degree of flexibility differs in each of these cases.

### 2.2. Competition Law Objectives and Their Interpretations

The 'modern' versions of competition law were first implemented in the United States in the late 1890s and in many other countries since then.[1] For a law that has been around for some time and one in which is strongly based on economic principles, is there a need to discuss the objectives of competition law? Is there not a consensus on the objectives of competition law? A perusal of some of the major textbooks and articles on the subject provides a list of main objectives of competition law (Jones and Sufrin 2008; Whish 2001):[2]

- Economic welfare – consumer, social, public, or total welfare
- Economic efficiency (allocative, productive, and dynamic)
- Free and fair competition

There are also other objectives that are less-often stated in competition law – some of which go beyond economics and that may be ideological in nature such as:

- Freedom (liberty and dispersal of economic power)

[1] Competition laws are likely to have existed in the ancient world. See Dunham (2007) for a discussion of competition law in Ancient Greece.

[2] The objectives of competition law are often discussed together with that of competition policy. Note that the above objectives are different from statements on objectives that are based on the types of anti-competitive business practices (actions) that are prohibited. For example, the objectives of competition law in UNCTAD (2010, p.3) are stated as: 'To control or eliminate restrictive agreements or arrangements among enterprises, or mergers and acquisitions or abuse of dominant positions of market power, which limit access to markets or otherwise unduly restrain competition, adversely affecting domestic or international trade or economic development.'

- Socio-economic or public interest objectives such as employment, export promotion, economic development, national economic competitiveness, and productivity growth
- Economic integration (single or common market)

It is not uncommon for competition laws to have multiple objectives, though this could lead to conflicts and inconsistent applications (OECD, 2003). The presence of multiple objectives can also be seen in East Asian and Association of Southeast Asian Nations (ASEAN) countries. Table 1 provides a summary of the objectives of competition law in five ASEAN countries that have implemented national competition laws. With the exception of Thailand and Viet Nam, the objectives of competition law are stated in the law itself.

There is diversity in the stated objectives of competition law. A number of competition laws in these countries emphasize welfare (consumer and/or public), efficiency, free and fair competition, and economic development.

It is beyond the scope of this paper to discuss each in detail as this is done in many textbooks. We briefly discuss these objectives and more importantly, examine the relationships between some of these objectives.

## Table 1: Objectives in Competition Laws of Selected East Asian and ASEAN Countries

| Country | Objective Statement | Objectives |
|---|---|---|
| Japan<br><br>Source:<br>Act on Prohibition of Private Monopolization and Maintenance of Fair Trade (Act No. 54 of April 14, 1947) | The purpose of this Act is, by prohibiting private monopolization, unreasonable restraint of trade and unfair trade practices, by preventing excessive concentration of economic power and by eliminating unreasonable restraint of production, sale, price, technology, etc., and all other unjust restrictions on business activities through combinations, agreements, etc., to promote fair and free competition, to stimulate the creative initiative of entrepreneurs, to encourage business activities, to heighten the level of employment and actual national income, and thereby to promote the democratic and wholesome development of the national economy as well as to assure the interests of general consumers. | • Free and fair competition<br>• Entrepreneurship<br>• Employment and national income<br>• Democracy and development<br>• Consumer welfare |
| Republic of Korea<br><br>Source:<br>Monopoly Regulation and Fair Trade Act, 1980 | The purpose of this Act is to stimulate the creative initiative of enterprises, to protect consumers, and to strive for the balanced development of the national economy by promoting fair and free competition through the prevention of the abuse of market dominance and excessive concentration of economic power by enterprises and through regulation of improper concerted practices and unfair trade practices. | • Entrepreneurship<br>• Consumer protection<br>• Balanced development<br>• Free and fair competition |
| Indonesia<br><br>Source:<br>Law of the Republic of Indonesia No. 5 of 1999 Concerning the Ban on Monopolistic Practices and Unfair Business Competition | The objectives of this law are:<br>a. to maintain public interest and improve the efficiency of the national economy as one of the means to improve public welfare;<br>b. to create a conducive business climate through healthy business competition, thus securing equal business opportunity for large, middle, and small scale entrepreneurs;<br>c. to prevent monopolistic practices and/or unfair business competition by the entrepreneurs; and<br>d. to create effectiveness and efficiency in business activities. | • Public welfare<br>• Free and fair competition (equal business opportunities)<br>• Efficiency (effective and efficient business activities) |
| Malaysia<br><br>Source:<br>Competition Act 2010 | An Act to promote economic development by promoting and protecting the process of competition, thereby protecting the interests of consumers and to provide for matters connected therewith.<br><br>Whereas the process of competition encourages efficiency, innovation and entrepreneurship, which promotes competitive prices, improvement in the quality of products and services and wider choices for consumers." | • Economic development<br>• Process of Competition<br>• Consumer welfare<br>• Efficiency |
| Singapore<br><br>Source:<br>https://www.ccs.gov.sg/about- | The objective of the competition law in Singapore is to 'promote the efficient functioning of our markets towards enhancing the competitiveness of the Singapore economy. | • Efficiency<br>• Competitiveness of economy |

