

Special Project for the 2009 ICN Annual Conference

**SURVEY ON COMPETITION LAW IN SMALL ECONOMIES**

**Contribution by the Belgian Competition Authority (Directorate general)<sup>1</sup>**

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**2 The Notion of a “Small Economy”**

**2.1 Are the abovementioned criteria adequate in your view?**

The following criteria are in our opinion certainly relevant (in estimated order of significance when assessed from the perspective of an EU Member State):

- (i) Population in absolute terms, and the density of population rather than the population compared to the neighbouring economies;
- (ii) Degree of regional economic integration, including entry barriers, dependence on international trade, economic ties with neighbouring countries;
- (iii) Size of the economy in terms of GDP and GDP/capita;
- (iv) Comparative importance or size of the undertakings, or of the number of global players which have their seat in the territory of a small economy, etc.
- (v) Size of the territory, in which the economy “takes place” and its geographic location; and more specifically some key geographic characteristics (climate, access to sea and waterways, flat or mountains, dry or fertile or flooded)

Legal, cultural, social and historical differences compared to the neighbouring economies can certainly be significant market characteristics, but they seem less relevant to make a distinction between large and small economies.

*2.1.1 Very small and small to medium sized economies*

We also see the need to distinguish between very small and other small (or perhaps medium sized) economies because they present, especially in respect of merger control, differences that have a direct impact on the competition policy environment.

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<sup>1</sup> With special thanks to Christian Huveneers, vice president of the Competition Council, for his contribution. He contributed to this survey in his personal capacity.

In this survey, we will use the following definitions:

- very small economies: economies with a market of usually less than half a million and no more than 1 million inhabitants (i.e. economies that have roughly the size of a still rather provincial city) in particular if they have a high density of population;
- small to medium sized economies: economies with a market of less than 15 million inhabitants (i.e. economies that have roughly the size of a metropolis) in particular if they have a high density of population.

### 2.1.2 Member of a network or part of a larger jurisdiction?

*Prima facie* it also makes a significant difference whether a competition authority of a small economy is part of a larger network of competition authorities or not, and in particular whether or not a small economy is part of a larger jurisdiction of another competition authority that supervises a larger economy or group of economies. However, we suspect that this distinction will in practice be more relevant to small to medium sized economies than to very small economies.

Very small open economies are often likely to benefit as much from the antitrust enforcement by the authorities of larger economies as from their own antitrust enforcement. Most restrictive agreements and practices are likely either to be concerned with a larger geographic area than the domestic market of a very small open economy or to remain relatively ineffective because of cross border alternatives. Domestic antitrust enforcement will primarily have a complementary function. For very small economies, trans- or supranational antitrust enforcement can not be expected to complement significantly the enforcement on larger markets because cases that are specifically concerned with a very small economy will often be too small to be taken up by a trans- or supranational authority<sup>2</sup>.

Small to medium sized economies are more likely than very small open economies to be the specific target of significant anticompetitive agreements or practices that do not come within the jurisdiction of any other authority. They are also more likely to be object of interventions of trans- or supranational authorities.

Closed economies will almost by definition have to rely on their own antitrust enforcement.

## **2.2 How do you define your economy (“large” or “small”)? By which standards? How do you define the size of your neighbouring economies or major trading partners?**

In the light of our response to question 2.1 we consider that Belgium is a small to medium sized economy<sup>3</sup>:

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<sup>2</sup> An exception being e.g. the Luxembourg beer case decided by the European Commission (Commission decision of 5 December 2001, case COMP 37.800/F3. This case was, however, closely related to cases concerned with the Belgian, Dutch and French markets.

<sup>3</sup> Source: federal website Belgium.be.

## Belgian Competition Authority

### Directorate General

Population	10.584.534 inhabitants (2007)
Surface area	30.528 km <sup>2</sup>
GDP	314 billions of EUR (2006)

By the same standards we consider:

- the Dutch economy to be borderline large,
- the German economy to be large;
- the French economy to be large;
- the Luxembourg economy to be very small.

Economic analysis shows that these four economies and Belgium still present different characteristics that are relevant for the purpose of this survey, notwithstanding the degree of market integration in the European Union<sup>4</sup>.

