

**The Notion of a "Small Economy"**

For the purpose of this Survey, an "economy" in the context of competition law refers to a distinct legal jurisdiction, defined by borders and governed by legal institutions empowered to enact and enforce a competition law regime.

The "smallness" of such an economy depends on the framework in which we operate the comparison. Possible criteria to be used include, inter alia, the following:

- Size of the economy, in terms of GDP;
- Size of the territory, in which the economy "takes place" and its geographic location;
- Population in absolute terms, or population compared to the neighbouring economies;
- 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.
- Degree of regional economic integration, including entry barriers, dependence on international trade, economic ties with neighbouring countries.

Analysis of the above abstract criteria brings us the following questions, most notably:

**Q1. Are the above criteria adequate in your view?**

1. In principle a relatively small GDP would seem to be the defining characteristic of a small economy. However, from the perspective of competition policy design it seems equally relevant to appreciate the underlying factors which cause an economy to be small. If the drivers of smallness are different, so the implications for competition law might differ. For example, the lessons for competition law in small developed economies (i.e. countries with a small absolute GDP but a high GDP per capita) might not apply to developing economies with large domestic populations. Similarly, it might also be the case that a small country endowed with significant natural resources, such as large oil reserves, will face different choices to other "small" economies that have limited natural resources. The discussion as set out in this response is limited to Singapore's experience as a small, open, developed economy.

2. CCS is aware that there has been extensive debate on the precise characteristics of a "small" economy. Simon Kuznets in "Economic Growth of Small Nations"<sup>1</sup> used an upper limit of 10 million people to define smallness. Other indicators such as a country's geographic area<sup>2</sup> and concentration level<sup>3</sup>

<sup>1</sup> Kuznets, Simon "Economic Growth of Small Nations" in E.A.G. Robinson, ed. 1960. Economic Consequences of the Size of Nations.

<sup>2</sup> Marcy, G (1963) "How Far Can Foreign Trade and Customs Agreements Confer Upon Small Nations the Advantages of Large Nations," EAG.

<sup>3</sup> Gal, MS (2001) "Size Does Matter: the Effects of Market Size on Optimal Competition Policy" University of Southern California Law Review 74: 1437-1478.

have also been used. All appear reasonable and what these definitions seem to have in common is that in each case there is an inherent constraint on domestic demand. If domestic demand is constrained then so are the size of domestic markets and the opportunities for the firms that serve them.

3. It also seems sensible not to confuse the driver of smallness, be it a measure of population or other resource constraint, with some of the responses designed to overcome that smallness. Some of the factors suggested in the background paper, for example the degree of international integration, dependence on international trade or the number of global companies based in a country, would seem to fall into this latter category.

4. Whatever definition is used it is expected that Singapore, as a city state of 4.84 million people, would be included in a list of small economies. Singapore's geographic size, small population and limited natural resource all provide a natural constraint on the domestic economy. Overcoming these difficulties has guided not just competition policy considerations but has also influenced economic policy over many years.

**Q2. 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?**

5. By any standard Singapore is likely to be regarded as a small economy, it accounted for just 0.3% of the global economy in 2007 and 1.5% of East Asian GDP. The size of the Singapore population, its small geographic size and the absence of natural resources are all factors which contribute to Singapore being a small economy. Given these features the economy will always be dependent on external demand.<sup>4</sup> This is consistent with the approach taken by the Singapore government, which has tailored economic policy over many years to reflect all of these issues.<sup>5</sup> Singapore has embarked on several phases of development since independence. In doing so Singapore has evolved from a labour-intensive, low-technology production base in the 1960s to the capital-intensive, high-technology, knowledge-and-skill based economy of today. Amongst other things these changes in development strategies were designed to overcome constraints on the domestic economy, changes in regional trade and the evolution of the global economy.

6. Table A (Annex A) shows the size of Singapore's GDP, population and trade-to-GDP ratio as compared to our neighbouring economies.

