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**EU Competition Law:
An Unaffordable Luxury in Times of Crisis?**

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EU COMPETITION LAW: AN UNAFFORDABLE LUXURY IN TIMES OF CRISIS?

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ABSTRACT: The paper looks at two aspects of the Covid-19 pandemic. These are (i) the nature of this event and its implication for evaluating past policy and policy into the future, and (ii) the suitability of proposed changes in the implementation of competition policy affecting firm behaviour, market structures and state intervention.

The first conclusion the paper reaches is that it is incorrect to describe the Covid-19 pandemic as a “Black Swan” event, unpredicted and unpredictable, and something for which it is not possible to prepare. Policy makers should accept responsibility for possible future events such as pandemics even when timing is uncertain. In the case of Covid-19, policy measures were clearly inadequate.

The paper then considers the design and implementation of measures aimed at supporting economic recovery. The arguments that competition policy should be relaxed for the duration of the problem is rejected as ill-founded and counter-productive. In particular, it is wrong to treat the response to the Financial Crisis of 2008-2011 as justifying reduced competition in general. Some aspects of particular policy designs, decisions and actions in response to the recession flowing from the medical response to Covid-19 are subjected to critical analysis.

Keywords: COVID-19; Economic recovery

JEL codes: I15, I18

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I INTRODUCTION.

The Covid-19 pandemic has resulted in a major economic recession, the extent and depth of which is unknowable at the time of writing. Concerns arising from the perceived need to ensure the survival of particular firms, or of available capacity, in the context of current economic conditions has led to a view, in some quarters at least, that the goal of supporting economic recovery may require a less stringent approach to the application of competition law coupled with more active state intervention to foster industries considered strategic (“national champions”) and promoting greater self-sufficiency in certain products.¹ While the focus of the present paper is on policy within the EU, such demands are not unique to EU states. Calls for a relaxation of competition rules during serious economic downturns are equally not new. Similar calls were made during the Great Depression² and in the wake of the financial crash a decade ago.³ Nor are such demands confined to downturns as evidenced by the significant scaling back of US antitrust laws over the past 25 years.⁴ Criticisms that EU competition rules inhibit the development of strategically important industries resurfaced following the EU Commission prohibition of the proposed *Siemens/Alstrom* merger when the French and German governments called for a relaxation of European competition policy to favour mergers among large European companies on industrial policy grounds, independent of their impact on competition.⁵

¹ For a summary, see F. Jenny, (2020), *Economic Resilience, Globalization and Market Governance: Facing the Covid-19 Test*, Covid Economics, 1(3): 64-77.

² G.B. Eggertsson, (2012), *Was the New Deal Contractionary?* American Economic Review, 102(1):524-555.

³ For a refutation of such calls, see B. Lyons, (2009), *Competition Policy, Bailouts and the Economic Crisis*, Competition Policy International, 5(2): 25-48; A. Heimler and F. Jenny, (2012), *The Limitations of European Union Control of State Aid*, Oxford Review of Economic Policy, 28(2): 247-267;

⁴ R.H. Lande, (1994) *Beyond Chicago: Will Activist Antitrust Rise Again?* Antitrust Bulletin, 39(1): 1-25; D.I. Baker, (2009), *An Enduring Antitrust Divide Across the Atlantic Over Whether to Incarcerate Conspirators and When to Restrain Abusive Monopolists*, European Competition Journal, 5(1): 145-159; C. Shapiro, (2019), *Protecting Competition in the American Economy: Merger Control, Tech Titans, Labor Markets*, Journal of Economic Perspectives, 33(3): 69-93; and T. Philippon, (2019), *The Great Reversal: How America Turned its Back on Free Markets*, The Belknap Press of Harvard University Press. Cambridge Ma.

⁵ R. Kotzeva, D. Kovo, S. Lorincz, G. Sapi, L. Sauri and T. Valetti, (2019), *Recent Developments at DG Competition 2018/2019*, Review of Industrial Organization, 55(4): 551-578.