The distinction between very small open economies (like Luxemburg), small open economies (like Belgium), borderline large economies (like The Netherlands) and large economies (like France and Germany), can be assessed analytically by relying on empirical research of pricing-behaviour:

- It appears that Belgian undertakings mostly have to align their prices on German prices, i.e. they are price-takers. It also appears that their profitability is significantly constrained by import competition because the size of the Belgian domestic market is small enough in order to allow foreign undertakings to cater for the entire domestic market at “cut-throat competition” prices<sup>5</sup>. Similar constraints apply with regard to the possibility for Belgian exporting undertakings wishing to roll over their unit cost increases into their selling prices, i.e. in the long run, their pricing seems to be constrained by the Law of One Price. In economic theory, these are precisely the distinctive features of a small open economy as compared with large (open) economies<sup>6</sup>.

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<sup>4</sup> See on the market integration between these economies, at a general level, e.g. A. Jacquemin and A. Sapir, “International Trade and Integration in the European Community: An Econometric Analysis”, reprinted from *European Economic Review*, 32, 1988, in A. Jacquemin and A. Sapir (eds.), “The European Internal Market – Trade and Competition”, Oxford University Press, 1991, pages 202 – 212.

<sup>5</sup> See for academic analysis of empirical data e.g. E. de Ghellinck, “Effets de l’ouverture sur les structures et performances d’une petite économie – Le cas de la Belgique”, Ciaco, Louvain-la-Neuve, 1986. D. Frantzen, “The Cyclical Behaviour of Manufacturing Prices in a Small Open Economy”, *The Journal of Industrial Economics*, Volume XXXIV, N° 4, June 1986. H. Pauwels and A. Van Poeck, “Export Pricing: The Case of Belgium”, *Tijdschrift voor Economie en Management*, Vol. XXVII, nr. 4, 1982, pages 417 – 433. Ch. Huveneers, “Rol van economische analyse in de toepassing van de Wet tot bescherming van de economische mededinging”, chapter VIII in J. Stuyck, W. Devroe, P. Wytinck (eds.), “De nieuwe Belgische Mededingingswet 2006”, Kluwer, 2007, pages 214-215 and references quoted in footnotes 46 to 51.

<sup>6</sup> See e.g. in the field of Macroeconomics: R. Dornbusch, “Open Economy Macro-Economics”, Harper International Edition, Basic Books, New York, 1980. In the field of Industrial Economics see : R. Caves, M. Porter, M. Spence with J. Scott, “Competition in the Open Economy – A Model Applied to Canada”, Harvard University Press, 1980; special issue on “L’économie industrielle internationale : une discipline en construction”, *Revue d’économie industrielle*, N° 55, first quarter, 1991.

- For the Dutch economy, the constraints of international competition on pricing and on mark ups are less severe than for the Belgian economy, and the markups are on average higher in Dutch manufacturing industries than in their Belgian counterparts<sup>7</sup>. This supports the view that the Dutch economy is “borderline large” whereas the Belgian economy is a small open economy.
- The specific characteristics of Luxemburg as a very small open economy are also illustrated by economic research<sup>8</sup>.
- In large (open) economies, undertakings are typically price-setters (as opposed to price-takers) and are able to roll over their unit cost increases onto their selling prices; in the long run, their pricing seems to be based upon some sort of “cost-plus” pricing<sup>9</sup>.

### **3 Anticompetitive Agreements**

**3.1 How, if at all, should such elements be taken into account? What is the importance of open borders in this context? Is there evidence for more oligopolies in small economies? If so, what type of competition policy is best suited to cope with the implications that oligopolies have on competition? Could the enhanced risk of collusion and anti-competitive conduct justify harsher sanctions or a different focus of the competition laws?**

The degree of ‘openness’ of markets is a key issue, especially in respect of small to medium sized economies.

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<sup>7</sup> See J. Konings, P. Cayseele and F. Warzynski, “The Dynamics of Industrial Markups in Two Small Open Economies: Does National Competition Policy Matter?”, *International Journal of Industrial Organization*, 2001, number 19, pages 841-859. J. Konings and P. Van Cayseele, “The Implementation of National Competition Law and the Dynamics of Price Cost Margins: Evidence from Belgium and the Netherlands, 1993-1999”, in J.-L. Gaffard and E. Salies, “Industrial Dynamics”, Edward Elgar, 2008, forthcoming.

<sup>8</sup> See e.g. G. Schuller, “De l’analyse des relations économiques extérieures”, *Cahiers d’économie*, Publications du Centre Universitaire Luxembourg, Fascicule IX, pages 15 – 24, et P. Pieretti et G. Reinesch, « La croissance d’une très petite économie ouverte est-elle « import-driven » », *Cahiers d’économie*, Publications du Centre Universitaire Luxembourg, Fascicules IX et X, Luxembourg, 1994.