| | | |
|---|---|---|
| ccs/what-we-do/ccs-and-the-competition-act (Accessed 11 May 2015) http://www.mti.gov.sg/legislation/ Pages/Competition%20Act.aspx (Accessed 11 May 2015) | … In assessing whether an action is anti-competitive, we will also give due consideration to whether it promotes innovation, productivity or longer-term economic efficiency. This approach will ensure that we do not inadvertently constrain innovative and enterprising endeavours'. | |
| Thailand<br><br>Source: http://www.dit.go.th/en/backoffice/ uploadfile/255609191022214222490.pdf (Accessed 11 May 2015) | The Office of Thai Trade Competition, set up within the Department of Internal Trade, Ministry of Commerce, plays an important role to promote and establish rules for free and fair competition process to strengthen the country's economic system. The Trade Competition Act of 1999 is used as a tool for eliminating anti-competitive conducts and monitoring business to run their business with ethics. | • Free and fair competition |
| Viet Nam<br><br>Source: http://www.vca.gov.vn/ extendpages.aspx?id=9&CateID=194 (Accessed 11 May 2015) | The Viet Nam Competition Authority is a government agency established under the Ministry of Industry and Trade with the mandate of state management over competition, consumer protection, and trade remedies against imports into Viet Nam. | • Management over competition<br>• Consumer protection<br>• Trade remedies against imports |

*Source*: Compiled by authors.

### (a) Welfare

Welfare is, without doubt, a key objective of competition law. The question is whether one should emphasize **consumer welfare** (consumer surplus) or something more expansive such as **social welfare** (consumer and producer surplus) or **total welfare** (total value of output produced).

Even though social welfare is an important concept in economics, it is not often discussed in competition law and policy. This is because it raises complex distributive issues. For example, producer surplus in a monopoly market is much larger than in a competitive market. Given that monopoly firms have owners who are also consumers, the producer surplus might ultimately accrue to consumers. Less complicated is the notion of total welfare, which is the total value of output produced and consumed in society. In this regard, the goal of achieving maximum total welfare is derived from benchmarking against the perfectly competitive model.

Given that consumer welfare is a subset of social or total welfare, the decision on which to focus on can be analysed in terms of whether there is a need to look beyond consumer welfare when examining the effects of business practices. In other words,

should we consider compensating gains to any loss incurred in consumer welfare (due to higher prices and/or lower quantity and/or lower quality)?

Hovenkamp (2013) has argued that historically the United States' courts have chosen to emphasize actual consumer harm. As he pointed out, this resembles the notion of Pareto optimality involving two parties – consumers and producers. In other words, when consumers are harmed and the efficiency gains accrued to producers exceed consumers' welfare losses – the outcome is not Pareto optimal. This naturally leads to the application of the Kaldor-Hicks compensation criterion – in which producers compensate consumers for their welfare losses. The question that arises is how such compensation can take place ex-post.

**(b) Efficiency**

Another commonly stated competition law objective is efficiency. It can feature as an important consideration in merger reviews, vertical agreements, and abuse of dominance cases (OECD, 2013). Often, efficiency is associated with welfare such that the pursuit of efficiency brings about welfare maximization and vice versa. However, scholars have argued that efficiency does not always imply maximization of welfare (Brodley, 1987). To further dwell on this debate, it is useful to discuss the different types of efficiencies (allocative, productive, and dynamic) and whether there are trade-offs between them.