Economic nationalism advocating protectionism and isolationism has been on the rise in Western Europe since the early 1990s.⁶

The present paper argues, in the first place, that such policies represent an inappropriate response to the current pandemic induced economic crisis because (a) the crisis does not constitute a Black Swan event and (b) historic experience suggests that such policies are likely to deepen the recession and delay recovery. Secondly, it argues that there are significant problems arising from approaches to policy intervention in response to the impact of the pandemic on economies.

The balance of the paper is structured as follows. The following section considers whether the Covid-19 pandemic constitutes a Black Swan event. In section III we review historic experience and empirical studies to assess whether relaxing competition policy and encouraging larger firms are likely to foster economic recovery. This is followed in section IV by an analysis of state aid/industrial policy and whether these need to be reviewed because of (a) supply shortages during the pandemic and (b) unfair international competition. Some conclusions are offered in the final section.

II IS THE COVID-19 PANDEMIC A BLACK SWAN EVENT?

The concept of a Black Swan event has been applied to the Covid-19 pandemic by some commentators.⁷ As will be seen, this is not really supported by what has happened in the years before it broke out of China, but the importance of the concept is that it more or less exculpates decision-makers from any responsibility for the lack of preparedness to confront the spread of infection.

What is a Black Swan event? The originator of the term sets down three characteristics of an event that must be met if it is to be classified as a Black Swan event.⁸

⁶ I. Colantone and P. Stanig, (2019), *The Surge of Economic Nationalism in Western Europe*, Journal of Economic Perspectives, 33(4):128 -151.

⁷See, for example, I. Kotorchevikj, *Is Coronavirus (COVID-19) a Black Swan Scenario for the World Economy?* April 6, 2020, at <https://read.hyperight.com/is-coronavirus-covid-19-a-black-swan-scenario-for-the-world-economy/>

⁸N.N. Taleb, *The Black Swan: The Impact of the Highly Improbable*, 2nd ed., Penguin, 2010, Prologue, p.xxi.

(a) It is an event that is (colloquially) “unexpected”, where expectations are based on experience and existing knowledge.... “*nothing in the past can convincingly point to its possibility*”. It is *ex ante* unpredictable. Another way of looking at it is a weaker version of this. It is an event that occurs with an *ex ante* probability of occurring approaching zero (while possible, may safely be dismissed) or the non-occurrence of an event that has an *ex ante* probability of occurring approaching 1 (statistically more or less certain).

(b) It is an event that has an extreme impact.

(c) It is an event that, *ex post*, can be seen to have been predictable in terms of explanations offered as to why, how, and when it occurred. These may be illusory.

Illustrative examples of such Black Swan events are the outbreak of World War 1 in August 1914, and mobile personal (and subsequently) “smart” phones in the period after 1990.

It is clear that up to and immediately after Sarajevo until very late in July 1914 a world war was regarded as extremely improbable.⁹ The best evidence for this lies in the behaviour of bond prices. It certainly had a significant impact. An entire historical academic industry has grown, based on offering (frequently contradictory) explanations as to what led to and finally caused the outbreak of hostilities.

Today’s availability of smart cell phones and usage was unexpected. An interesting example of the absence of any such expectation is the well-known 1968 movie, *2001: A Space Odyssey*. It made an educated guess as to how space travel would have developed by the early 21st century, extrapolating ongoing developments in the field. But when a character needed to call home to let his family know where he was, he had to use a telephone booth (with a video screen!) supplied by AT&T. Retrospectively we can see that when the World Wide Web was set up and microchips replaced transistors, permitting miniaturisation, the advent of the smart phone was a predictable event that nobody predicted.