<sup>9</sup> For the pricing-behaviour of German undertakings, see C. Morel and A. Steinherr, “An Empirical Study of World Market Influences on Price Formation in West Germany”, *Empirical Economics*, 1978, Vol. 3, Issue 3, pages 183-201

### 3.1.1 *Very small economies*

In a very small economy, all economic actors of any significance are likely to know each other. Especially in case the market is also relatively closed, the risk of collusion is almost endemic. There is at best a narrow margin between oligopolistic market behaviour and cut-throat competition.

In case of more open very small economies, the relevant geographic market will usually be larger than the domestic market of a very small economy. But there may nevertheless still be a higher risk of collusion between the domestic players and markets may often prove to be less open than the regulatory framework suggests.

### 3.1.2 *Relatively closed small to medium sized economies*

In case of relatively closed small to medium sized economies, the relevant geographic market is less likely to be larger than their domestic market than in very small economies. They may therefore be even more inward looking than very small economies. For broad ranges of products and services, the markets are moreover as likely to be oligopolistic as in very small closed economies and there may be a significant number of ‘natural quasi-monopolies’<sup>10</sup>. Closed small to medium sized economies are therefore probably quite similar to very small economies in respect to the answers to these questions.

### 3.1.3 *Open small to medium sized economies*

The answer to these questions is different in respect of more open small to medium sized economies. They have more in common with larger economies:

- As regards oligopolies, as we have indicated sub 2.2 that export opportunities and integration into a common market alleviate the constraint of a small or medium sized national market by creating room for more domestic undertakings and plants reaching “minimal technical efficient scale” (METS), leading to a less oligopolistic market structure without sacrificing technical efficiency. This supports the view that more open small to medium sized economies may not differ so much from larger economies in respect of oligopolies.
- As regards the risk of collusion, it can also be stated that open small to medium sized economies may not differ much from larger economies. First, the economic actors of any significance do not necessarily know each other as well as in very small economies. And import competition, export opportunities and multinational activity limit the scope for collusion between domestic actors in a small open economy<sup>11</sup>. High levels of *actual imports* dilute domestic (seller) concentration

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<sup>10</sup> See supra under 2.2. There is a negative relationship between the size of the domestic market and the level of concentration.

<sup>11</sup> W.J. Adams, “International differences in corporate profitability”, *Economica*, nr. 43, 1976, pages 367-379. R. Caves, “International Trade, International Investment and Imperfect Markets”, *Special Papers in International Economics*, N° 10, 1974. E. Pagoulatos and R. Sørensen, “Foreign Trade, concentration and profitability in Open economies”, *European Economic Review*, nr. 8, 1976, pages 255-267.

and reduce the ability of domestic undertakings to maintain prices above long-run average cost of production. Moreover, *potential import* competition through the threat of entry of new foreign competitors, may also constrain domestic producers and force them to adopt prices that are more closely approximating competitive levels. As regards *export opportunities*, the presence of export markets may render sellers less conscious of their mutual interdependence in the small domestic market. And as regards *multinational activity*, foreign direct investment into a small economy is likely to increase the degree of competition on the host country's market since the establishment of foreign subsidiaries in a small economy usually constitutes a large new entry.

However, open small to medium sized economies and larger economies also differ in respect of collusion with regard to the passing-on defence in the case of damages actions for breach of antitrust rules. Price taking is a distinctive feature of a small open economy. Undertakings in a small economy are not actually in a position to roll-over into their own selling prices the higher costs of their inputs caused by a cartel between their suppliers. Therefore, in the case of damages litigation, cartel members who sold the goods to a small open economy's firm are in a more difficult position to use a passing-on defence.

It further follows from the characteristics of open markets of price-takers, that competition policy should focus on industries and undertakings that nevertheless enjoy some power of price-setting due to product differentiation or sheltering from international competition<sup>12</sup>.

#### 3.1.4 *Open-market policies*

Given the fact that the degree of 'openness' of markets is a key issue and the difficulties of achieving a sufficient antitrust enforcement in very small and relatively closed small to medium sized economies, the emphasis of competition policy when defining priorities and remedies, as well as of market policies in general should in small economies be on the opening of markets for foreign competition, i.e. for foreign trade and direct investment. This issue is not only relevant in respect anticompetitive agreements, but also in respect of abuse of dominance and merger control. We refer in this respect to par. 6.1.

