The Telegraph

A “big is bad” competition policy would be extremely damaging

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March 23, 2018

The UK public might be fed up of economic experts. But it would be disastrous if this meant abandoning a consumer-centric competition policy in favour of importing the “big is bad” narrative sweeping the US.

A “hipster antritrust” movement has gathered momentum in America, blaming high concentration levels in markets for everything from high prices to low wages, excess profits, inequality, and political rent-seeking. Markets with a small number of firms are regarded a “problem” that can only be solved by breaking them up, denying mergers or heavy regulation (for tech giants, as utilities). All this irrespective of evidence on profits, prices or anything else.

An anti-big-business impulse has been threatening to break out of certain elements of the conservative political and journalistic world here too for some time. This week, the centrist think-tank Social Market Foundation has taken a lead. It’s director James Kirkup began an article claiming “if you can name all the big players in a market, or even just count them, there’s something wrong with the market.” The answer, again, was more aggressive competition policy.

Yet a crude approach that says “big is bad” and “tougher competition policy is always better” is based on bad economics. In the 1960s, such a “structuralist” approach to looking at industries led to worse outcomes for consumers.

High market concentration can be a leading indicator of oligopolistic practices and damaging barriers to entry in certain industries. But it can arise too as the dynamic process of competition itself weeds out inefficient producers, with larger firms harnessing economies of scale to deliver low price, high-quality goods or services. Measures of market concentration, in isolation, tell us little. The consumer welfare school that replaced the structuralist approach recognized that the effect on customers required detailed, technocratic market analysis.

Tale supermarkets. The 4-firm concentration ratio in the UK sector was 72.3 percent in 2016. Yet supermarkets engage in cut-throat price competition and have expanded provision of products hugely over the last 50 years. In fact, when the concentration of supermarkets was much smaller and there were more independent, local stores, these operated a lot more like local monopolies in practice. As former Adam Smith Institute director Sam Bowman has explained,

prices would likely be higher and quality lower if a firm-counting concentration test had led to the break up of giants such as Tesco and Sainsbury.

The problem with Kirkup's opening line then is that it conflates maintaining a competitive environment with maintaining large numbers of competitors. Yet the two are not the same. In markets with low barriers to entry, the threat of entry itself can lead to efficient outcomes. If firms do not deliver low prices or high quality, there exist profitable entrepreneurial opportunities for others to do so. That's why across time, it's difficult to think of companies that dominate as monopolies for generations.

It is just wrong then to claim concentrated markets are prima facie evidence of bad consumer outcomes. But new antitrust policy movements want to overturn the "consumer welfare" approach to competition policy entirely, and often bring shapeshifting arguments for why change is needed when this evidence is highlighted.

Take Amazon, a firm that people regularly say is too big and needs breaking up. In other sectors excess profits are pointed to as a sign of excess market power, yet Amazon is barely profitable. So critics instead suggest the company engages in predatory pricing to capture market share to become a monopolist later. Yet we cannot predict the future with any certainty. And the reality is that Amazon's low profits arise a lot more because it has been using its cash to invest heavily into new products and services, including its new grocery store, Kindle, Echo and cloud computing – products which enhance consumer welfare. Point this out, and the critics seamlessly shift to discuss Amazon's supposed monopsonistic purchasing power damaging suppliers.

The current framework of judging markets according to the impact on consumers has a clear rationale and means of testing conclusions. But this kitchen sink throwing at Amazon just shows a prejudice against large firms. One cannot run a competition policy on such an arbitrary, all-encompassing basis.

Indeed, in other cases it is not entirely clear what the market is. Facebook provides lots of services for practically zero out-of-pocket costs to most customers, and is hugely popular due to its network effects. But there is no "social media market" as such given users sign up to multiple social media outlets at once. Though Facebook may dominate its sub-sector, the technical barriers to entry, except for the network building aspect, are pretty low. Facebook took over from Myspace, after all.

It's possible that new-age antitrusters are right that firms with high market power in certain sectors may be more likely to nobble politicians to insulate them from outside competition. But this is neither universally true, nor does it allow that the solution is the heavy-handed breaking up of companies. Small local grocery stores and retail businesses can be protectionist too – using the planning system to attempt to block developments by large chains. An arbitrary, unclear competition and associated regulatory policy is also far more likely to see companies attempt to use the courts and authorities to stymie competition. Heavy-handed action to break up businesses in lots of highly concentrated industry is surely not an efficient way of dealing with the more limited problem of rent seeking.

Despite popular wisdom then, big business and highly concentrated markets are not synonymous with bad consumer outcomes. The new competition policy hawks and antitrust enthusiasts seem to be using vague platitudes such as “we need to restore faith in capitalism” and “corporations are too powerful” to justify an agenda which is ill-thought-through and arbitrary, and which risks substantial economic damage.

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