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<sup>4</sup> Khee Giap, Tan and Kang, Chen "Enhancing Singapore's Competitiveness: Some Fundamental Rethinking" a paper prepared for the Asian Economic Panel meeting jointly convened by the Hong Kong Institute of Economic and Business Studies, University of Hong Kong, the Earth Institute at Columbia University, the Global Security Center, Keio University, and the Korean Institute for International Economic Policy, 12-13 April 2004, Hong Kong.

<sup>5</sup> For example see the 1986 report of the Economic Committee, The Singapore Economy: New Directions

**Analytical Framework**

**The application of competition law in a small economy brings into play the notion of the State (“law”) and the notion of a social fact (“economy”). While the economy is given and constitutes a fact of life, the State which has the power to adopt the legal system governing the functioning of its economy, is created by law and defined by boundaries which may not coincide with the “size” of the economy. The “effects doctrine” translates the mutual international understating that each State has the right to organize its market, and to protect it, if it chooses to do so, against anticompetitive behaviour that affects it, independently of the place where this behaviour originates, and independently of the fact that a small economy may more often be exposed to anticompetitive behaviour which originates in another State.**

**Q3. Does the size of the economy affect the application of competition law, and if so how?**

7. In a small economy, the growth of domestic firms is likely to be constrained by the size of the local market or a lack of resources. This will clearly have implications on the competitiveness of the domestic economy. In particular, some domestic firms will either not achieve a minimum efficient scale or these industries will be unable to sustain a large number of firms. It has been suggested that small economies face higher levels of market concentration than their larger counterparts.<sup>6</sup>

8. In addition, other factors that are often associated with small economies, including a constrained labour supply, limited access to natural resources or high land prices could act as entry barriers further impeding the development of competition.

*The role of foreign trade*

9. The obvious way to minimise such constraints is by opening up the domestic economy to trade. Through an open trade policy firms can thus look to export markets to achieve economies of scale. Competition from overseas products and firms, along with new foreign investment, can diminish the domestic market power of incumbent firms. Similarly, access to both imports and export markets has the potential to significantly reduce barriers to entry for new or aspiring firms. This is a model that Singapore has adopted.

10. The extent of Singapore’s global orientation can be demonstrated by comparing the trade to GDP ratio with other economies both in the region and worldwide (see table A appendix A). Singapore’s domestic producers are more

<sup>6</sup> See discussion in Evens and Hughes, Competition Policy in Small Distant Open Economies Some Lessons from the Economics Literature, New Zealand Treasury Working Paper, December 2003, Page 5

dependent on foreign markets than most economies in the world. This can be seen by considering Singapore's tradable sector, where 93% of final demand (excluding intermediates) derives from external sources.<sup>7</sup> Unsurprisingly this global focus is reflected in trade policy. Roughly 96% of imports enter Singapore duty-free; exports typically have the same privileges. Complementing the free trade policy, the government has also actively promoted Singapore as an attractive location for foreign capital.

11. The extent to which an open trade policy can enhance the degree of domestic competition or access to export markets can provide economies of scale will ultimately depend on the nature of the individual product. Where markets are naturally bounded by geography, for example due to high transport costs, any problems arising from the small size of the domestic market will remain. However, with technological advances and improved communications, more and more markets have become global in nature. A number of CCS enquiries have concluded with positive clearances due to the international dimension of the markets involved. It is clear that the Singapore economy is more competitive than it would otherwise be as a result of its openness.

12. If foreign trade can alleviate many of the competition constraints that can arise in small economies, competition policy must complement and support policies that open the economy to trade and foreign competition. CCS is conscious that our regime should not unduly increase the cost of doing business in Singapore or add to business uncertainty. A transparent legal regime supported by reasoned decisions published on the CCS website can help to boost confidence in the objectivity and soundness of CCS' decisions.