#### 3.1.5 *Conclusions*

- (i) Whether borders are open or not to international trade and foreign direct investment flows, or whether a smallish economy is a well integrated part of a larger economic area, is very relevant, especially in respect of small to

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<sup>12</sup> See for theoretical and empirical studies on the extent there can be price setting by undertakings in a small open economy like Belgium: E. de Ghellinck, P. Geroski and A. Jacquemin, "Inter-industry variations in the Effect of Trade on Industry Performance", *Journal of Industrial Economics*, 1988, volume 37, N° 1, pages 1-19. P. Geroski and A. Jacquemin (editors), "Symposium on Industrial Organization and International Competition", *Recherches Economiques de Louvain*, Volume 47, 1981, N° 3-4. A. Van Poeck, "Competitieve en beschermde sectoren in de Belgische economie", *Economisch en Sociaal Tijdschrift*, jaargang 1977, nr. 1, pages 101 – 112.

medium sized economies. The answers to questions 3.2, 4.1 and 5.1 will further illustrate the relevance of this issue.

- (ii) When exchanging experiences with NCAs of larger economies, we do not have the impression that there is a significantly higher risk of collusion and anti-competitive conduct in *open* small to medium sized economies. The types of cases dealt with by competition authorities are on the contrary very similar.
- (iii) There seems therefore to be no need for harsher sanctions in *open* small to medium sized economies.
- (iv) The focus of Competition Authorities in open small to medium sized economies should be on the industries and undertakings enjoying some power of price-setting due to product differentiation or sheltering from international competition.
- (v) There is a significantly higher risk of oligopolistic market structures, collusion and anti-competitive behaviour in very small economies, especially if they are moreover relatively closed. And the same conclusion applies to relatively *closed* small to medium sized economies.
- (vi) We do not know whether harsher sanctions are called for in very small and in relatively closed small to medium sized economies. Careful advocacy and systematic enforcement seem required. There is a real risk that the business communities in small economies will lack peer pressure, or may even generate a strong undercurrent of opposition to the idea that competition policy is in the public interest.
- (vii) Given the significant difference in level of difficulty to promote a proper functioning of markets between closed and more open small economies, the emphasis of competition policy and market policies in general should in closed small economies be on the opening of markets for foreign competition.
- (viii) There will also inevitably need to be more focus in small economies<sup>I</sup> on issues such as cooperative oligopolistic market behaviour.
- (vii) With regard to EU Member States we may add that national competition authorities in open small economies are bound to apply article 81 EC more frequently than national competition authorities in large economies. More agreements and practices are likely to “affect trade between Member States, or at least it will be less difficult to interpret the ability of agreements to appreciably affect trade between Member States” given the fact that anticompetitive agreements are more likely to cover the whole territory of an open small to medium sized economy than to cover the whole territory of an open large economy<sup>13</sup>.

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<sup>13</sup> According to paragraph 77 of the guidelines on the effect on trade concept contained in Articles 81 and 82 of the treaty (OJ 2004 C 101/07), horizontal cartels and other agreements covering the whole of a Member State territory are by their very nature capable of affecting trade between Member States.

**3.2 Vertical restraints are often linked to imports in small economies. Does this require or justify a different analysis of vertical restraints, especially of resale price maintenance and of parallel import bans, in small economies? Moreover, could the fact that the risk of foreclosure is higher justify a different analysis?**

*3.2.1 Open economies*

Distribution networks tend to protect their territory. Where the territory coincides with (or is larger than) the relevant geographic market, the impact of such vertical restraints on competition is limited. Their impact on cross border trade is also limited in the EU. The gradual realisation of the internal market and the search for synergies and economies of scale make that distribution networks in the EU are increasingly organised on a cross-border basis.

But there is in our opinion in economies that are open from a regulatory perspective, still an increased risk of market partitioning even when the relevant geographic markets<sup>14</sup> are larger than the domestic market of an economy (in the meaning of jurisdiction as used in this survey) in case distribution systems are organised by jurisdiction.

This risk is larger in small than in large economies in which the domestic market is more likely to coincide with the naturally relevant market. It may also be larger in small to medium sized economies than in very small economies in which it is more difficult to justify the organisation of a distinct distribution network.

*3.2.2 Closed economies*

The impact on competition and cross-border trade of vertical restraints in nationally organised distribution networks is obviously smaller in case the (small or small to medium) economy is closed anyway for other reasons.

