

# Economics of EU Integration

## Lecture 7

### Competition Policies, Regional Policies, and Environmental Policies

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## Today

- 1 Competition Policy: Where it came from, what it is, how it works
- 2 Regional Policy: what it claims to do
- 3 Environmental policy: what it might do in the future.

## Part I

### Competition Policy

## Why do we need competition law?

EU Competition policy attempts to ensure markets

- remain competitive (*Anti-trust/caterls/mergers control*)
- become more competitive (*liberalization*)
- maintain level playing field (*state aid*)

Benefits of competitive markets in the EU

- ensures the competitiveness of industry
- *may* lead to technological innovation
- produce benefits for consumers (lower prices)

## History of Competition Policy in EEC/EU

- 1951 European Coal and Steel Community (ECSC)
  - ① Antitrust and merger rules for coal and steel
  - ② Concept of supranationality EC Treaty
- 1957 agreement on ambitious competition law (except merger control)
- 1989 Direct exclusive competence of European Commission  
Introduction of Merger Control Decentralization of the power to apply antitrust rules
- 2004 Sharing of competence between European Commission and Member States' competition authorities
- 2009 Lisbon?

## Important Legal Pillars

- ① Article 81: No Cartels, no anti competitive agreements
- ② Article 82: No Abuse of Dominance
- ③ Article 86: Liberalization
- ④ Article 87: State Aid Controls
- ⑤ Reg. 139/2004: Merger Control

See Massimo Motta, *Competition Policy: Theory and Practice*, CUP, 2004.

## Benefits of Competition Law Enforcement?

- Air transport liberalisation: Market entry of low cost carriers (Ryanair's average European fare ca. 40 eurs / British Airways 268 eurs)
- Air transport cartel: SAS / Maersk cartel (ticket prices increased 50%)
- Mobile telephony liberalisation: (OECD study)

(See <http://europa.eu.int/comm/competition/>)

## Costs of Collusive Behaviour

From Art. 81(1): Collusive behaviour is considered contrary to consumer interests when it entails agreements to:

- Raise prices;
- Restrict output, markets, technical development or investment;
- Share markets or sources of supply;
- Apply dissimilar conditions to equivalent transactions with other trading parties;
- Make the conclusion of contracts subject to supplementary obligations.

## Mergers and Acquisitions

- M&A activity is high in EU.
- Much M&A is mergers within member state:
  - about 5 per cent 'domestic'
  - remaining 45 per cent split between:
    - one is non-EU firm (24 per cent),
    - one firm was located in another EU nation (15 per cent)
    - counterparty's nationality was not identified (6 per cent).

## Economic Logic of M&A

Liberalise markets (open them up) → De-fragmentation (imperfectly competitive firms now face overseas competitors) → Pro-competitive effect → Industrial restructuring (M&A, etc.) ⇒ RESULT: fewer, bigger, more efficient firms facing more effective competition from each other .

## Industrial Policy in EU

Big idea: use industrial policy to increase competitiveness for benefits described above.

- Assume imperfect competition, increasing returns to scale.
- In the absence of perfect competition firms will change a price that is above their marginal cost in order to maximize profit
- If there are more firms in the market, competition will lower the mark-up that each firm can charge
- With imperfect competition and increasing returns to scale only a given number of firms can survive in a market.
- The higher the mark-up (or gap between prices and marginal cost) the more firms can survive.
- The break-even curve (or zero profit curve) shows how many firms can break even at each level of mark-up

## Relationship summarised in BE-COMP Diagram

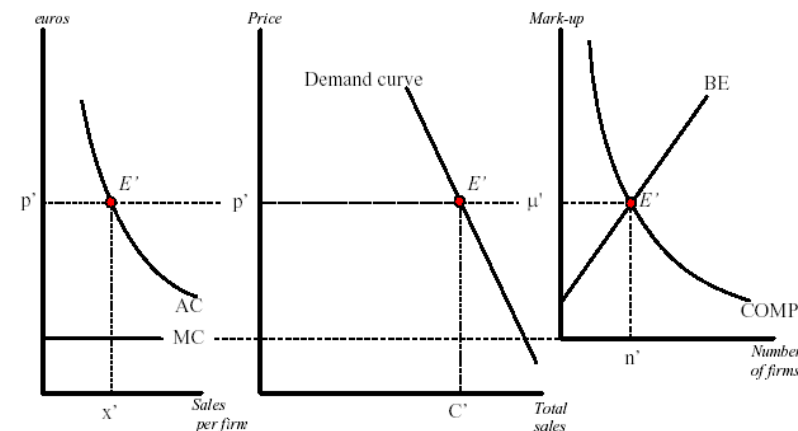


Figure: The break-even curve (or zero profit curve) shows how many firms can break even at each level of mark-up

## Use BE-COMP to think about integration

Assume integration leads to trade liberalisation between two countries: home and foreign.

- ① The impact of the trade liberalisation implied by integration is to increase the size of the market leading to more competition.
- ② Increased competition means that the typical firm will have to cut its mark-up.
- ③ At the same time the larger market means that more firms can survive.
- ④ This is because the larger market creates opportunities for higher sales, so with a given mark-up a larger number of firms can survive.

Can also think about mergers and acquisitions. See paper by [3], also [1, Chapters 6 and 12], and [2].