⁹We discount essays in fiction and science fiction in which Britain faces invasions. See William LeQueux, *The Great War in England*, (1897), in which the arrival of help from Germany permits plucky Britain to defeat a French invasion; *The Invasion of 1910* by the same author, in which the Germans invade Britain (1906); H.G. Wells, *The War of the Worlds* (1898), in which the invaders arrive from Mars, and are defeated by the common cold; and Erskine Childers, *The Riddle of the Sands*

So, was the Covid-19 pandemic a Black Swan event? Looking at the above characteristics, it might be thought to have failed the first criterion test, whether the strict or the weaker test is applied. There was a similar pandemic just 100 years ago, in the aftermath of World War 1, loosely referred to as the Spanish Flu epidemic. The spread and lethality of the pathogen was well documented and studied. Differential mortality incidence was well known. The potential spread of “new” diseases and their transmission vectors were well known from history: the Great Plague of Athens during the Peloponnesian War (5th century BC), Justinian’s Plague (6th century AD), the Black Death (14th century AD) and the infection that destroyed Aztec civilisation in meso-America (16th century AD) are well known examples of previous epidemics/pandemics. More recently, and within the past 20 years, MERS and SARS appeared, both related to Covid-19. The latter two were contained and vaccine development started, only to be abandoned when it became clear that containment was sufficient to prevent the spread of the diseases.

That Covid-19 has had a huge impact cannot be denied. It is also incontrovertible that in retrospect the origins and the vectors of transmission of the infection have been objects of research and the source of much new information about the pandemic and its incidence. This has “explained” how the original infection in China has resulted in the incidence of the disease and the numbers who have been killed by it, It also suggests that steps that were not taken, but might have been taken, are contributory factors.

Unless Covid-19 satisfies criterion (a) above, it is not a Black Swan event. This is important if we are considering policy responses to the present situation. The point is that if it is/was a Black Swan event there was never any failure to take steps to prevent it. If you simply cannot predict an event you cannot by definition do anything to affect it, for better or worse. It follows that there is little purpose in identifying and/or quantifying causal events preceding the event in question that could have affected it but did not happen. Such events simply could not happen, since the decisions to make them happen could not have been rationally made if it was a genuine Black Swan event. If it is or was not possible to identify a

(1903) in which preparations by Germany to invade Britain are uncovered by a British intelligence agent on a sailing holiday.

future event as a prediction it is or was also impossible to take steps to affect it. It is only if it is predictable that such steps can be defined and implemented.

The evidence indicates that the risk of a major pandemic was widely recognised. In 2005 and 2006, the US government accumulated a large strategic stockpile of 52 million surgical masks and 104 million N95 respirator masks in preparation for pandemic influenza. About 100 million of these masks were used in 2009 in the H1N1 pandemic and were never replaced. The French government was criticised for having spent large amounts of money on PPE in anticipation of an outbreak of the H1N1 virus which failed to materialise and consequently allowed its stock of protective medical equipment to run down leaving it unable to react to a genuine epidemic.¹⁰

Similarly, the ability of the UK NHS to cope with a widespread flu pandemic was the subject of published reports.¹¹

“The report finds that in a major pandemic the newly reorganised NHS in England is likely to face extra challenges. In part, this is an inevitable consequence of the disruption caused by such a major re-organisation. In a pandemic, when there will need to be clear lines of communication and responsibility, with the centre having capacity to direct personnel and healthcare resources towards areas of greatest need, there is instead fragmentation and a lack of clarity within the newly-created organisational structures about who does what and how the system is co-ordinated. The potential problems stretch from the top, with an ill-defined role expected of the Chief Medical Officer, through confusing multiple and parallel structures embracing the NHS, Public Health England and local government, right down to the front line with its increasing number of private providers.”¹²

¹⁰ Both episodes are described in Jenny, (2020) supra note 1.

¹¹ See, for example, Dame D. Hine, (2010), *The 2009 Influenza Pandemic: An independent review of the UK response to the 2009 Influenza Pandemic*, available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/61252/the2009influenzapandemic-review.pdf retrieved 8th May 2020; and H. Pickles and D. Rowland, (2013), *Getting Behind the Curve: Is the New NHS Ready for Pandemic Flu?* Centre for Health and the Public Interest, available at <https://chpi.org.uk/wp-content/uploads/2014/01/CHPI-report-GettingBehindCurve-Dec-2013.pdf> Retrieved 8th May 2020.

¹² Pickles & Rowland Id. p.4.