*3.2.3 Conclusions*

- (i) Given the fact that the vertical restraints that are most likely to keep economies artificially closed qualify as hardcore restrictions in EU competition law, we do not see the need for a different analysis in the EU. But we do see the need for continued vigilance whenever distribution networks are organised on the scale of a domestic market of a very small or a small to medium sized economy, while the regulatory framework and economic characteristics of goods or services suggest that the relevant geographic market for goods or services is larger than national.
- (ii) There is no similar need for vigilance in case very small or small to medium sized economies are already closed for other reasons. Priority should be given to the main causes of market fragmentation.

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<sup>14</sup> In this context: relevant independently of the organisation of distribution.

#### **4 Abuse of Dominance**

##### **4.1 Does this mean that a specific regime should apply to the conduct of dominant undertakings in a small economy? Or does this make no difference? Is there a different approach towards collective dominance issues?**

We do not see the need for a specific regime or a different competition law approach.

But as already indicated in the answer to question 3.1, we do expect to see in most small and in particular in very small or relatively closed small to medium sized economies a different balance between cases concerning anticompetitive agreements and abuse of dominance cases. We expect that there will be more emphasis on issues such as single- and collective or oligopolistic dominance.

Given the significantly higher risk of oligopolistic market structures, collusion and anti-competitive behaviour in very small (especially if they are moreover relatively closed) and in relatively closed small to medium sized economies, it is bound to be more difficult to avoid the use of concepts such as collective dominance in order to achieve an adequate level of antitrust enforcement in these economies. The inherent uncertainties created by the use of this concept will in turn require appropriate guidance and advocacy.

In very small or relatively closed small to medium sized economies, there is also bound to be additional pressure for a more regulatory approach to market management given the risk of market failure. However, especially the very small economies are bound to find it difficult to organise market regulators as well as an effective competition authority. The competition authority is therefore likely to be asked to act also as the (price setting) market regulator for a number of goods or services. The OECD Competition Committee, among others, considers that this combination of tasks risks diluting the nature of antitrust enforcement<sup>15</sup>.

These problems can be alleviated when their competition authority is a member of a network of authorities or if small economies envisage even the organisation of cross-border authorities or clusters of authorities.

Regulatory pressures may also inspire an ambiguous attitude to state monopolies and state-owned enterprises in general:

- The presence of state monopolies or state-owned enterprises is unlikely to facilitate the opening of economies (regardless of their size).

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<sup>15</sup> See e.g. peer review questionnaires.

- But in case of natural monopolies state-owned enterprises may well be one of the both economically and socially more acceptable ways to provide the relevant goods or services with the required level of regulation.

Several of the concerns expressed in this response are related to the degree of openness of an economy. We refer to par. 6.1 and the need for remedies and market policies that aim at an opening of markets for foreign competition.

## 5 Mergers

**5.1 Are there any differences with respect to the substance of the merger control regime? Are there different justifications for having a merger control regime in small economies? Should there be different guidelines for geographic market definition? How might the size of the economy affect the application of legal presumptions? Which types of remedies are best suited for small economies?**

### *5.1.1 Open economies*

We do not see the need for a different approach to merger control in open very small or small to medium sized economies compared to larger economies.

On the contrary, open very small and small to medium sized economies should in our opinion take care not to look at markets as a larger economy would in order to avoid using artificially narrow definitions of relevant geographic markets. There is always a certain temptation to consider markets to be national. But given the fact that undertakings in open very small or small to medium sized economies are typically price-takers, it will often be possible to argue that the relevant geographic market extends beyond the national jurisdiction and that these undertakings do not enjoy the market power a purely national perspective may suggest<sup>16</sup>.

The need to avoid the temptation to consider relevant geographic markets to be national may impact on the use of concentration indices like the Herfindhal-Hirschman Index (HHI). If some industry or undertakings in open small or small economies nevertheless enjoy some degree of price-setting power due to product differentiation or to sheltering from international competition, it is theoretically possible that a SSNIP test might lead to the result that a non-transitory increase of the price would lead to an increase in profits. But in order to take into account potential competition and future market developments when assessing the impact of concentrations (and not of actual market behaviour), competition authorities in small

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<sup>16</sup> E.g. applying the SSNIP test would lead to the result that a non-transitory increase of the price above the level of the international price would lead to a sharp decline in the quantities sold and to a fall in profits.

economies should ideally compute these concentration indices at the level of a larger regional market (e.g. the whole European market). If the relevant regional figures are not available, they should correct the market shares for trade flows. An empirically robust correction consist in computing HHI based on domestic market shares, i.e. each firm's total turnover less each firm's exports. This variable has been shown – both theoretically and empirically – to interact with import competition in determining profitability (price-cost margins, markups) in Belgian industries<sup>17</sup>.