**Allocative efficiency** is achieved when goods and services are produced and distributed to consumers who value them the most. Allocative efficiency has also been defined technically as marginal cost pricing. **Productive efficiency** is related to cost minimization.[3] Both allocative efficiency and productive efficiency are considered to be static efficiencies. Static efficiencies are 'one-off' gains from improvements in resource allocation given that no change in technology takes place. To some extent, these concepts are associated with general equilibrium theory, which is essentially static in nature. Both social welfare and total welfare are maximized in perfectly competitive markets. Thus, for such markets – at least theoretically – efficiency coincides with welfare maximization.

[3] Another way of thinking about these efficiencies is that allocative efficiency is related to the 'what to produce' and 'for whom to produce' questions, while productive efficiency is related to 'how to produce'.

**Dynamic efficiency** results from technological progress. The time dimension is important as the efficiency gains from technological change take place over a long time. Such gains could take the form of improvements in production processes and/or new products and/or services. Compared to allocative and productive efficiencies, it is very difficult to estimate dynamic efficiencies. Part of this difficulty arises from the fact that it is difficult to determine ex-ante whether an innovation activity such as research and development (R&D) will result in actual innovation. A reflection of this is the modelling of innovation as a stochastic phenomenon.

The existence of three types of distinct economic efficiencies has led to two debates that emphasize trade-offs between different types of efficiencies. The first debate surrounds the trade-off between the two types of static efficiencies, namely allocative efficiency and productive efficiency. Is there a possibility that mergers would reduce allocative efficiency but increase productive efficiency? The Williamson (1968) trade-off model would be an example of this in which a merger results in price increase and lower production (marginal) cost. It is more difficult to find the opposite example in which production cost would rise but deadweight loss would decline. This is because any increase in production cost (especially variable cost) would presumably result in higher prices and lower quantity.

In the second debate, the trade-off is between static efficiency (allocative and productive) and dynamic efficiency.[4] Brodley (1987) has argued that dynamic (innovative) efficiency is more important than static efficiencies, due to the fact that technological progress has been the main factor driving economic growth in the United States and other industrialized countries. Table 2 shows such differences and provides a summary of sources of growth for selected countries from 1960–2000.

[4] Note that whilst dynamic efficiency shifts the production possibilities frontier, productive efficiency is still required to stay at this new frontier. Thus dynamic efficiency should be accompanied by productive efficiency to reap the benefits from the former.

**Table 2: Change in Output, Inputs, Technical Efficiency, Technology, and Total Factor Productivity, 1960–2000**

| Country | Output | Labour | Capital | Capital per Worker | Technical Efficiency | Technology | TFP |
|---|---|---|---|---|---|---|---|
| United States | 3.64 | 1.67 | 5.56 | 3.82 | –0.50 | 0.70 | 0.20 |
| Japan | 5.20 | 0.96 | 8.58 | 7.53 | –0.40 | 0.40 | 0.00 |
| Republic of Korea | 7.85 | 2.68 | 11.64 | 8.72 | 0.30 | –0.30 | 0.00 |
| China | 6.14 | 1.96 | 7.97 | 5.89 | 2.30 | –1.80 | 0.50 |
| Indonesia | 5.64 | 2.54 | 10.54 | 7.80 | 0.50 | –2.10 | –1.70 |
| Malaysia | 6.74 | 3.12 | 10.27 | 6.94 | –0.10 | –0.10 | –0.20 |
| Singapore | 9.46 | 3.66 | 13.65 | 9.68 | –0.10 | 0.90 | 0.80 |
| Thailand | 6.99 | 2.56 | 10.12 | 7.36 | 0.70 | –0.50 | 0.30 |

