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Fair Competition: The Engine of Economic Development

The idea of competition is central to economics. The study of perfectly competitive economies attracted economists till mid 1900s when Edward Chamberlain and Joan Robinson attempted to develop a competition theory which is more realistic. Today, this is known as imperfect competition. Economists have also looked at how oligopolies, monopolies and monopsonies operate, in a theoretical setting, often with the help of game theoretic tools. In conventional economics, the study of competition falls under the label of microeconomics. However, both macroeconomics and growth theories implicitly assume a certain notion of competition. Thus, in economic theory, conclusions emanating from growth theories crucially depend on what sort of competition is assumed.

Competition and economic development

Economic development refers to an improvement in the livelihood of people – in terms of incomes, availability of employment, access to safe drinking water, access to health facilities, access to housing facilities, access to education, access to credit, access to information, access to transportation, access to telecommunication and so forth. Usual accounts of economic development highlight the role of human capital, incomes, health facilities, better institutions, etc in improving the quality of life of people and thereby promoting economic growth as well as development. Though all accounts of economic growth implicitly assume a certain *state* of competition (perfect competition, oligopoly, monopoly or a combination of the three), this state is often given inadequate attention in the literature and in policy discussions. In fact, what is often overlooked is that the factors which promote economic development work only under a certain configuration of competition. However, an adequate understanding of the concept and mechanism of competition is yet to be found in the economic literature. This lacuna creates problems not only for economic theory but also for applied economics; in particular, for policies designed to promote economic development such as competition law, banking restrictions, financial regulation, labour laws, trade directives, etc. For instance, it has been pointed out that attempting to promote competition and efficiency may actually cause unemployment (Bhattacharjea 2010, 32).

What is fair competition?

Prefixing competition with fair brings to our consideration the issues of justice and ethics. There, however, cannot be a universal algorithm for what is just and ethical. These have to be devised based on concrete socio-economic conditions prevailing in a country. For example, in a country which has a small population of labourers, adoption of labour-saving technology is relatively less unjust when compared to a country which has a large unemployed labour force. In short, the idea of fairness should be contextual, especially when examining a complex phenomenon such as competition. Therefore, fair competition can only be defined keeping in view the broader macroeconomic objectives of India such as elimination of poverty, increasing employment, ensuring price stability, etc. This brings us to the question: can the objectives of competition law be diametrically opposed to the broader macroeconomic objectives? Can we have efficiency as an objective even it leads to job losses? Shouldn't competition law be so designed to promote economic development? Bharracharjea categorically writes in the negative that

> the objective of modern anti-trust is to present market players from restricting competition in ways that are on balance harmful to efficiency and consumer welfare. It targets abuse of a dominant position in the market, not firm size or dominance as such, and it does not seek directly to control prices or profits: it only strives to preserve conditions which would allow market forces to keep them in check. It does not attempt to fulfill social objectives such as protecting employment. (Bhattacharjea 2010, 32)

In the following paragraphs, it will be argued that fair competition is a necessary condition for economic development and in order to ensure this, one requires an in-depth understanding of the sphere of production and social relations in an economy.

Competition policy

Usually, competition laws are in place to ensure that firms can make price and quantity adjustments with ease without abusing its dominant position; the merits of such adjustments are efficiencies in allocation and production and the welfare of consumers. Moreover, as the following excerpt (which is part of a recent judgment pronounced by the Supreme Court of India) indicates, the notion of competition is only applied to market structures:

> The main objective of competition law is to promote economic efficiency using competition as one of the means of assisting the creation of market responsive to consumer preferences. The advantages of perfect competition are three-fold: allocative efficiency, which ensures the effective allocation of resources, productive efficiency, which ensures that costs of production are kept at a minimum and dynamic efficiency, which promotes innovative practices. (*Judgment in Civil Appeal No. 7999 of 2010 pronounced on 9th September, 2010*)