### 5.1.2 *Closed economies*

The answer to this question can be different in respect of more closed very small or small to medium sized economies. The competition authority should in our opinion in the first place assess the impact of a transaction on the degree of opening (or lack thereof) of their economy.

Authorizing transactions with appropriate remedies that help to open up markets may prove to be more pro-competitive than prohibiting envisaged concentrations even if they result *prima facie* in an even more oligopolistic market structure. To open up markets means to open up the domestic market to imports as a competitive constraint, as well as making domestic undertakings more likely to export. By enlarging the relevant geographic market, it may be possible to accept a higher degree of concentration among domestic undertakings.

### 5.1.3 *But do small economies need merger control?*

A more fundamental question is whether small economies need merger control, i.e. whether merger control can deliver added value to small economies.

We start from the assumption that anti-trust enforcement in respect of cartels and abuse of dominance makes a more valuable contribution to sustainable development than merger control.

If that assumption is correct, no competition rules should provide for merger control unless it has been ascertained that the competition authority will also have sufficient means for an efficient enforcement of antitrust rules.

As we have seen above, the value added of merger control in small open economies seems to be low for price-taking industries. If some industry or undertakings in open very small or small to medium sized economies enjoy some degree of price-setting due to product differentiation or to sheltering from international competition, merger control may still make sense but will make a less valuable contribution than anti-trust enforcement.

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<sup>17</sup> See A. Jacquemin, E. de Ghellinck and Ch. Huveneers, “Concentration and Profitability in a Small Open Economy”, in R. Caves (editor), “Symposium on International Trade and Industrial Organization”, The Journal of Industrial Economics, Volume XXIX, December 1980, N° 2, pages 131 – 144. An additional possible correction lies in the inclusion of imports of similar goods into the computation of apparent domestic consumption (A. Jacquemin, E. de Ghellinck and Ch. Huveneers, “Concentration industrielle en économie ouverte”, Bulletin de l’Institut National de Statistique, Brussels, April, 1978, formulae shown on page 400.

**5.2 On the level of the procedural regime, what are the appropriate criteria triggering an intervention or an inquiry into a merger project: turnover thresholds; structural criteria, such as the degree of organisational integration (existence of branches or subsidiaries) of one or both of the merging companies; effect on competition? Should there be a mandatory or a voluntary notification regime, with or without a prohibition to proceed without clearance?**

Merger control should be designed in a way that it is likely to catch transactions that risk to have a substantially negative impact on competition on the domestic market, without catching more transactions than necessary in order to achieve that goal.

*5.2.1 Very small economies*

Very small economies present in this respect several specific characteristics that are relevant when defining thresholds and notification requirements:

- (i) Turnover thresholds that are sufficiently low to catch mergers that may have a significant impact on the domestic market of a very small economy, will result in case of mandatory notifications in the obligation to notify in that jurisdiction an unreasonably high percentage of regional or global transactions, even in case the merger control rules include an adequate “local nexus” requirement. And if their turnover thresholds are in line with international practice, merger control rules will produce little added value in a very small economy.
- (ii) In small communities it is unlikely that potentially affected customer groups or competitors, if not regulators, will be unaware of locally significant transactions.
- (iii) The smaller the economy, the more the economy needs to be seen as a constructive part of a larger market in order to attract foreign investment. Low turnover thresholds that allow to catch mergers that may have a significant impact on the domestic market of a very small economy, also risk damaging the reputation of their jurisdiction by inflicting transaction costs that are disproportional to the relative significance of their market.
- (iv) Except in isolated markets, it is unlikely that major transactions that affect the domestic market of a very small economy will not be caught by the merger control rules of one or more ‘larger’ economies. This holds in particular true in the case of small economies that are part of a larger entity with its own merger control regime such as the European Union or the European Economic Area. And it is also unlikely that a transaction that has been prohibited by neighbouring jurisdictions, will only take place in respect of a very small economy of a jurisdiction that has no merger controls.
- (v) It is equally unlikely that a small economy jurisdiction will be able to block effectively a transaction that, from the point of view of the parties, is only marginally concerned with the market of that small economy.