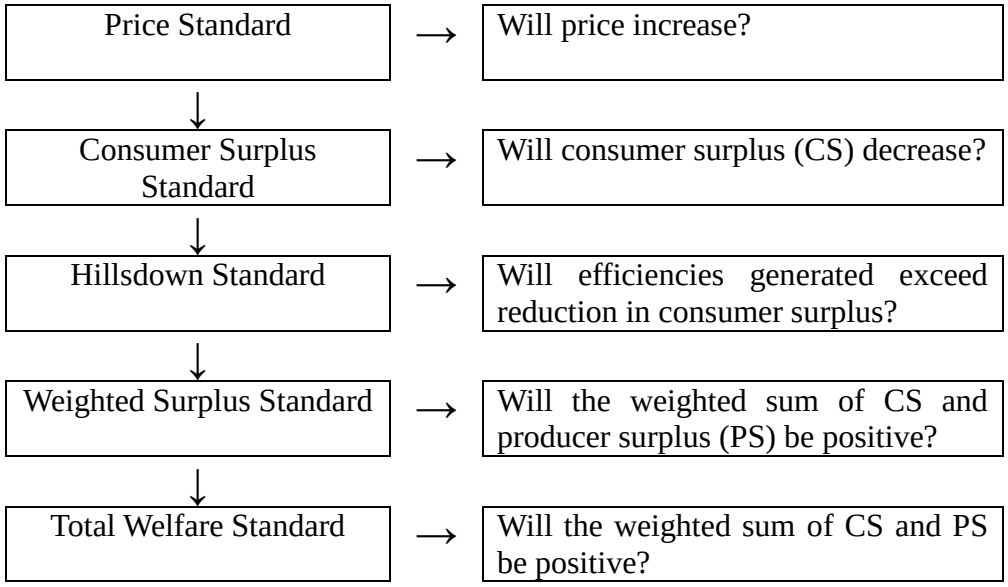
TFP = total factor productivity.
*Source*: Isaksson (2007).

Clearly, there is evidence that technological progress is a far more important source of growth in developed countries. Does this imply that, given the differences in economic structure and sources of growth for developed and developing countries, dynamic efficiencies may not be as significant in developing countries compared to developed countries? Would this mean the competition laws in developed and developing countries assign different weights to dynamic efficiencies? Surely this is controversial as developing countries also aspire to climb the technological ladder or reach the technology frontier. Furthermore, innovation activities such as R&D are more intense in the private sector in developed countries whereas most R&D activities are carried out in the public sector in developing countries. As noted earlier, the problem with dynamic efficiency is that innovation has a high degree of uncertainty.

Given the above discussions, how should policymakers proceed? Should they prioritize the different type of efficiencies? How are these efficiencies related to different notions of welfare? An interesting attempt at classifying the various approaches to efficiency and welfare considerations is discussed in OECD (2013), based on Renckens (2007). This is summarized in Figure 1 in which the standards used can be ranked based on the weight given to producer surplus. The price standard gives no weight to producer surplus and full emphasis is given on consumer surplus. In contrast, both consumer surplus and producer surplus is equally weighted in the total

welfare standard.

**Figure 1: Ranking Welfare Standards and Efficiencies for Merger Reviews**




*Source*: Adapted from OECD (2013) based on Renckens (2007).

Clearly, there is no consensus amongst legal scholars as to which standards are appropriate. Kaplow (2014) have argued for the consumer standard on the grounds that there are better policy instruments (such as taxes) that are more effective for redistribution (of surplus). Brodley (1987), on the other hand, has argued for a broader coverage, emphasizing the importance of dynamic efficiencies for total welfare. Ultimately, this issue could be decided in court based on the administrability criterion – which favours the consumer standard (Hovenkamp, 2013).

### (c) Free and Fair Competition

Competition is perhaps THE core concept in competition law. Within mainstream economic theory, competition is associated with maximizing society's well-being. Thus, the 'holy grail' within pure economic theory is the perfectly competitive market. Welfare maximization is assured by invoking the First Welfare Theorem, which states that the equilibrium of a perfectly competitive economy is Pareto optimal (Feldman, 1987). However, in reality, perfect competition is not a natural state – that is, markets do not have a natural tendency to become perfectly competitive in the absence of

government intervention. Even Adam Smith, whose allegory of the 'Invisible Hand' is often used to invoke the virtues of *laissez faire*, recognized the potential of collusion amongst sellers to the detriment of consumers. The early history of competition law in the United States was very much a reaction to the formation of 'trust' by dominant sellers to enhance their market power.

Given that competition or rivalry between firms is seen as desirable and as a means to achieve maximize welfare, what then is 'free and fair competition'? The term 'free' has a number of connotations. It could mean 'free entry and exit' from the market – a necessary but insufficient condition for perfectly competitive markets. For example, are there barriers – structural and behavioural – that prevent new firms from entering a market? Theoretically, incumbent firms could undertake strategic actions such as limit pricing or investment in excess production capacity to deter entry by potential rivals.