In December 2014, President Obama addressed the National Health Institute in the U.S. He warned of the need to prepare for “*the next epidemic*”, an airborne virus epidemic. His immediate concern was American preparedness, but he argued for international awareness of what needed to be done.¹³ In 2015 Bill Gates sounded a warning in a presentation at an online conference after the Ebola epidemic in West Africa.¹⁴ He argued that a pandemic arising from a novel pathogen was a serious probability. At the 2019 Davos Conference his Foundation argued for the need for preparedness against this eventuality, outlining what was seen as a necessary international response architecture to confront it when (not if) it occurred.¹⁵ *Vox clamantis in deserto?*¹⁶

The world was not prepared for Covid-19. The response by the Chinese authorities to a local epidemic in the city of Wuhan may well have generated a pandemic within three months of the first infections. This does not mean that the outbreak of the disease was a Black Swan event. It simply means that governments seriously under-estimated the probability of such a novel pathogen appearing in the near future,¹⁷ and the social and economic costs it would visit on an unprepared world. In the case of the initial and subsequent Chinese responses there are, unfortunately, other, and very disturbing but plausible, conclusions that have been drawn as to the rationale behind decisions of the Chinese Communist Party regime.

From the perspective of economic recovery strategy, classifying the Covid-19 pandemic as a Black Swan (unpredictable *ex ante*) would imply taking no steps to prepare for another such pandemic. If another pandemic is not a Black Swan, but a low probability high risk event, then it is logical to continue to invest continuously to prepare for it. The difficulty here is that as the probability of occurring in any given future period falls for any given event related risk, conventional expected value calculations lead to a declining net present value of

¹³ Speech to members of National Institutes of Health, December 2014, Courier, 16 May 2020, retrieved from www.couriernewsroom.cpm/2020/04/14

¹⁴ TED address, retrieved from www.youtube.com/watch?v/=6Af6b_wyiwl

¹⁵ Contribution to World Economic Forum: *Global Health Security and Epidemic Readiness Accelerator* programme.

¹⁶ Vulgate, Isaiah 40:3, John 1:23

¹⁷ It is ironic that disaster preparations are often described as being required in terms of the likelihood of the event occurring over time. Flood relief plans are usually designed in response to flood predicted periodicity: a 1

resources being used to fund preparations. It is analogous to expenditure on defence. There is a clash between expenditure based on the maxim “*si vis pacem, para bellum*” and probability-based calculations based on some (usually unclear) probability distribution. A classic example of the latter was the guiding instruction in the U.K. for the Admiralty and the War Office in 1919 that their planning and resource needs were to be based on an assumption, of no major war for 10 years ahead. This continued until early 1932.¹⁸

III WILL MORE LENIENT COMPETITION POLICY AID ECONOMIC RECOVERY?

Economic analysis indicates that competition increases efficiency¹⁹ and productivity.²⁰ In contrast, restrictions on competition not only lead to higher prices and reduce consumer welfare, they impede innovation and growth and reduce overall welfare.²¹ Some short-term easing of the rules was required in the face of shortages of essential medical supplies in the wake of the Covid-19 outbreak and the EU Commission response in this regard was welcome. However, such measures are only appropriate as a temporary response. Longer-term, the pandemic illustrates the need for greater coordination in order to develop new drugs and hopefully, at some point, vaccines to deal with Covid-19. Competition policy has long recognised that cooperation arrangements in relation to R&D activities should be viewed positively so long as they do not lead to collusion in product markets or measures aimed at

in 5 year, or 1 in twenty years or 1 in a hundred years categorisation. It is about 100 years since the last great pandemic, but there were few or no preparations to meet the next one in recent years.

¹⁸J. Royo. *British Military Decline, 1919-1939*, Small Wars Journal, 2012, retrieved from <https://smallwarsjournal.com/jrnl/art/british-military-decline-1919-1939> As a result, in 1939 13 of the Royal Navy's battle fleet of 12 battleships and three battle cruisers had been laid down before or during the First World War. There were only two aircraft carriers built as such (as opposed to three converted obsolete battle cruisers) and these had aircraft that were obsolete or obsolescent.