– *Thresholds*

It follows from the abovementioned specificities that the wish to ‘catch’ mergers that may have a significant impact on local markets is difficult to reconcile with the use of turnover thresholds or similarly objective criteria for a mandatory notification in the meaning of the 2004 ICN Recommended Practices for Merger Notification Procedures (the ICN Merger notification recommended practices).

Market share thresholds make it possible to catch only the transactions that are really relevant on the domestic market of small economies. But market share thresholds in mandatory notification procedures are, for good reasons, not in accordance with the ICN Merger notification recommended practices<sup>18</sup>. Belgium switched in 1999 from market share to turnover thresholds. It was our experience that when market share thresholds are combined with mandatory notification, the pre-notification research may well take up to 40% of the total time spent on the case. Rules that make knowing whether a transaction should be notified almost as expensive as notifying, are neither serving the public nor the private interests.

– *A voluntary notification system*

The disadvantage of a voluntary system is that authorities risk finding out too late that a significant transaction has happened. But as indicated in the second of the above mentioned specificities, it is unlikely that a significant transition would take place in a very small economy without anybody knowing.

It is therefore our impression that a very small country can easily live with the combination of voluntary notifications and market share thresholds.

5.2.2 *Small to medium sized economies*

Small to medium sized economies do not have the same specificities as the very small economies that have led to the conclusions in the previous paragraph:

- (i) Small to medium sized economies can more easily comply with the ICN best practices when combining a mandatory merger notification regime with turnover thresholds, as is demonstrated e.g. by a number of EU member states<sup>19</sup>.

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<sup>18</sup> In particular rule II.B.

<sup>19</sup> In the Belgian Competition Law, e.g., there was not only a switch from market share to turnover thresholds, but also, the choice of domestic turnover (instead of total turnover, thus including exports). This is very fortunate, in view of the arguments developed under par. 2.2 and 3.1.2.

Using total, worldwide, turnover as thresholds instead of domestic turnover would result in the obligation to notify in the jurisdiction of a small open economy like Belgium an excessively high percentage of transactions in respect of export oriented industries and economies. This was made clear by a recently published study (J. De Loecker, J. Konings and P. Van Cayseele, “Merger Review: How much of Industry is affected in an International Perspective?”, *Journal of Industry, Competition and Trade*, volume 8, 2007, pages 1 – 19): working with worldwide sales instead of domestic sales biases upward the estimate of the number of cases that would need to be cleared by merger control, and this upward bias seems to be stronger for a small open, heavy exporting economy like Belgium, than for an open large economy like France (P. Van Cayseele, “Indicators of Economic Competititon and Priorities in Competition Policy Enforcement”, *Algemene Rekenkamer, The Hague*, 22 November 2007 and *Lunchforum, FPS Economy and Tijdschrift voor Belgische Mededinging/Revue de la Concurrence Belge*, Brussels, 15 May 2008).

- (ii) It is in small to medium sized economies less likely that potentially affected customer groups or competitors will be aware of locally significant transactions.
- (iii) It is more likely that significant transactions will nevertheless not have a sufficient impact on neighbouring markets in order to be caught by the merger control rules of other jurisdictions.

### 5.2.3 Conclusions

- (i) The logical conclusion is that very small economies are, subject to what was stated in par. 5.1.3, probably better served by market share thresholds, and that they will therefore have to opt for a voluntary notification system in order to be in line with ICN recommended practices.
- (ii) We see on the other hand, always subject to what was stated in par. 5.1.3, no need to provide for a specific approach in small to medium sized economies in respect of thresholds and notification requirements in merger control rules.

## 6 Some general conclusions

### 6.1 Remedies and the importance of open market policies

Policies promoting international trade and foreign direct investment flows are the best way to promote competition in small economies. Open trade exerts a constant competitive constraint on the behaviour of domestic undertakings<sup>20</sup> that will always be more effective than the interventions of competition authorities that can only address a limited number of specific cases.

