

**KEYNOTE ADDRESS
BY
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**AT THE
MALAYSIAN COMPETITION LAW CONFERENCE**

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Introduction and context

1. I would like to start by saying how delighted I am to be here at the opening of this second Malaysian Competition Law Conference. I want to extend my congratulations to the organizers for the considerable efforts that have gone into staging a major international event such as this, on such an important and topical issue. The introduction and implementation of robust competition law in Malaysia is a very welcome development for our country. The opportunity provided by this conference to address the various issues associated with competition law is most timely. I know we will all benefit greatly from the insights of the eminent participants gathered here.

2. The implementation of Competition Law in Malaysia forms part of broader measures being put into place to meet international regulatory

standards in this and many other areas. Such regulations help create a stable and investor-friendly business environment for domestic and international actors. Over 120 countries now have competition legislation similar to that contained in Malaysia's Competition Act. This is an increase of over 600% in the two and a half decades since 1990 when only 20 countries had such legislation. Similar regulations are also set out in various multilateral and bilateral trade arrangements such as those of the EU, WTO and ASEAN. These form part of the deepening economic ties between countries as part of economic globalization. Implementation of competition law is also increasingly taking place at the global level. Far more cases than in the past that are brought in the US and the European Union, now have international dimensions.

3. The main aim of competition policy is the creation and maintenance of a level playing field for business, so that competitive forces can operate effectively and deliver optimal economic outcomes. This objective is encapsulated explicitly in the goal of the Malaysia competition law, 'to increase consumer welfare, economic efficiency and growth'. It is achieved by the prevention of harmful monopolistic practices – namely the abuse of dominant market positions by individual firms, and market-sharing agreements between dominant players. This is seen in practices such as collusion to artificially inflate prices or depress wages. The effective enforcement of competition law should help prevent such harmful practices and promote a fair and healthy competitive environment.

4. But while the extension of competition law is in itself undoubtedly highly positive, a closer look at its implementation reveals how contested it remains in practice. In an apparent dichotomy, while competition law is coming into force in an ever-increasing number of jurisdictions, at the same time there is also a clear trend globally towards a deepening concentration of market power. This is the case across a variety of industries, from cutting edge technology and communications to healthcare and pharmaceuticals, agriculture, and mining. The impacts of such concentration are also reflected in the many legal claims and cases heard around the world that relate to abuse of market by dominant economic players. These include collusion to depress wages such as by US tech companies including Google and Microsoft, and price setting in the healthcare and pharmaceutical industries.

5. This apparent dichotomy reflects the economic realities that drive processes of concentration. These are in turn reinforced by political dynamics, as the economic power enjoyed by dominant players is leveraged into political influence. Competition policy has since its earliest conceptions been shaped by the interaction of economic considerations with political dynamics. This means that in practice it has always been couched with exemptions and exceptions. Many mergers gain regulatory approval even though they result in excessively concentrated market power. The enforcement of competition policy is thus ultimately an attempt to maintain fair market conditions in the face of economic and political

pressures that seek to undermine them. As an economist, rather than a lawyer, I want to focus on these economic dimensions of competition law.

Economic dimensions of competition law

Economic theory

6. Standard economy theory suggests that a well-functioning market economy delivers significant benefits. It leads to job creation and lower prices, and as a consequence, higher living standards and economic growth. A well-functioning economy is not always fully competitive, however, as it is perfectly rational for firms to seek to strengthen their market positions and increase profits. This process also unfortunately serves to limit competition. When firms begin to display monopolistic behavior, consumers are the biggest losers, while economic growth is ultimately also constrained.

7. The dangers of monopolistic behavior were recognized by Adam Smith, known as the father of economics. As he put it in the “Wealth of Nations”, *‘A monopoly granted either to an individual or a trading company has the same effect as a secret in trade and manufactures. The monopolists, by keeping the market under-stocked, ... sell their commodities much above the natural prices, and raise their (own) emoulements, ... greatly above their natural rates’*. He went on to say that, *‘when people of the same trade meet, it always ends in conspiracy against*

the public, or in some contrivance to raise prices'. While such meetings cannot be prevented, it is the job of policy-makers to manage and regulate their outcomes. For Malaysia, it is the MyCC that plays this crucial and challenging role through their implementation of the 2010 Competition Act.