The above passage suggests that the creation of markets which respond to consumer preferences promote economic efficiency. Ultimately, competition law aims to create an economy which enjoys the benefits of perfect competition. By now, it is quite well known that the state of perfect competition is a situation in which “the possibility of any competitive behavior has been ruled out by definition” (McNulty 1968, 641); although it figures prominently in all textbooks of microeconomics. It is a state where the forces and effects of competition have reached their limit. In fact, according to McNulty, the concept of perfect competition is “analogous not to the principle of gravitation but rather to the idea of a perfect vacuum” (McNulty 1968, 643). Moreover, dynamic efficiency is not compatible with a state of perfect competition. For, innovation in one firm will enable it to fix prices and it will ensure extra-normal profits. In a state of perfect competition, the firms are price takers who earn just enough to cover their costs. Therefore, the above objective of competition policy seems to be flawed on the following grounds: (1) perfect competition as a state of affairs is not only unrealistic but also undesirable owing to the absence of any competitive forces, (2) sphere of exchange is preferred over sphere of production which can lead to the creation of inappropriate policies, especially for a country like India.

Understanding the process of competition: markets and prices

One of the explanations provided for sustaining competition in markets is the protection of consumer interests. A competitive market structure, in theory, alters quantities and prices in accordance with the consumer tastes and preferences. Such an understanding of competition makes the error of viewing consumers as distinct from producers. An individual, in most cases, is both a producer and a consumer of commodities and services. One wonders why competition protects only consumer interests. For instance, if an individual does not receive adequate income from production, she will not be able to participate in the consumption process. The reason behind this demarcation of individuals into consumers and producers is because of the dominance enjoyed by the sphere of exchange in modern economic theory and analysis. The prominent economist, Krishna Bharadwaj points out the danger in such analyses:

> The relations of exchange are not autonomous, nor are the extent and specific forms of exchange. They are primarily, and to a considerable extent, a manifestation of the relations in production, which, as it were, provide a basis for supporting the sphere of exchange (or circulation). The type of exchange signifies the existence of a certain institutional organizational form within which production takes place. (Bharwadwaj 1986, 66)

In other words, the study of exchange relations cannot be divorced from that of production relations and conditions. More importantly, the conception of competition cannot afford to look at the sphere of exchange alone.

The concept of competition has to have empirical relevance and should be operational in nature. Usual accounts of competition, limited as they are, primarily study the interaction between private business firms. This narrow outlook poses severe problems for an economy such as ours. For, as we know, organised sector employment forms less that 10 per cent of the total employment. A satisfactory account of competition for India must be able to describe how firms/households compete in the informal sector. Or, it should throw light on how the informal sector and formal sector compete, if at all, for labour. In other words, an informed competition policy can only be formed after we have an adequate understanding of the *structure* of the Indian economy – relating to production, exchange, consumption, employment, demographics, finance etc.

The idea of allocative efficiency is linked to the theory of prices. The relationship between market prices, efficiency and economic development therefore requires to be scrutinized. First, the idea that market prices are unbiased, neutral and apolitical needs to be dispelled. Such a view is tenable only if the sphere of exchange is divorced from the sphere of production. To quote Bharadwaj again:

> Under competitive exchange, an appearance is maintained of an intrinsic justice in the operation of the impersonal and 'self-propelling' market forces of supply and demand, especially when distribution is also explained on the same ground (Bharadwaj 1986, 21).

In short, it would be dangerous to make market prices the sole regulator of exchange. For, "exclusion in inherent in the logic of markets. Markets may exclude people as consumers or producers or both" (Nayyar 2003, 97). Consumers can be excluded from the market owing to insufficient incomes or because of their location. Producers can be excluded if they have neither physical nor financial assets. They can be also excluded if they do not have capabilities which are acquired through formal education, training or experience. However, from the point of view of efficiency, these exclusionary tendencies of the market pose no problem. But, if the objective is economic development, trying to achieve efficiency may not be the correct path to choose. Thus, the objective of fair competition becomes crucial, for market prices can have devastating effects on the livelihood of a large number of people.

Evidently, pricing mechanism alone cannot lead to fair competition and hence to economic development. Indeed, competition exists in varying degrees in all aspects of our economic lives – be it employment, production, consumption or sales. Fair competition, however, is largely a function of the institutions which are in place. They could be taxation laws, banking regulations, investment limits, restrictions on foreign exchange, labour laws, etc. Or they could be determined by gender, caste, region or language. Or they could be directly affected by the sector in which the individual is employed – formal or informal sector. Since competition law is an institutional arrangement which mediates between economic development on the one hand and social development on the other, it ought to occupy a more critical role in promoting development (see Nayyar 2003, 99 on the crucial role of institutions) and not just attempt at achieving efficiency.