The importance of trade flows made possible by integration into a larger market can be illustrated by the EU experience. We start from the observation that undertakings or plants must achieve a “minimal technical efficient scale” (METS) in order to lower unit costs and to be competitive. Therefore, the smaller the size of the national market, the less room there is for undertakings or plants reaching METS, and the higher the degree of concentration. It follows that markets in small to medium sized economies are likely to be oligopolistic for broad ranges of products and services and

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<sup>20</sup> For a traditional theoretical view on this, see e.g. R. Caves, “International Trade and Industrial Organization: Problems, solved and unsolved”, Paper prepared for European Association for Research on Industrial Economics, Bergen, August 1983. For an empirical application to Belgium, see E. de Ghellinck, op. cit., 1986, and Ch. Huveneers and Ph. Van Cauwenberge, “International Trade Factors and Profitability of Belgian Industrial Sectors”, *Tijdschrift voor Economie and Management*, volume XXIII, nr. 3, 1978, pages 279 – 299). A free trade policy should however be seen as a complement of competition policy rather than as a substitute of competition policy (see e.g. P. Van Cayseele, “De Belgische wet op de mededinging – Concentraties in een industrieel economisch en internationaal juridisch perspectief”, Maklu, Antwerpen-Apeldoorn, 1994, pages 111 – 113.

that there may be a significant number of “quasi natural monopolies”<sup>21</sup>. Export opportunities increase the possibilities for domestic undertakings and plants for reaching METS. And (potential) import pressure alleviates the risks of an oligopolistic market structure without sacrificing technical efficiency. The opening of markets or the integration of small economies thus avoid or alleviate the conflict between efficiency and competition:

- export-orientation allows the actual size of the plants to be closer to the theoretical METS<sup>22</sup>;
- export orientation is tantamount to an increase in the size of the market and thereby allows – all other things being equal - for a lower degree of concentration as measured by HHI and simultaneously for actual plant sizes being close to the METS<sup>23</sup>. This explains why on the territory of a small open economy like Belgium, several large plants and undertakings can survive even in industries requiring a large METS (like steel, flat glass, non-ferrous metals).

## 6.2 More generally

1. The smaller the economy, the more difficult it is to ensure that a competition authority is sufficiently equipped to achieve an adequate enforcement of the rules of competition. Starting from the assumption that antitrust enforcement makes a more substantial and direct (or less indirect) contribution to social and consumer welfare than merger control, we suggest that competition rules should only provide for merger control if it has been ascertained that the competition authority will also have sufficient means for an efficient enforcement of antitrust rules (restrictive agreements and practices and abuse of dominance).
2. Except for the comment sub (1), we see no significant differences in the competition law & policy environments of larger economies and open small to medium sized economies.
3. We submit that in very small economies and in relatively closed small to medium sized economies, competition is served best by measures that aim at a better integration of these economies in their economic region. In a small economy where all actors and government know each other and are bound to interact socially as well as professionally antitrust enforcement is not only more necessary but also more difficult.

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<sup>21</sup> See also sub 3.1.2. For an analytical underpinning of this proposition, see especially F. Scherer, A. Beckenstein, E. Kaufer, R. Murphy and F. Bougeon-Maassen, “The economics of Multi-Plant Operation: an International Comparison Study”, Cambridge, Massachusetts, 1975.

<sup>22</sup> F. Scherer and al., op. cit., 1975 for the cases of 12 industries in USA, UK, Canada, Sweden, France and Germany

<sup>23</sup> A. Jacquemin, E. de Ghellinck and Ch. Huveneers, “Concentration industrielle en économie ouverte”, Bulletin de l’Institut National de Statistique, op. cit., 1978, pages 410 and 411. Market integration does not only benefit undertakings or plants in small economies. Trade growth and its causes such as the integration into the European common market, has possibly had the effect of doubling the plant size in 12 German manufacturing industries (J. Müller and N. Owen, “The Effect of Trade on Plant Size”, in A. Jacquemin and A. Sapir (eds.), op. cit., 1991, pages 173-184).

4. Given the highly oligopolistic market structure that is likely to characterise significant markets in relatively closed small economies, there is also likely to be an above average pressure for a more regulatory approach to market management. But a regulatory approach to market management is at least as difficult to manage in small and closed economies as competition law enforcement. Especially price regulation is unlikely to force in the longer run the less competitive suppliers to improve their efficiency.

Pressure from competitors on larger markets is likely to offer a more important stimulus to competition than antitrust enforcement can ever hope to offer.

5. Competition authorities in small economies (small to medium sized as well as very small) benefit also more than authorities in large economies from the contributions of networks and larger authorities. It is therefore important for small economies to make their competition authorities an active (if perhaps primarily receptive) member of such networks, or to envisage even the organisation of cross-border authorities or clusters of authorities.

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