Competition, Innovation, and Growth

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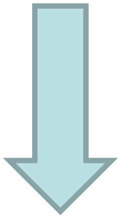
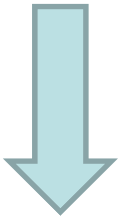
The link between competition and growth

Competition



Productivity



Growth

Competition (antitrust enforcement, liberalisation, market integration) contributes to productivity and economic growth.

- Internal productivity: competition induces firms to become more efficient to stay ahead of rivals.
- Sectoral productivity: competition allows high-productivity firms to replace laggards.
- Dynamic efficiency: competition pushes firms to invest and innovate.

The role of competition policy

How can competition policy affect this scheme?

Competition advocacy: Promote market liberalisation and the removal of entry barriers; foster a competition-friendly market culture.

Enforcement and deterrence

- Anticompetitive agreements and cartels (agreements among competitors raise prices but also decrease innovations)
- Abuse of dominance (internal growth is good but the level-playing field should be guaranteed)
- Merger control (external growth should be allowed if efficiency gains outweigh market power effects)
- State Aid policy (correct market failure; avoid crowding out of private funds and distortions of the internal market)

Finding the right balance

Investments and innovations are driven by the desire of firms to make profits and be better than rivals

Important to avoid policies which may deprive innovators of their expected fruits; else, incentives to innovate are reduced/eliminated

But also, need to avoid that future innovations are deterred and to guarantee that other companies could later challenge today's innovators

(IPRs laws are themselves the product of this balancing exercise)

Competition policy should respect innovators' rights, but be vigilant, and intervene in exceptional circumstances (cfr. case-law on refusal to license).

Pay-for-delay (reverse payments) cases

Several cases in US and Europe: a pharmaceutical company holding a patent on a pharmaceutical product pays a rival generic company to settle a patent litigation, with the latter committing not to enter the market (or delay entry)

EU: *Cephalon, Lundbeck, Servier (and Fentanyl, but not patent litigation)*

US Supreme Court: in *FTC v. Actavis*, it rejected the 'scope-of-the-patent test' (under which agreement would be legal if terms fell within the exclusionary potential of patent), because patent are *probabilistic*, i.e., may be invalid.

Relevant evidence: if the amount paid is much higher than the patent holder's expected litigation costs, and than the generic's expected market profit, difficult not to infer that the potential competitor is paid off to exit the market.

Expected strength of patent may also be an indicator.

Standard-Essential Patents (SEP) cases

Cases where the holder of a Standard-Essential Patent seeks (or threatens) an injunction against another firm, to extract higher payments

EU: *Samsung, Motorola*

Standards can be extremely beneficial: they create economies of scale and reduce barriers to entry by fostering interoperability.

But a firm which owns a SEP could hold up users. For this reason, owners of SEP should commit to license under FRAND (Fair, Reasonable, and Non-Discriminatory) terms.

By threatening an injuction to a willing licensee (which is ready to accept FRAND determination by a court or arbitrator), a SEP-holder contradicts its FRAND committment.

Google

Perhaps main business practice under investigation:

- Specialised search services ("vertical" search) such as product, hotel, restaurant, flight, search engines: Google displayed own services more prominently than competitors', even if latter very relevant to consumers

- Concern that lower visibility would divert internet traffic, and may affect negatively consumers depriving them of new and better rivals' products
- Google commits to display three rival links in a comparable way to its own services (e.g., pictures)
  - When Google charges merchants for inclusion in its specialised search the three rivals will be selected by an auction mechanism
  - When it does not, natural search will select the three rivals

- Objective: restoring visibility so as to allow competitors to offer new products with minimum interference with Google's property rights and algorithm.

R&D Cooperative Agreements

Because of spillovers of its R&D results, a firm may not be able to appropriate all of the benefits from its R&D expenditure (well-known public good problem, leading to under-investments)

R&D cooperation may allow to internalise these spillovers, as well as put together complementary skills/assets, thus raising R&D. But:

(1) Firms carry out R&D to improve their competitive positions vis-a-vis rivals. The larger their joint market share the less procompetitive the agreement
(2) Spillovers tend to be the larger the 'higher' the R&D stage (more difficult to appropriate basic research; easier when getting close to production and commercialisation)

Regulation 1217/2010 on research and development agreements:

- If parties are not competitors, then agreement is exempted from art. 101(1)
- If competitors, exemption if their share of relevant market is lower than 25% (they can also have joint exploitation of R&D results)