¹⁹ D.S. Hay and G.S. Liu, (1997), *The Efficiency of Firms: What Difference Does Competition Make?* Economic Journal, 107:597-617.

²⁰ R. Disney, J. Haskel and Y. Heyden, (2003), *Restructuring and Productivity Growth in the UK*, Economic Journal, 113:666-694.

²¹ J.B. Baker, (2003), *The Case for Antitrust Enforcement*, Journal of Economic Perspectives, 17(4), 27-50.

eliminating rivals.²² It is unclear that any relaxation of EU competition policy is required to facilitate such efforts.

EU competition policy is sometimes described as too strict and is accused of hindering the achievement of strategic objectives.²³ As we argue below the problem is not that EU competition policy is too rigorous, but rather that US policy has become overly lax.

*“...nothing suggests that Europe implements an ‘excessively rigorous’ competition policy, in the sense that it would hinder development”.*²⁴

The reform of the EU merger control regime was found to have reduced Type 1 errors (wrongly rejecting mergers on competition grounds), while the evidence suggests, if anything, the Commission blocks too few mergers.²⁵

There are two reasons at the outset to be sceptical of claims that competition is likely to impede recovery during severe economic downturns:

(1) Demands for a relaxation of EU competition policy predate the current crisis; and, more importantly,

(2) Because the Covid-19 epidemic is not a Black Swan event, historic experience applies. It tells us that rolling back competition policy during economic downturns is unlikely to promote economic recovery. We illustrate this by considering three historic episodes (a) the Great Depression; (b) the 2008 financial crash; and (c) the erosion of US antitrust law over the past 25 years. While much of this is based on the experience of the U.S., there is also evidence that a lack of competition unnecessarily prolonged the 1990s Japanese recession.²⁶

A The Great Depression.

²² See, for example, J. Ordover and W. Baumol, (1988), *Antitrust Policy and High Technology Industries*, Oxford Review of Economic Policy, 4(4): 13:34; W. J. Baumol, (1992), *Horizontal Collusion and Innovation*, Economic Journal, 102: 129-137.

²³ S. Jean, A. Perrot and T. Philippon, (2019), *Competition and Trade: Which Policies for Europe?* Notes du Conseil d’Analyse Economique, 2019/3 (No.51): 1-12.

²⁴ Id.

²⁵ L-H. Roller and Neven, D., (2002), *Discrepancies Between Markets and Regulators: An Analysis of the First Ten Years of EU Merger Control*. The Pros and Cons of Merger Control, Stockholm, Swedish Competition Authority; and T. Duso, K. Gugler and F. Szucs, (2013), *An Empirical Assessment of the EU Merger Policy Reform*, Economic Journal, 123: F596-F619.

²⁶ M.E. Porter and M. Sakakibara, (2004), *Competition in Japan*, Journal of Economic Perspectives, 18(1): 27-50.

In the 1930s in the US, politicians, journalists and even some economists claimed that Government enforced cartelisation would boost prices and wages, stimulating recovery by ending the “ruinous” or “cut-throat” competition which was widely seen at the time as the primary cause of the Great Depression.²⁷ This led to the enactment of the National Industrial Recovery Act (NIRA), 1933, which encouraged the formation of cartels in US industry and temporarily suspended the antitrust laws in respect of such arrangements.²⁸ Initially, the NIRA was a key element in President Franklin D. Roosevelt’s “New Deal” but was abandoned during his second term. The measures were criticised at the time by Keynes²⁹ and Hotelling³⁰ among others. Shapiro argues that Roosevelt recognised, albeit belatedly, the error of restricting competition during economic downturns.³¹

Most studies of the period have concluded that NIRA cartels raised prices and reduced output thereby prolonging the Great Depression and delaying recovery as predicted by standard economic theory.³² Taylor found that NIRA cartels resulted in a ten percent reduction in manufacturing output.³³ Romer argued that NIRA prevented the economy’s self-correction mechanism from working.

“Thus, the NIRA can be best thought of as a force holding back recovery, rather than as one actively depressing output.”³⁴

²⁷ See, for example, J.E. Taylor and P.G. Klein, (2008), *An Anatomy of a Cartel: The National Industrial Recovery Act of 1933 and the Compliance Crisis of 1934*, *Research in Economic History*, 26, 235-71.