#### *A focus on economic efficiency*

13. CCS supports the view that in small economies the principal focus of competition law should be economic efficiency. In this regard the objective of competition law in Singapore is "to promote the efficient functioning of our markets and hence the competitiveness of our economy."<sup>8</sup> Effective enforcement of competition law ensures that firms remain lean, sharp and able to compete internationally, while ensuring the benefits of global competition flow to consumers.

14. CCS adopts a case by case approach in appraising the economic effects of particular activities. The approach is designed to provide certainty to businesses where possible, while not prohibiting activities that can be justified on economic efficiency grounds. For example, transparent enforcement is supported by clear guidelines and supported by flexible schemes that allow parties to notify particular activities to CCS for approval.

#### *Resource commitments*

<sup>7</sup> Economic Survey of Singapore Second Quarter 2008

<sup>8</sup> Second Reading speech for the Competition Bill by then Senior Minister of State for Trade and Industry, Dr. Vivian Balakrishnan.

15. In enforcing competition law, small economies may need to invest comparatively more resources than in larger economies. For example, the CCS budget as a ratio of Singapore GDP is 3 times greater than that of the JFTC budget relative to Japanese GDP, and 2.5 times the ratio of the OFT budget relative to UK GDP. If the cost of the agency is calculated on a per tax payer basis the higher relative cost of operating an effective competition agency in a small economy is equally clear. If there is a practical lesson that can be learnt from this it is that to run an effective agency in a small economy requires political will and an ongoing commitment from the government.

### *Anticompetitive Agreements*

**Anticompetitive agreements are the best analysed and least controversial part of competition law. There will probably be fewer differences in the application of competition law in this respect. But the fact that people and operators know more about each other in smaller economies than in larger ones may make a difference. To this end the role on information, information sharing and networking mechanism may play a significant role in facilitating collusion. The limitation of the relevant market by state borders may make another difference.**

**Q4. 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?**

16. Section 34 of the Act covers anti-competitive agreements. CCS interpretation of these provisions is consistent with the approach followed in Europe, the US and other jurisdictions. Like most competition regimes CCS regards certain types of agreements, such as those between competitors that fix price, limit output, share markets or rig bids as, by their very nature, restrictive of competition to an appreciable extent. Such hardcore restraints are rarely efficiency enhancing and are likely to impose a significant negative risk to the economy.

17. CCS is not aware of any research to verify the suggestion that competitors in small economies know each other better or that there is more collusion in smaller economies. If it is verifiable that smaller economies are more concentrated, it would seem reasonable to suggest that with less people to organise, a cartel could prove easier to sustain. However, care needs to be taken to not make bold assumptions about the degree of interaction in small economies. Competitors have opportunities to mix through formal and informal networks in small and large economies alike. Experience would suggest that the nature of the industry is likely to be a better indicator for the likelihood of collusion than whether the firms are located within a small economy.

18. The risk of collusion among domestic firms arising from a relatively small concentrated population should also be reduced (at least in some markets) by

open borders and low barriers to entry. Even if domestic firms are able to organise collusive contact more easily in a small economy, foreign trade should reduce barriers to entry, introduce new competitors and help to undermine such co-operation. It is notable that most of CCS' section 34 enquiries have involved local geographic markets, typically service industries or non tradable goods. CCS has considered the role of trade associations in facilitating inappropriate contact between members on several occasions, a feature of the Singapore economy that might reflect its small size and close ties. On the other hand, CCS has also been able to use these established networks to channel a pro-competition message, to encourage compliance through education and to enhance the understanding by local businesses of the prohibitions within the Act. Competition law is still relatively new in Singapore (the Competition Act 2004 was passed on 19 October 2004, and became effective 1 January 2006) and as a young agency much of our work involves advocacy and promoting a culture of competition.