Another possible interpretation of free has to do with the absence of any restraints on buyers or sellers to undertake actions that allow them to compete with other firms more effectively. Vertical restraints are examples of such restraints – they restrict the freedom of downstream firms to undertake such actions. For example, in retail price maintenance, downstream retailers are not allowed to sell their products at prices below the price fixed by the wholesaler.

The term 'fair' is more complicated. Unlike the notions of welfare and efficiency, fairness is relatively new to mainstream economics. Even today, fairness is a topic discussed mainly in game theory and economic justice. There is very little discussion of fairness in industrial economics (the field which studies imperfectly competitive markets). One concept of fairness that has been developed in economics is based on the notion of envy-free. A fair distribution would be defined as one in which a party does not prefer (envy?) another party's allocation. If we were to apply this to the concept of competition, it would imply that a firm would deem the surplus it receives to be fair if it is not possible to obtain greater surplus given the resources (including capabilities) that it has and that of their competitors. This situation is similar to the definition of the Nash equilibrium. Extending the analysis on fairness further, if firms are heterogeneous in terms of capabilities (productivity and other firm-specific resources), each firm would consider any unequal outcome to be a fair one provided

the distribution of surplus is proportional to each firms' capability.

Another dimension of fairness is related to the welfare of others. Would firms reward other firms for their fair behaviour at their own expense? Here, firms are acting in a way not dictated by pure self-interest (as in collusion). Within this context, Rabin (1993) has shown that the (mutual-max or mutual-min) Nash equilibrium is a fairness equilibrium.[5] Discussing works by other scholars, Rabin pointed out that consumers may reject a monopolist's attempt at extracting all surplus if it is not too costly for them. Alternatively, consumers may be willing to pay more if a good is bought from a fair but high cost monopolist.

A more complicated case would be when products are differentiated. Do consumers consider the higher producer surplus arising from product differentiation to be fair? If the answer is in the affirmative, it would be consistent with the view with which product differentiation is considered in competition policy.

Finally, the term 'fair competition' is also often used in the context of competition between small and large firms. The concern here is related to a lack of a level playing field between small and large firms. There is no way to completely equalize the playing field between small and large firms given that the latter has numerous advantages – such as scale economies and easier access to financial markets – unless, of course, governments are willing to provide assistance or special treatment for small firms. Even so, the justification for doing this is unlikely to come from unfair competition between small and large firms.

**(d) Other Objectives**

Apart from the three key economic objectives discussed above, there are many other objectives. One objective that is present in competition law is the preservation of freedom and the dispersal of economic power (Stucke, 2013). These are 'democratic' or libertarian-related objectives. The **dispersion of economic power** is consistent with the striving for a perfectly competitive economy where freedom to choose and compete are assumed to be important conditions. Merger policies can take up this value via their

[5] According to Rabin (2009), mutual-max outcomes are those in which each person maximizes the other's material payoffs. Mutual-min is the converse. A complication in extending individual-based analysis to firm-level analysis is whether the latter is driven in the same manner as the former (which is likely to be true for the case of sole proprietorship).

monitoring and prevention of market concentration. '**Freedom**' can be regarded as a form of 'right' to participate in economic activities freely.

**Macroeconomic and development objectives** are complicated. They are often justified based on market failure arguments. The economy left on its own results in suboptimal outcomes from a social welfare perspective. Thus, there is a need for some form of intervention such as fiscal or monetary policies (unemployment, inflation), industrial policies (import substitution, export promotion, productivity growth), and rural development (poverty eradication**). Macroeconomic objectives** do not often feature in competition laws. When such objectives are incorporated in competition law, these are usually related to exemptions for business practices that may have an anti-competitive nature but contribute to the revitalization of the economy. Examples of these are the provisions for anti-recession cartels in the Japanese competition law prior to its revision in 1999 and 2000 (Tanaka, 2008).

**Industrial policies** are often seen as diametrically opposed to competition law. This is because competition law focuses on the protection of competition rather than the protection of competitors. This is true only if a narrow interpretation of industrial policy is adopted (that is, as involving protection of firms and industries). However, Evenett (2005) has argued otherwise – that competition policy can in fact complement industrial policies. The form of competition law may matter if it is to support industrial policies in developing countries (Singh, 2002).