8. From the perspective of economics, the question of regulating monopoly power comes down to a comparison of costs and benefits. Economists' views on how to achieve an effective balance between monopoly power and competition have evolved considerably over time, along with the policies and practices of regulation that are based on them. Sound economic argument can justify the need for non-competitive larger-scale operations in some settings, including those of so-called 'natural monopoly'. This refers to situations with high fixed costs and economies of scale, which require huge investments to reach optimal production levels. This may justify the presence of a dominant market player. In these cases, rather than enforce competition policy, governments may adopt policies that encourage or protect them. This is especially likely to be the case when the sector involved is deemed of national or strategic importance.

9. Infrastructure provision is the classic natural monopoly, along with other public services such as electricity, water and security, which also have high fixed costs and additional welfare considerations as public goods. National development strategies based on import substitution

policies may also entail the protection and nurturing of key national industries and firms. Such an approach has been implemented successfully in East Asia and elsewhere over the past few decades. Special treatment is also often afforded to national airlines, widely seen as national champions deserving of government protection and support. Here in Malaysia, although they do have their own regulators, the telecoms and energy sectors are exempted from the provisions of the Competition Act.

Historical trends

10. Such exemptions are very common in competition legislation. Although there has been some movement away from protected monopolistic providers of public services recently in more mature industrialized economies, cases abound historically of effective industrialization based explicitly on protective government support for monopoly conditions. This approach was implemented in Germany and Japan in the first half of twentieth century, relatively successfully from an economic point of view, although the associated concentration of industrial power is also thought to have contributed to the rise of facism in both countries.¹ Both countries adopted more competitive policies after the war, as part of the broader post-war strengthening of competition law

¹ F.M.Sherer Introduction, in F.M.Sherer (ed.) 1994 Monopoly and Competition Policy, Volume I, The International Library of Critical Writings in Economics 0, Edward Elgar Publishing

in the European Union and in the US. The 1957 Treaty on the Functioning of the European Union included competition law as one its key provisions, while in the US, there was a revival of existing anti-trust legislation. This period of more active implementation there culminated in the successful break-up of the communications firm AT&T in the early 1980s.

11. As well as more democratic political tendencies in post war decades, this also reflected the growing recognition among economists at this time of the welfare and economic costs of a lack of competition. But there has since been a movement away from this more activist competition policy, and towards a much lighter regulatory touch, or what the Washington Post called 'extremely permissive enforcement'.² This is particularly true in the US, as reflected in the approval by regulators of numerous large-scale mergers over the past two decades. The Economist estimates that concentration has increased in two thirds of the 900-odd sectors of the US economy since 1997, with a wave of US\$10bn worth of mergers taking place since 2008.³ Given the global dominance of US companies, greater concentration in the US results in greater concentration globally.

12. This policy trend has again been based to some extent on changing economic thinking, including the argument that the costs of regulating

² Sherer 1994, Washington Post, 11/6/14

³ The problem with profits, The Economist, 26th March 2016

monopoly behavior may be so high that they outweigh any welfare benefits. Free market-leaning economists since the 1980s have been increasingly convinced of this.⁴ Since the cost of regulation is likely to be high, as it involves various transaction costs and creates its own distortions, and as the impacts of successful regulation are anyway still contested, the balance of costs and benefits may be judged to lie in less regulation and allowing the market to find its own equilibrium. Even if this is a sub-optimal outcome, it may still be the best available in welfare and efficiency terms.

13. A further argument relevant to any cost benefit analysis is that the extra-ordinary profits being made by concentrated corporate power in some sectors are necessary to fund their cutting edge scientific R&D. Such arguments are sometimes used in merger or anti-trust cases to help justify claims that any profits generated by the resulting monopoly status will anyway be reinvested into such valuable innovation. The creation of extraordinary benefits based on some form of monopoly protection can be used as grounds to apply for an exemption to Malaysia's competition law. Economists also believe that any excessive profits being made by dominant players will and do eventually attract competitors, and so ultimately the distortions created by excessive market power are likely to be self-correcting as new entrants drive down prices, restoring optimal welfare outcomes. Such arguments, put forward convincingly by well-

⁴ Posner, Miller et al. in Sherer, ed.

regarded economists in recent decades, have helped to influence regulators to pursue a permissive competition policy.