19. It is possible that agreements between competitors could give rise to efficiency claims in small economies, for example, as a way of achieving economies of scale. In this context, the Competition Act allows parties to apply for guidance or a decision if they consider that an agreement could be in risk of breaching section 34. This provision, which is not mandatory, could help to reduce the risk that firms will be deterred from undertaking an efficient activity by offering an opportunity to seek the views of CCS as to whether a (likely) anti-competitive agreement would bring a net economic benefit.

**Q5. 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?**

20. Being a small economy does not necessarily imply the need for a stricter enforcement of vertical agreements, even if these are related to imports. Unlike in the EU (but consistent with the approach of the UK prior to May 2005 when the Competition Act 1998 was amended to bring it in line with the EC Modernisation Regulation) the Third schedule of the Act excludes vertical agreements from Section 34. This reflects the position that that such agreements are in most circumstances unlikely to raise serious competition concerns, while they are often efficiency enhancing. Vertical agreements are only likely to prevent, restrict or distort competition in the presence of certain horizontal factors, typically where inter-brand competition is already weak. Given that the root cause of the problem in such circumstances is market power such actions are dealt with under the abuse of dominance provision. In some circumstances vertical restraints imposed by a manufacturer in response to pressure from competing customers, can facilitate collusion amongst horizontal competitors. This can be pursued as a horizontal cartel.

**Abuse of Dominance**

**It is likely that the number of large firms and their respective weight affect small economies more than large economies. State monopolies might also be more common in small economies than in large ones. Economies of scale may call for these sizes and at the same time limit the number of viable companies within the territory of such a small economy.**

**Since small economies may not be able to accommodate too many competitors in each industry, more emphasis might be put on efficiency considerations.**

**Q6. 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?**

21. CCS would agree that competition law in small economies needs to be careful with regard to economic efficiency considerations. In Singapore this efficiency focus is reflected not only in the legislation but reaffirmed through CCS' guidelines, which explain how CCS will interpret and give effect to the Act. The small nature of the economy may suggest a higher degree of concentration, but this does not necessarily imply that competition will not be effective, nor does it preclude taking a strong stand against exclusionary conduct by dominant firms.

22. Even in the presence of foreign trade, some non-tradable sectors, or other markets that are for some reason geographically contained, will continue to face difficulties arising from limited domestic demand. In particular, scale considerations mean that the degree of concentration is likely to be greater than in larger countries. For this reason in Singapore most of the market share thresholds (below which CCS is of the view that competition concern are unlikely to arise) are slightly higher than those found in larger economies, such as Europe or the US. For example, the EU uses a combined market share of below 25% to indicate that a merger is unlikely to be a concern. CCS has indicated that competition concerns are unlikely to arise unless the combined market share of the merging entities exceed 40% or, in cases where the combined market share of the merging entities is between 20% and 40%, the post merger CR3 is 70% or more. Similarly, in considering if a firm is likely to be dominant, CCS will as a starting point consider a market share exceeding 60% as likely to indicate dominance in the relevant market, rather than 40% in the EU. The higher figure of 60% takes into account the fact that some degree of market concentration is inevitable in small economies.

23. As with anti-competitive agreements and mergers that substantially lessen competition, CCS' substantive analysis in abuse of dominance cases does not adopt any prescriptive rules stemming from Singapore's small size, but considers the facts of each case on a case-by-case basis. CCS will thus apply rigorous economic analysis, in determining the (likely) effects of a particular conduct by a dominant undertaking. As in the EU the Competition Act has explicit provisions

that allow for efficiency considerations when considering anti-competitive agreements and mergers. CCS also considers that there is ample discretion in the abuse of dominance framework for it to account for efficiency considerations as part of an investigation.

24. Competition is a key tenet of Singapore's economic strategy. Wherever appropriate, Singapore has opened up sectors of the economy to market competition. Sectors such as telecommunications and energy generation, which used to be run by vertically integrated state-owned monopolies, have now been privatized, and subjected to competition. Outside of a few natural monopoly-type sectors, which are subject to their own regulatory regimes, state monopolies do not make up a significant proportion of the economy.