²⁸ The legislation was declared unconstitutional by the US Supreme Court in 1935.

²⁹ In an open letter to President Roosevelt, published in the *New York Times* Keynes argued vigorously against the NIRA’s cartelisation programme, Eggertsson (2012), *supra* note 2. Keynes views were subsequently echoed in M. Friedman & R. Schwartz, (1963), *A Monetary History of the United States 1867-1960*, Princeton University Press.

³⁰ H. Hotelling, (1990) *Curtailing Production is Anti-social* in A.C. Darnell (ed) *The Collected Economics Articles of Harold Hotelling*. Springer, New York, NY

³¹ C. Shapiro, (2009), *Competition Policy in Distressed Industries*, speech to ABA antitrust symposium *Competition as public policy*, 13th May 2009.

³² See, for example, J.C. Miller, T.F. Walton, W.E. Kovacic, and J.A. Rabkin (1984), *Industrial Policy: Reindustrialization Through Competition or Coordinated Actions?* *Yale Journal on Regulation*, 2(1), pp. 1-37.

³³ J.E. Taylor, (2002), *The Output Effects of Government Sponsored Cartels During the New Deal*, *Journal of Industrial Economics*, 50(1), pp.1-10.

³⁴ C. Romer, (1999) *Why Did Prices Rise During the 1930s?* *Journal of Economic History*, 59(1), pp.167-199, at p. 197.

Cole and Ohanian estimate that NIRA caused unemployment to be 25 percent higher than it would have been otherwise and suggest it may have prolonged the Depression by seven years.³⁵

Eggertsson claims that NIRA assisted the recovery, arguing that, in the somewhat unique circumstances of a liquidity trap, cartelisation may contribute to recovery by increasing inflationary expectations. He concedes, however, that expansionary monetary and fiscal policies were the main drivers of the recovery from the Depression and that NIRA played only a minor role.³⁶

B The 2008 Financial Crisis.

In the wake of the 2008 financial crash, calls for a relaxation of competition policy because it was inappropriate during times of crisis were widely rejected. The then Assistant Attorney General for Economics at the US Department of Justice observed:

“...research by historians and economists, support the conclusion that the expansion in output resulting from competition is part of the solution to tough economic times, not one of the causes of economic downturns. Put differently, restriction of output at the industry level, which is the hallmark of a cartel as well as the consequence of the artificial shortage associated with monopoly prices, exacerbates the fundamental economic problem in a recession, namely that production in the overall economy is well below capacity.”³⁷

Jenny argued that competition law should be rigorously enforced during economic downturns.³⁸ Heimler and Jenny also argue against relaxing competition policy during downturns pointing out that competition policy operates counter-cyclically during economic

³⁵ H. Cole and L. Ohanian, (2004), *New Deal Policies and the Persistence of the Great Depression: A General Equilibrium Analysis*, *Journal of Political Economy*, 112 (4): 779-815.

³⁶ *Supra* note 2.

³⁷ Shapiro, (2009), *supra* note 31.

³⁸ F. Jenny, (2010), *The Economic and Financial Crisis, Regulation and Competition*, in *Taiwan 2009 International Conference on Competition Policies/Laws*, edited by the Fair Trade Commission, Executive Yuan, Republic of China.

crises.³⁹ Similarly, Lyons rejects “*crude, populist, deeply-flawed claims that it [competition policy] is an unnecessary luxury in times of recession—or even that the crisis itself is due to ‘too much competition’.*”⁴⁰

The EU Commission, nevertheless, accepted that a more “flexible” application of competition rules was required as part of a response to the ongoing financial sector crisis in particular with respect to Member State measures to support distressed financial institutions.

It is hardly necessary to point out that the financial crisis required responses to the fact that a very large proportion of the major players suddenly discovered that they were “failing firms”. The response of Governments across the world was (in some cases only temporarily) to take them into public ownership, raising questions about “aids to industry”, or arranging shotgun mergers, or both.