14. There is now growing recognition, however, that the greater concentration of firms in the US, and therefore globally, has resulted in the very negative welfare and efficiency impacts that competition policy is designed to prevent. This can be seen in both the direct impacts of dominant player abuses on price and wages, as well as in more indirect impacts resulting from the restriction of competition. Prices in the US have risen in a number of sectors following consolidation, including healthcare and communications, while consumer choice has also been greatly restricted in many sectors. More indirect impacts on innovation and entrepreneurship are reflected in a declining rate in the growth of new firms, with the creation of small and medium companies reportedly at its lowest level since the 1970s. Even though the higher profits enjoyed by dominant players do help to fund R&D and other investments, competition itself serves as an apparently indispensable spur to innovation and efficiency, and its absence ultimately constrains productivity growth.⁵

⁵ Washington Post, "How America became uncompetitive and unequal, June 11th 2014, New York Times, 'How Mergers Damage the Economy', October 11st 2015, The Economist

Welfare and efficiency

15. As mentioned, the ultimate goal of competition policy, whether in the US, Malaysia or elsewhere, is to enhance consumer welfare, economic efficiency and growth. Competitive processes promote welfare and growth in a number of ways. Firstly, they contribute to efficiency and productivity, thereby pushing out the production frontier and expanding the potential growth in an economy. Secondly, competition serves to foster innovation, proving a more important trigger in this process than the excess profits earned by monopolists. Thirdly, healthy competitive processes increase consumer welfare directly, by promoting lower prices, better quality of goods and services, and a wider choice of better products. There may also be a positive distributional aspect of this, as these benefits are enjoyed disproportionately by the poorest. Finally, the existence of a robust regulatory framework that includes competition law, helps to stimulate investor confidence.

16. In relation to efficiency and productivity, human nature dictates that when there is competition, we work harder. Just as with Darwin's 'survival of the fittest', competition drives firms to adapt effectively to their environment in order to survive and prosper. Studies show that markets with more competition experience greater productivity gains than those with higher levels of protection. This is not surprising, as businesses operating in a competitive environment are pressured into minimizing

costs, reducing waste, and allocating their resources as effectively as possible, in order to survive. The low barriers to entry in competitive markets enhance these incentives for greater efficiency, as more efficient businesses will prevail over less efficient ones.

17. The increased productivity that results contributes to lower costs and prices, with trickle-down effects as consumers and other firms benefit. Vigorous competition in upstream sectors can in this way greatly improve productivity and employment in downstream sectors. Productivity gains at the domestic level then enable Malaysian firms to compete more effectively in international markets. This is both in export markets, and against imports into the country. The importance of healthy domestic competition can be seen in China, where the lower costs and relative efficiency of its highly competitive local firms contribute to their competitiveness in global markets. This in turn has underpinned China's success as an export-oriented economy.

18. For firms to survive in a competitive marketplace, efficiency alone is not sufficient. As well as promoting efficiency, competitive forces also provide incentives for innovation. They help to keep firms on their toes, as a leading position today does not necessarily guarantee the same in the future. Their existing products and processes are continually being challenged by innovations that could force them out of business if successful. Competition thus drives businesses to innovate and create

new products and services, in order to maintain or increase their market share and profits. Although firms with large market shares do have high rates of innovation, helped by their excessive profits, so do businesses in more competitive sectors, spurred by these pressures.

19. As well as its role in increasing consumer welfare as a whole by increasing purchasing power and standards of living, greater competition may also have positive distributional effects. One recent study on Mexico by the OECD suggested that, *'the welfare losses due to the exercise of monopoly power are not only significant, but also larger, in relative terms, for the poor. Moreover,.. the inhabitants of the poorest states (are) the most affected by firms with market power'* (OECD 2013). This is not only the case for developing economies. A similar study on Australia and New Zealand also found that monopoly harms lower income groups more than higher ones.

20. The business and regulatory environment of an economy are key determinants of investment decisions. According to the Asian Development Bank, *'the appropriate enforcement of competition law both enhances the attractiveness of an economy as a location for foreign investment, and is important for maximizing the benefits that flow from such investment.'* (ADB 2005). For a small open economy such as that of Malaysia, in which inward investment still plays an important role, the presence of a robust competition law is vital. It creates a stable operating

environment for investors and national stakeholders, helping to ensure that domestic and international firms alike enjoy a level playing field.

