Government in Markets: why competition matters

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Outline

● Why competition matters
● Why and how government intervenes in markets
● Changing role of government
● More effective intervention
Why should government care about markets?

- Competition in markets delivers big benefits
- Examples show benefits of increased competition
- But hard to predict benefits in advance
Case study: EU aviation

- The EU aviation market was very heavily regulated up until the 1990s
- Reforms lead to reduced support for national carriers, and any airline with a license from an EU country was allowed to operate any route
- Led to exit (Sabena) and entry (e.g. Ryanair, Easy Jet)
- Results:
  - lowest non-sale fare fell by 66% between 1992 and 2002,
  - flight frequency increased by 78% during the same time period.
  - No worsening of safety associated with low-cost airlines or increased competition.
Why should government care about markets?

- Government and markets closely linked
- Intervention is frequently required
  - Market failure
  - Outcomes
Why Government intervenes

Why does Government intervene in markets?

Even with a market framework markets can fail or may not deliver the ‘right’ outcome

To make markets work more effectively
- Setting the market framework
- Protecting competition in markets
- Ensuring that consumers are able to exercise choice, and are not coerced or defrauded.

To influence market outcomes
- Addressing externalities – e.g. pollution, congestion
- Using markets to deliver public services
- Adjusting the outcomes for different groups.

Government interventions to influence outcomes can have an impact on market effectiveness
How Government intervenes

Direct Government participation in markets

Acting as a supplier
- Through direct provision of goods and services to the public, and as collector and holder of public sector information

Acting as a buyer
- Through competitive tendering

Indirect Government participation in markets

Taxes and subsides
- Through changing the costs of goods and services

Regulation and influence
- Through statutory requirements, information campaigns
How is Government’s approach changing?

- **Long term trend** – from direct state ownership to regulation and indirect control

- **Impact of the economic downturn** – too soon to tell?

- **Softer intervention** – alternatives to direct regulation

- **Burden of proof** – from justifying government intervention to justifying markets?
Effective Intervention

- Entry and exit
- Alternative instruments
- Consumer and producer interests (and evidential bias!)
- Importance of competition assessment early in the policy making process
  - Part of Competition Authority advocacy role
Regulation issues in the UK

- Pharmacies
- Energy
- Taxis
- Alcohol retailing
Regulation case study: pharmacies

- Control of entry regulations were introduced in 1987 to reduce costs to the NHS. This:
  - restricted consumer choice and convenience
  - restricted competition on ‘over the counter’ drugs
  - provided blunt incentives for pharmacies to compete on additional customer services

- The regulation of entry costs consumers £25-30 mn per year more for over the counter drugs, businesses £16mn per year in compliance costs, and the NHS approximately £10mn per year in administrative costs
Key questions for policymakers

Does the policy affect...

- Entry and exit
- Nature of competition between firms
- Consumer behaviour in markets
Conclusions

● Decisions to intervene
  - Are we at a turning point?

● How we intervene
  - Can we improve the quality?

● “Government in Markets”
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