However, an aspect of the problems facing the financial sector is that while intermediaries in trouble could well be said to be failing firms, (a) their predicament did not arise from higher costs structures, or a fall in demand for their product variants, but from unwise (to put it mildly) investment decisions (purchases of assets) or creation of liabilities, which had the effect of bankrupting them via their balance sheets without affecting their underlying ability to trade profitably, and (b) that the crisis was not caused by a cyclical or structural fall in demand for intermediation. The reality was that management had bet the banks’ equity (and more) and lost it

There were two broad explanations advanced for the explosion of trade in complex structured financial products prior to the crash. The first suggested that these developments represented a more sophisticated form of risk sharing and risk transfer, an exemplification of the benefit of the creation of new markets. The second was that such transactions were largely driven by information asymmetries: the products were bought by people who simply overestimated their value. In the first case, private profitability is mirrored by public benefits in the form of lower costs of risk. In the second, the private profitability is illusory and disappears when asset values correct themselves. In retrospect, it is evident that the latter

³⁹ Heimler and Jenny (2012), *supra* note 3.

⁴⁰ Lyons, (2009), *supra* note 3.

explanation was closer to the truth.⁴¹ Nor is this merely down to hindsight. Minsky, for example, warned that the fragility of the financial system increases during the expansionary phase of the economic cycle as unrealistic expectations of asset values on the part of one bank are highly likely to be matched by unrealistic expectations by other banks.⁴² Similarly Dow pointed out that valuations of bank assets were contingent on a range of unknowns which meant that it was not possible “to talk in general of the ‘true’ value of a bank’s assets.”⁴³ The collapse in intermediation was not the cause of the crisis but a consequence arising from greater uncertainty and increased risk aversion that flowed from the incipient rash of bank failures.⁴⁴

That suggests that standard failing firm arguments are irrelevant to actions undertaken by regulators and governments to shore up the banking system. Banking is different to other industries because of the potential twin contagions (a) to other parts of the financial system and (b) to the wider economy.⁴⁵ Nevertheless, the fact that the sector was contracting had implications for firms within the sector.

Is it, then, simply an extension of efficiency arguments for mergers that underlies the acceptance by the EU authorities of the actions of national governments to shore up failing banking firms by nationalization or merger? Or is there something else behind the “*too big to fail*” approach?

It is helpful in considering these questions to look at the normal wealth consequences of firm failure. When a firm fails and its assets are redistributed by factor markets, the wealth of third parties (i.e., excluding shareholders) falls by the difference between realised value of the firm’s assets and its liabilities, since this is now worthless. The losses are broadly speaking confined to trade creditors and holders of the firm’s debt paper. These losses may be large in

⁴¹ J. Kay, (2009), *The Rationale of the Market Economy: A European Perspective*, Capitalism and Society, 4(3).

⁴² H.P. Minsky, (1982), *Inflation, Recession and Economic Policy*, Brighton: Wheatsheaf. See also S.C. Dow (1996), *Why the Banking System Should be Regulated*, Economic Journal, 106: 698-707.

⁴³ Dow, Id. p.701.

⁴⁴ Kay (2009), supra note 41, and others have argued that increased uncertainty in the sense of an underlying volatility in asset prices was not the problem, but a realisation that the information set of decision makers was defective. Known unknowns are one thing: unknown unknowns are quite another. In other words, their decisions reflected knowledge concerning financial risks that was simply incomplete. As this became clear, and as wholly unexpected (by them) events occurred, the world appeared to become more uncertain. A good reference on these issues is Taleb (2010), supra note 8.

⁴⁵ B. Lyons (2009), supra note 3.

absolute terms, but they are typically only a proportion (and in many cases a small proportion) of the firm's gross assets and liabilities.