21. Competition policies cannot work in isolation. They must be complemented by other related policies such as consumer protection, with robust implementation in one area helping to reinforce actions in others. Competition enhances consumer welfare by providing consumers with a wider choice of goods and services at competitive prices. Consumer protection, on the other hand, helps ensure that consumers can exercise their rights in relation to services and goods providers. Both are necessary to support a well-regulated and competitive business environment.

Challenges for competition policy in Malaysia

22. Rather than the harmful impacts of excessive concentration as in the US and more broadly, the challenges faced in applying competition law here in Malaysia, relate mainly to enforcement issues among small and medium companies. While any welfare and growth impacts are likely to be on a relatively small scale, the damaging effects of restrictions to competition are still felt however. This can be seen in the cases mounted so far by the MyCC against collusion and price setting, some of which do involve much larger scale cases. There is also increasing interest in our relatively flourishing Southeast Asian markets from the global giants in a number of sectors. These relationships offer a potentially rich source of

economic growth for the country. But they must also be managed effectively to ensure that dominant market players are not able to manipulate or abuse their favourable global positions in our domestic economy.

23. Small and medium-sized enterprises (SME) make up 97% of the Malaysian economy, and 90% are in the services sector, many of them very small-scale and family-owned. Many of these firms are in fact too small even to be of concern to the law, which only applies to activities involving a 20% market share or above. Cases brought by the MyCC so far have involved relatively clear-cut forms of collusive behavior within this sector, particularly relating to price-setting agreements within trade associations. These associations help smaller companies to overcome some of the limitations of their size, including through what are very common price setting practices, which many may not realize violate the new legislation. One review identified a widespread lack of awareness that such agreements are now prohibited.⁶ Further education of these stakeholders in the objectives and mechanisms of the new competition legislation is thus a key challenge.

⁶ Shila Dorai Raj and Rachel Burgess, 'SMEs and Malaysia's New Competition Law : Experiences to Date', in Michael Schaper and Cassey Lee, eds., *Competition Law, Regulation and SMEs in the Asia-Pacific : Understanding the Small Business Perspective*

24. As well as greater efforts in educating all those affected by the law, in the SME sector and beyond, an important role for the MyCC is to ensure that the law is being applied as widely as possible. Efforts in this area are demonstrated by a marked increase in the number of cases under investigation and their size. In its largest case yet, the Commission recently announced fines of nearly RM 214m for insurance companies accused of colluding with a local car mechanics' association. This case is likely to be vigorously contested by the companies however. An earlier conviction against two airlines, on the grounds of a market sharing agreement, was subsequently overturned. The Competition Appeal Tribunal found that their collaboration did not in fact represent damaging collusion. This highlights the fact that one of the biggest challenges for the MyCC - as with other regulators - remains to prove that abusive behavior has actually taken place.

25. While these cases point to the continued challenges faced in the implementation of the Competition Act at the domestic level, the MyCC must also monitor the operations of global players on the competitive environment here. This is especially salient in relation to foreign penetration of the country's retail sector, a target market for global companies. E-commerce is another challenging area due to the growing presence of sites like Alibaba and Amazon, both of which are already of course highly dominant players in other markets.

26. As the global economy evolves further towards cutting edge, high tech and sharing-based interactions, the challenges faced by regulators will be exponentially amplified. Influential companies who defend their dominant positions on the basis of their cutting edge R&D, will also continue to try to blur the line between anti-competitive and fair behavior. The job of policy makers and regulators remains to find the distinction between what is acceptable and what is clearly not. In this way, a balance may be achieved between economic tendencies towards monopoly, the special requirements of natural monopolies and national development strategies, and the consumer welfare and growth benefits of competition.

Ladies and Gentlemen,

27. It is very encouraging that Malaysia's Competition Policy is now in place and being applied, as just one of the many crucial elements of the country's broader regulatory framework. The MyCC must now work towards the further development of its approach in order to ensure it can fulfil effectively its challenging mandate.

28. As the organization itself puts it, it must proceed as if it were playing a highly sophisticated game of chess, in which clever strategy and tactics are required to fulfill the objective of creating a fair and healthy competitive environment. I'm sure that your deliberations over the next two days will explore these issues and more, and hope that these will be fruitful.