## Part II

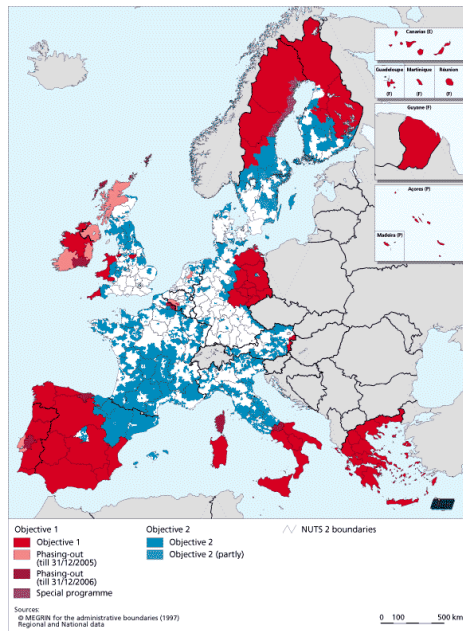
### Regional Policy

## Who is regional policy for?

- Less-favoured regions
- Areas with specific handicaps
- Vulnerable groups in society
- Local and regional authorities
- Applicant countries

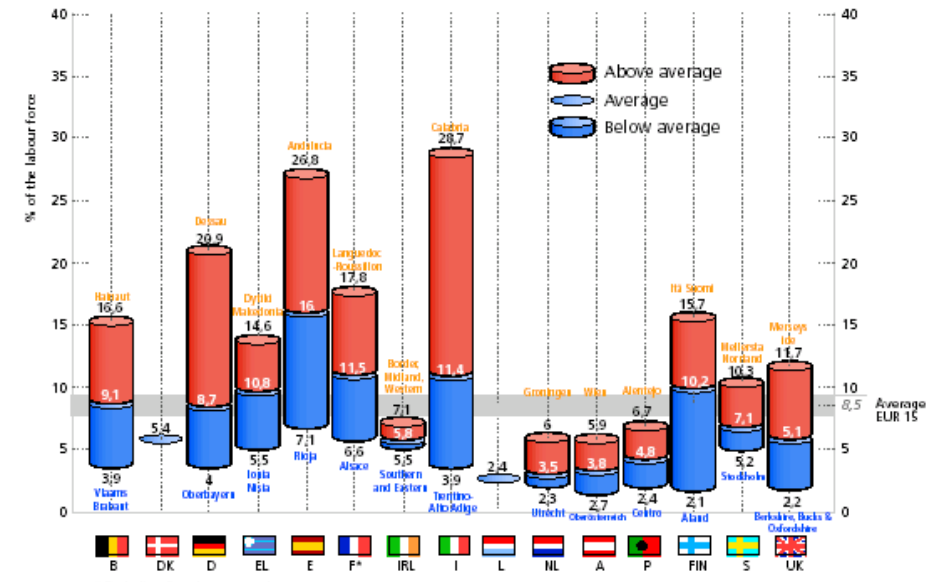
## What does it do?

- Improving regional competitiveness
- Expanding and improving employment
- Balanced development in urban and rural areas and areas dependent on fisheries
- Embeds other Community policies at the service of the regions
- Supports notion of 'Europe of Regions'
- Facilitates loans from the European Investment Bank



## Unemployment: A Pressing concern in the EU

Unemployment rates by Member State and their worst-hit regions (April 1999)



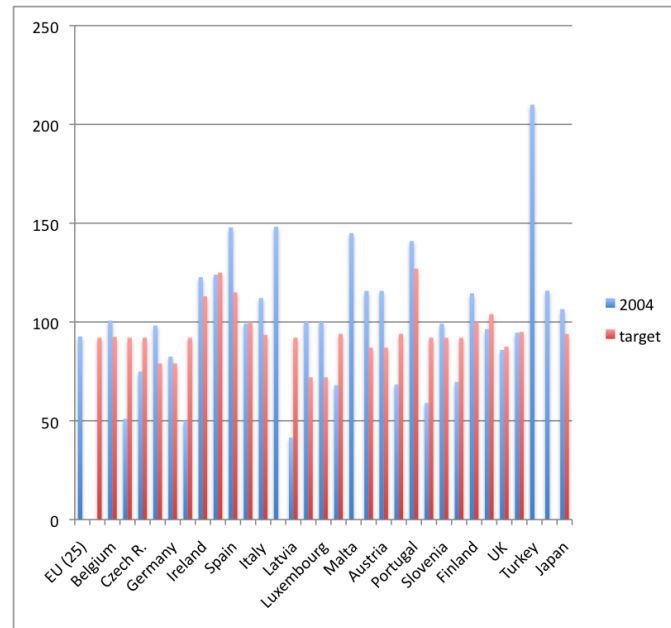
## Challenges for Regional Policy

- Competition
- Flexibility of firms due to technological change
- Enlargement

## Part III

### Environmental Policy

## There is a problem.



## Summary

- 1 Competition policy is key for economic and monetary union to succeed
- 2 Regional policy is built on opposite of competition—all about social cohesion
- 3 Environmental policy: a lot done, more to do.

## References

- [1] Richard Baldwin and Charles Wyplosz. *The Economics of European Integration*. McGraw-Hill, London, 3rd edition, 2009.
- [2] Michael Burda and Charles Wyplosz. *Macroeconomics: A European Text*. Oxford University Press, 2nd edition, 1997.
- [3] Martina Martynova and L.D.R. Renneboog. Mergers and acquisitions in europe. Discussion Paper 6, Tilburg University, Center for Economic Research, 2006.