Towards 'fair' competition

Interestingly, the word competition comes from the Latin word *competere* which meant 'strive together'. An appropriate notion of competition should, perhaps identify, ways in which individuals and firms can 'strive together' or compete which could result in improvement in quality of commodities and services, increase in profits and wages, strengthening of consumer loyalty as well as freedom, better organizational arrangement, environmental gains and overall gains to the entire community. Only if competition is conceptualised in such a manner can we achieve economic development. The above outcomes of competition become irrelevant if one cannot describe the process of competition itself. Since economics primarily deals with prices and quantities, non-economic factors affecting competition such as gender, caste, religion, language, etc are not taken into account. In fact, these socio-cultural factors play a very significant role in the Indian production sphere. For example, a dalit woman may be denied a service even if she can pay its market price. Or they end up in poorly paid jobs such as sweepers, loaders, unskilled construction workers, security guards, etc (Ghosh 2011).

A satisfactory account of competition must at least contain answers to the following questions:

(1) What processes can be considered competitive?

(2) Which factors determine the ability to compete?

(3) What are the benefits of competition?

The temptation to answer these questions in terms of equilibrium outcomes must however be resisted.

Processes which can be considered competitive would depend on the specific socio-political and economic conditions of an economy. For instance, because 60 per cent of Indians are employed in agriculture, one should be skeptical about a competition policy which favours non-agricultural sectors at the expense of agriculture. For, such a policy will have undesirable affects on the earnings of those involved in agriculture.

Similarly, a competition policy which targets the formal sector alone will have adverse effects on the informal sector. Therefore, our competition policy should be one which not only takes intra-industry and inter-industry competition into account, but also the competition between agriculture and non-agriculture, formal and informal and rural and urban sectors. The existing notion of competition is one which only tries to attain efficiency. Surprisingly, it has been argued that firms which promote development could engage in anti-competitive behaviour (Ghosh and Ross 2008, 37) and hence competition policy should not try to promote economic development. Such a rationale cannot be accepted if the objective of competition policy is to attain fair competition and through this economic development.

The *ability to compete* will be constrained by the availability of factors such as: incomes, technology, property, learning, information, credit, etc. Access to credit is a major hurdle especially for small firms (Penrose 1959, 192). In addition, the location of firms will crucially determine the ability to compete. For example, a producer who is located in an urban slum will not have easy access to public services. Non-economic factors such as gender, caste and language also play an important role as pointed out earlier.

No ex ante judgments can be made about the outcomes of competition. This is because, the outcomes would be determined through a complex interaction of economic and non-economic forces. Sylos-Labini, an economist who devoted numerous years studying oligopoly, writes:

> cost reductions due to new methods which, because of technological discontinuities, are not within reach of all firms lead not to price reductions but to increased profits. On the other hand, trade-union pressure or government intervention may cause cost reductions to be translated into higher wages (Sylos-Labini 1969, 123).

The above excerpt highlights the dynamic role of interdependence present in an economy. That is, the rice industry, steel industry, electronics industry and mobile phones industry are interrelated. This interdependence is clearly brought out in an input output transactions table. In any case, because technological improvements are often firm specific, they generally result in increased profits and not in price reduction.

Additionally, the presence of institutions such as trade unions help the workers in receiving a portion of the technology-induced profit rise. However, it will be possible to analyse the social benefits by examining variables such as wages, profits, employment, etc in particular industries as well as across the entire economy.

Summing up

To conclude, economic development is broadly understood as the betterment of livelihood of the individuals in an economy. These individuals, who are both producers and consumers, could be employed in agriculture, industry or services. A sustainable plan for economic growth and development is one where all the producers compete (work together) in such a way that all the participants gain. Such a plan can be devised only if we pay particular attention to the production sphere and take non-economic factors into account. By concentrating our competition policy on the exchange sphere, we are forced to consider ways to only achieve efficient allocation of resources and not the generation of resources. Whereas, the concept of competition ought to be a broader one, which suggests ways and means of increasing output, employment and incomes. In short, a policy to achieve fair competition must be envisioned so that it will promote economic growth as well as development.

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