

Competition Policy vs. Industrial Policy as a Growth Strategy

TATSUO HATTA

Asian Growth Research Institute

Part I:

Growth Strategy

1. Two policies for growth strategy

- **Industrial Policy** promotes targeted industries through
 - trade protection,
 - net transfers,
 - tax breaks, and
 - government loans.
- **Competition Policy** makes the economy competitive through
 - anti-cartel policy,
 - trade liberalization,
 - deregulation, and
 - privatization of publicly owned monopolies.

2. Two Sources of Economic Growth

1. Innovation

2. Shifting resources

from low to high productivity sectors

- For example, migration of workers from the agricultural to the manufacturing sectors improved nation's productivity during the rapid growth period.

3. Why competition policy?

- If left to the competitive market, resources will flow in the direction of higher productivity, where the rewards are higher.
Hence markets allocate resources efficiently.
- However, this natural flow of resources often faces obstacles set up by incumbent firms to protect their vested interests.
- Competition policy is designed to remove the obstacles that hamper the natural flow of resources.

4. Theoretical Underpinning

- **Basic Theorem of Welfare Economics :**

A competitive market mechanism allows efficient resource allocation in the absence of market failures.

- **Market Failures:**

- Scale Economies
- Externalities
- Public Goods
- Information Asymmetry

Part II:

Industrial Policy

1. Cases for industrial policies

- Industrial policy, which intervenes with the market, can be justified only when a market failure exists.
 - Scale Economies (the infant industry)
 - Externalities
 - Krugman's Strategic Trade Policy Argument
 - Krugman, P. R. (1987). Is free trade passé?. *The Journal of Economic Perspectives*, 1(2), 131–144.
 - None of these justifications is well-founded in practice.
- ⇔ Chalmers Johnson, METI and the Japanese Miracles, 1982

2. Failure of Industrial policies in Japan

- Hiroshi Ohashi (2005)

- The subsidy on export of steel had an “insignificant impact of the industry growth of steel”

- Ohashi, H. (2005). Learning by doing, export subsidies, and industry growth: Japanese steel in the 1950s and 1960s. *Journal of International Economics*, 66(2), 297–323.

- Richard Beason & David Weinstein (1996)

- “There is no evidence that productivity was enhanced as a result of industrial policy measures.”

- Beason, R., & Weinstein, D. E. (1996). Growth, economies of scale, and targeting in Japan (1955-1990). *The Review of Economics and Statistics*, 286–295.

3. Industrial policies for declining industries

- Richard Beason & David Weinstein:
 - A disproportionate amount of Japanese targeting occurred in low growth sectors and sectors with decreasing returns to scale.
- Noland & Pack:
 - The Japanese industrial policy was mainly focused on agriculture and mining, which do not have international competitiveness.
 - Noland & Pack. (2003). *Industrial Policy in an Era of Globalization: Lessons from Asia (Policy Analysis in International Economics)*. Institute for International Economics.

4. Growth without government help

- Sony, Honda, and Panasonic did not get benefit from industrial policy.
- Hirotaka Takeuchi's list of successful industries that grew without government help
 - industrial robot, air conditioner, sewing machine, video tape recording, fax machine, audio equipment, car audio, typewriter, camera, carbon textile, tracks, TV games, music instruments, and forklifts
 - Takeuchi, Hirotaka. (2002). *Efficacy of Government-led business model (Nihongata seifu moderu no yukousei)*, Ministry of Finance, Policy Research Institute, Chapter 5.

5. Choice of Growing Industries

- **In an industrial policy, the government chooses the target industries politically.**
 - If an industrial policy fails, no one in the government takes responsibility.
- **In an competition policy, the private sector chooses the growing industries**
 - If a private Initiative fails, the investor has to bear the burden.
 - Careful studies of cost-effective of the investment before the start of projects.

Part III:

Competition Policy: A Historical Review

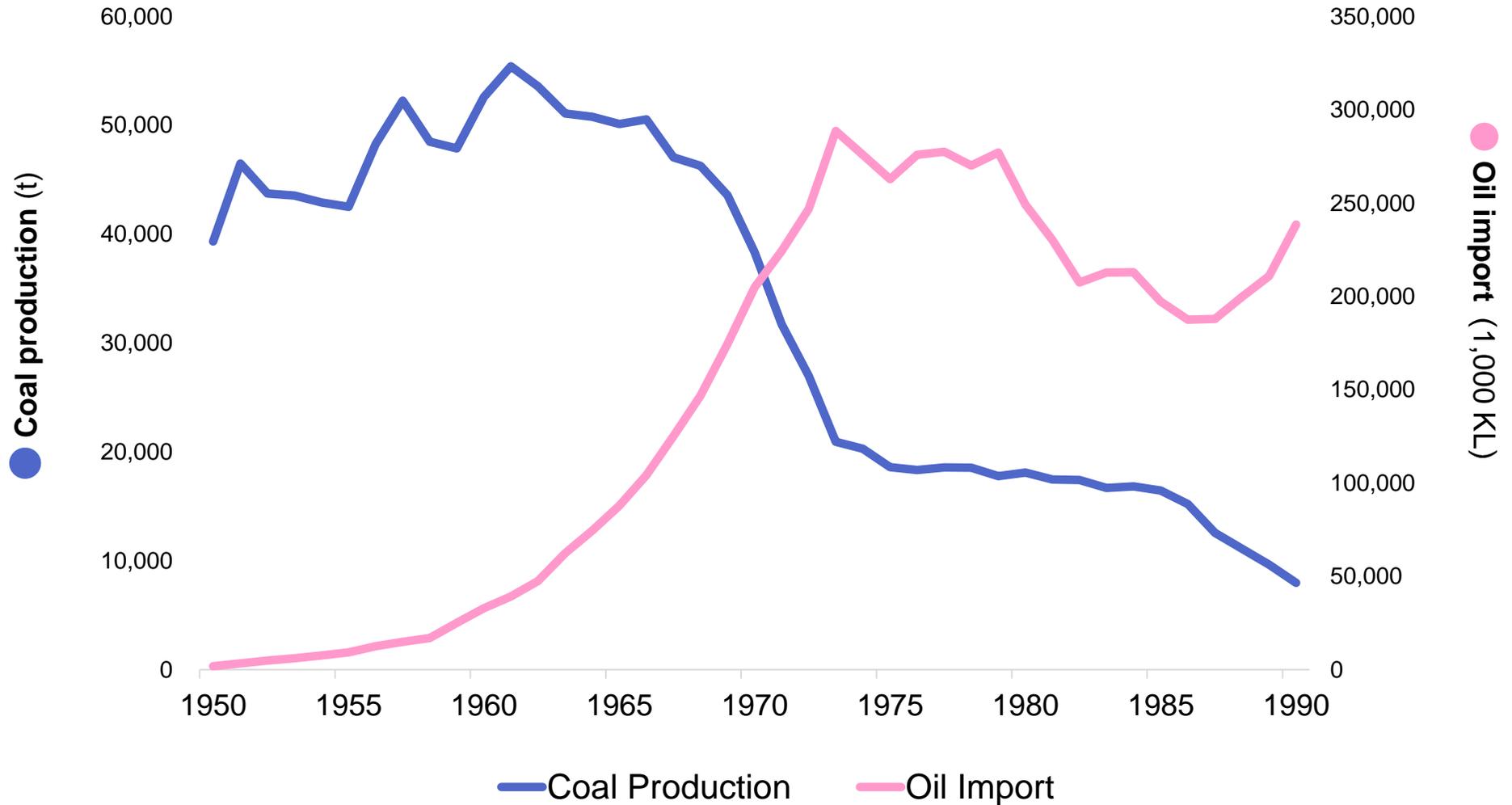
1. The tariff-free opening of ports in 1859.

- Domestic cotton growing was completely wiped out in 10 years after that opening.
- Ex-cotton farmers had to either change crops or find new jobs in cities. It placed an enormous hardship on farmers.
- The high growth of the early Meiji Period, however, would have been impossible without it.
- The opening of ports in 1859 was an archetype of competition policy.

2. The Post-war competition policies

- Dissolution of Zaibatsu
(the prewar industrial conglomerate) (1945–1950)
- Establishment of the Fair Trade Commission
(late 1947)
- Trade liberalization (1960s)

Coal production and oil import



Part IV

**Political Economy of
Competition Policy
&
Industrial Policy**

1. Why did Japan stop growing in the last 20 years

- Failure to adopt new competition policy.
 - Policy makers has been reluctant to adopt competition policy since this policy is against the interests of the incumbents with strong political power.
- New industrial policies added.
 - Extremely tempting for policymakers, who can expect kickbacks.

2. New waves of competition Policy (1)

- Privatization of Public Utilities by Nakasone (1980s):
 - Japanese National Railways and
 - Nippon Telephone Telegraph Company.
- Regulatory reform by Koizumi (early 2000s)
 - Privatization of the Japan Post

2. New waves of competition Policy (2)

- Revision of the “Anti-monopoly Law” (2005)
 - Amnesty measures for informers that drastically reduced bid-rigging among major construction companies regarding public enterprise.
- Expansion of its coverage to promote competition in the nursing care industry, which is a heavily controlled by the government.

3. Abenomics(2013-)

- Liberalization of the Electricity Market
 - Coverage expanded to household in April, 2016.
 - Unbundling in 2020.
 - Establishment of EGSC in September 2015.
- National Strategic Special Zone
 1. Corporations can own agricultural land
 2. New medical school
 3. Homestay is legalized despite resistance from the hotel industries

4. More structural reform needed for economic growth in any country

Whether or not Japan can regain its strength depends on how vigorously it can implement competition policy.

This must also be the case for any growing Asian countries.