**Economic integration** has also received attention as an important objective in competition law. Here, as in the case of industrial policy, there can be a conflict between promoting competition and regional economic integration (Jones and Sufrin, 2011). For example, the interpenetration of new markets may require marketing expenses that can only be recovered via retail price maintenance or territorial restrictions, which are considered anti-competitive practices (Jones and Sufrin, 2011).

National development and competitiveness objectives may also conflict with a regional integration objective (Lee and Fukunaga, 2013). For example, a country's intent on making its industry competitive internationally via domestic production (for example, to achieve scale economies) may restrict imports – a move that is against regional integration. Sectoral interdependence may also reduce the overall national competitiveness due to the protection of selected industries, which raises input costs

of other industries.

In summary, competition law often incorporates a number of objectives. There is a possibility that these multiple objectives are either conflicting or some degree of trade-off exists. Two dimensions are worth examining further – the intellectual framework underlying competition law (Sections 3 and 4) and the political economy (Section 5).

## 3. Theoretical and Empirical Foundations of Competition Law Objectives

> The economic models involved are essential to all antitrust analysis, but they are simple and require no previous acquaintance with economics to be comprehended (Bork, 1978, p.90).

Amongst the many branches of law, competition law is unique for its close link with economics. No doubt, the evolution of economic thinking, particularly in the field of industrial organization (also known as industrial economics) has influenced competition law. This came about mostly after the 1930s following the work by Edward Mason at Harvard and his PhD student Joe Bain in the 1950s (Lee, 2007). The empirical work, especially by Bain, provided a framework called the structure-conduct-performance (SCP) paradigm that has influenced competition law until today. Essentially, in the SCP paradigm, market structure determines how firms behave (pricing, output decisions, among others) which in turn affects performance (price and output levels, welfare, efficiency, price-cost margin, among others). Using industry level data, Bain conducted empirical work to test the relationship between market structure and performance. His view had a significant impact on the operationalization and enforcement of competition law, especially since the 1960s – for it suggested that anti-competitive behaviour could be tackled best by addressing market structure via merger controls. This emphasis on market structure can be labelled the Harvard School approach to competition law.

How has SCP influenced the objectives of competition law? One way to think

about this is to ask what does an emphasis on a structural approach mean for the objective of competition law. The answer could depend on the types of models underlying SCP – models which comprise three stylized cases – perfect competition, oligopoly, and monopoly. It is plausible that the relevant benchmark would be social welfare (the sum of consumer surplus and producer surplus).

The SCP paradigm continued to be dominant until the 1980s until the emergence of more game theoretic models of oligopoly competition. The so-called 'New Industrial Organization and its empirical counterpart, the 'New Empirical Industrial Organization' focused on strategic modelling of competition in markets. This new approach essentially shifted the emphasis from market structure (SCP) to firms' behaviour or conduct. Whilst the approach is not entirely Chicago School – it is possible that it provided the ammunition for a more rigorous justification for more permissible business conduct.[6] The impact on competition law objectives is less clear because this approach continues to rely on similar microeconomic foundations, albeit with greater emphasis on strategic market models. For example, both the Chicago School and Harvard School would be equally comfortable with the Cournot or Bertrand models of oligopoly. This could explain why scholars such as Hovenkamp (2013) have suggested that the differences between the Harvard School and the Chicago School approaches may not be as large as some have suggested. The differences may not be a technical one, but more ideological in nature as some have suggested. Both schools would subscribe to the same welfare objectives but may differ in whether the source of market power is benign (due to efficiency) or not (barriers to entry).

Within the mainstream literature, there are at least two 'minor revolutions' that have impacted industrial organization and possibly, competition law. The first is Coase's transactions cost theory and theory of the firm (and extended by Williamson and Hart).[7] These theories frame the firm as a vertically integrated entity that combines activities internally that could have been purchased externally (from markets). This is done to minimise transactions costs, which include search and contract costs as well as hold-up costs (which arise from relationship-specific

[6] The Chicago School emphasizes on the importance of efficiency as a goal of competition law.
[7] For detailed discussions, see Holmstrom and Tirole (1989).

investments). This theory does not affect the objective of competition law directly. However, it does affect the calculus of welfare and efficiencies related to vertical mergers (integration). These objectives are affected via effects on investment incentives and surplus generated.