### Mergers

**Q7. 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?**

25. As Singapore is a small economy, some market concentration seems unavoidable. As noted above the merger thresholds have been adjusted to reflect this. Thresholds aside, the merger regime reflects standard international best practice and aims to prevent only mergers that substantially lessen competition and that do not have offsetting efficiencies.

26. Like most jurisdictions, there are provisions in the Act that allow CCS to consider arguments that a loss of rivalry might be outweighed by corresponding efficiency gains. For example, if a party can establish that a merger is likely to result in significant efficiency gains, such as cost savings, this can be sufficient for CCS to clear a merger, provided they offset the effect of any substantial lessening of competition. We will however require the parties to demonstrate that the claimed efficiencies arising from the mergers are clear, quantifiable, merger specific and likely to materialize within a reasonable timeframe.<sup>9</sup> Similarly, section 34, which prohibits anti-competitive agreements, excludes agreements that give rise to a net economic benefit. A party needs to show that the agreement improves production or distribution or promotes technical or economic progress, is indispensable to achieving the claimed benefits and does not substantially eliminate competition.

27. CCS sees no reason, as suggested in the background paper, why geographic market definition should not follow the standard SSNIP methodology. Identifying the geographic scope of a market is intended to delineate the market based on all potential competitive constraints, which logically has to include those originating

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<sup>9</sup> "CCS Guidelines on the Substantive Assessment of Mergers" paragraph 7.18.

overseas. Any analysis that excludes (or includes) overseas competition without considering the circumstances of the case simply risks identifying the market incorrectly. Inferences drawn from this, such as looking at market shares as a proxy for the degree of competition, will thus become meaningless.

**Q8. 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?**

28. The current voluntary notification system was adopted as it was felt that a light-handed legal framework for mergers was more appropriate for Singapore's small open economy. Given that most mergers in an open trade orientated economy are unlikely to raise serious competition issues, a voluntary regime avoids unnecessarily increasing business costs or delaying business decisions as a result of lengthy merger investigations. This also allows CCS to focus on mergers that are more likely to raise competition issues and devote its limited resources to areas of greater benefit. The relatively small size of the economy also means that CCS is likely to become aware of mergers that might raise competition concerns yet have not been notified. In line with this framework merger parties are also allowed to complete an anticipated merger or to undertake further integration of a merger at their own commercial risk, when an anticipated merger/merger is being reviewed as part of a notification or during an investigation.

## ANNEX A

**Background on the size of the Singapore economy relative to other countries**

Table [A] ASEAN Economies and population data

Country	GDP (mln current US\$)	Population (thousands)	Trade to GDP ratio (2004-2006)*
Indonesia	364,459	223,042	60.4
Thailand	206,247	64,724	143.7
Malaysia	148,940	25,767	222.0
<b>Singapore</b>	<b>132,158</b>	<b>4,393</b>	<b>456.7</b>
Philippines	116,931	84,590	100.7
Vietnam	60,884	84,108	144.4
Myanmar	13,123	50,962	54.2
Cambodia	7,193	14,351	140.0
Brunei Darussalam	6,400	381	144.9
Laos	3,404	5,765	69.7

\*"Trade-to-GDP ratio" is the sum of exports and imports divided by the gross domestic product. There is no direct cause and effect relationship between this ratio and the health of an economy. It measures a country's "openness" or "integration" in the world economy. It is expressed as a percentage.

Source: World Trade Organisation (2006 data)

Table [A1] Large and medium economies and population data

Country	GDP (mln current US\$)	Population (thousands)	Trade to GDP ratio (2004-2006)
USA	13,201,819	298,988	26
Japan	4,340,133	127,565	28.8
UK	2,345,015	60,361	57.6
Canada	1,251,463	32,556	72.3

Source: World Trade Organisation (2006 data)