The second mini revolution in IO is Baumol's theory of market contestability which argues that the behaviour of monopoly firms (or incumbent dominant firm) can be pressured by potential competition (entrant) in such a way that they behave like firms in a highly competitive market. The key assumptions underlying this theory are, however, highly restrictive, for example, 'hit and run firms' with very low sunk costs. As such, this theory is not likely to have strong effects on competition law objectives.

A potentially more influential contribution that may have had some influence on competition law comes from the Austrian School (the second generation). Whilst this school shares similar approaches with the Chicago School on the importance of free markets, the two schools differ in terms of how markets work. For the Austrian School, information in markets is decentralised with consumers and producers actively engaged in a discovery process that brings various transactions. Entrepreneurs play an important role in this discovery process, especially in new products and production processes via innovations. For this to happen, entrepreneurs need to be incentivised to undertake innovations via future super-normal profits. This Schumpeterian argument provides the basis for the positive relationship between market power and innovation. In addition to this, markets are theorized to undergo turmoil through a 'creative destructive process' where new innovations render old products obsolete.

Even though the ideas of the Austrian School are peripheral compared to mainstream theories, a number of these concepts are influential in competition law. These include entrepreneurship, free competition, and innovation. However, it is not clear whether these concepts have been framed in a way with the Austrian School's ideas. This issue is raised because many of the neoclassical models of competition do not address issues of entrepreneurship and if they do, perhaps not in the way it is conceptualised by the Austrian School. Another issue that looms in the background when discussing the above ideas of the Austrian School is the relevance of the theories of distributive justice to competition law objectives. We turn to this issue next.

## 4. Theories of Justice and Competition Law

> Fairness seems to be a dirty word today in American antitrust circles.
> (Horton, 2013)

For the most part, discussions on competition law objectives have skirted around theories of distributive justice. This is a reflection of the dominance of the consequentialist approach in economics. It is also due to the strong emphasis in economics on welfare and efficiency. The welfare theorems embody these considerations – only outcomes matter. To this can be added the utilitarian emphasis on individual and collective welfare – known as 'welfarist justice'. As these elements are implicitly embedded in the existing micro-foundations of competition policy, it might be more useful to discuss alternatives.

Aside from welfarist justice, other approaches to the theory of distributive justice have emerged (Sen, 2000). The libertarian theories of justice focus on the fulfilment of rights and liberties. Key aspects of the libertarian approach to justice include no trade-offs and egalitarianism. With regards to competition law objectives, it is useful to ask whether the freedom to compete freely and fairly is one such right. The same could be asked for the rights of consumers – are such rights different from human rights? Are such rights applicable for only certain types of (primary) goods? An important issue that may arise – should there be a link between such theories of justice and competition law objectives – would be whether such violation of rights and liberties are subject to *per se* (as opposed to rule of reason) standards. This is because of the no trade-off nature of rights and liberties.

The Rawlsian theory of justice emphasizes a fair social arrangement or structure based on the 'veil of ignorance' in which each person is assumed to not know his/her identity (position) in society (Rawls, 1971). One important element of Rawls's theory is the difference principle, which puts emphasis on the most disadvantaged group in society. If small and medium sized firms (SMEs) are construed to be the most disadvantaged enterprises in markets, might this be a justification for SME-related objectives in competition law? This question requires further investigation.

In Sen's capabilities approach, the emphasis is on the capabilities of individuals

that define a person's freedom to choose amongst alternatives (Sen, 2000). This, in turn, depends partly on the set of functionings accrued to an individual which Basu and Lopez-Calva (2011, p.154) define as 'what a person manages to do or to be'. Whether an individual with a given set of functionings is able to achieve the highest level of well-being depends on opportunities that are available as well as the individual's freedom. It is plausible that anti-competitive business practices can affect consumers' well-being via their impact on functionings and capabilities.

Finally, it is also useful to reflect on the relevance of procedural justice as opposed to consequentialist justice. Konow (2003), for example, highlights the differences between act utilitarianism (consequential) and rule utilitarianism (procedural). Should competition law contain objectives that relate to procedural justice? It is plausible that competition law could address this issue by focusing on procedural fairness during the enforcement process (Varney, 2009). This would greatly improve the governance of the decision-making processes by courts and competition agencies.

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