In this context what is meant by "*too big to fail*" as an explanation of intervention to keep a failing firm in existence, or arranging for an acquisition of assets that increases market concentration? Consider railway nationalisation in the UK post 1945, or the establishment of the British Steel Corporation in the late 1960s or the creation of and subsequent nationalisation of British Leyland Motor Corporation during the same period. Another example was using defence contracts to force mergers in the aerospace sector culminating in the duopoly of BAC and Hawker Siddeley, subsequently merged to produce BAe. The rationalisation in all these cases was based on "strategic" or "externality" arguments, or on propositions that there were scale or scope economies that could not or would not be realised if left to market decision-making. In some, however, it was simply a case that the government could not face the employment shock involved in closure and acquisition of assets. In none of these was it the case that too big to fail meant that the impact on third party balance sheets was unsustainable.

The banking firm, especially the modern post big bang banking firm (a multi-product financial intermediary, rather than a "boring" traditional bank) is different from the classic firm threatened by closure in three ways.

First, its *gross* liabilities constitute, directly (e.g., firm or household deposits) or indirectly (interbank deposits and bonds), a large proportion of third-party wealth. Secondly, its assets are for the most part not readily saleable capital assets the value of which is their contribution to production of saleable goods, but the liabilities of third parties or of other intermediaries (and, as we have seen, of varying degrees of certainty as to their underlying income stream to the holder). Finally, their liabilities are held primarily because they are used as a medium of exchange and a liquid store of wealth and are substitutes for cash.

In this context too big to fail means that failure would so affect the assets of other intermediaries as to cause a systemic collapse of the intermediation sector. No matter how big or economically important a car producer is it is hard to envisage circumstances in which a failure by one firm would cause other car producers to fail. It is however hard to see how the failure of a large bank would not threaten the viability of other banks. We have also seen,

unfortunately, that banks can be too big to save in the sense that the high cost of allowing the bank to fail is less than the cost of recapitalising it, however this is done.⁴⁶

Governments therefore had no alternative but to “bail-out” the banks in some fashion,⁴⁷ although questions still arise as to the actual measures adopted. Such measures also sheltered other financial intermediaries from what would have been the expected competitive market consequences of catastrophic bad debts for their solvency by supplying public investment of capital to shore up their balance sheets.

In many cases, the arrangements put in place to rescue banks were explicitly designed to weaken competition between intermediaries so as to increase profitability, in order to repair balance sheets by increasing prices for services sold and reducing prices of inputs. The UK government intervened to rescue *Northern Rock*, although arguably it was not a systemically important bank. Several private offers to buy the bank were rejected by the shareholders.⁴⁸ A rescue merger between *Lloyds TSB* and *HBOS*, which was in severe financial difficulty in the wake of the *Lehman's* collapse, was put in place following a private conversation between the then Chancellor, Gordon Brown, and the chairman of *Lloyds TSB*. The plan represented a “once in a lifetime opportunity” for *Lloyds TSB* as the merger would not have been allowed at any other time.⁴⁹ Vickers argued that there were less anti-competitive alternatives available.⁵⁰ The UK government amended competition legislation to prevent a Phase II investigation of the merger by the Competition and Markets Authority (CMA) which had been recommended by the Office of Fair Trading (OFT). Following the merger, *HBOS's* assets proved to be more toxic than previously realised and the merged entity soon needed emergency state aid. The EU Commission approved the aid without addressing the anti-competitive aspects of the merger.

⁴⁶ A. Demirgüç-Kunt and H. Huizinga, (2010), *Are Banks Too Big to fail or Too Big to Save. International Evidence from Equity Prices and CDS spreads*, World Bank. Policy research working paper 5360.

⁴⁷ Lyons (2009), supra note 3

⁴⁸ Lyons and Zhu (2013) note that the EU Commission failed to explain why these offers were rejected, while the cost of a private bid could not be compared with the cost of state aid provided to *Northern Rock* as the Commission apparently had no criteria for judging whether such bids should be acceptable. B. Lyons and M. Zhu, (2013), *Compensating Competitors or Restoring Competition? EU Regulation of State Aid for Banks During the Financial Crisis*, *Journal of Industry, Competition, and Trade*, 13(1): 39-66.

⁴⁹ Id..

⁵⁰ J. Vickers, (2008), *The Financial Crisis and Competition Policy: Some Economics*. Global Competition Policy (December).

“...it may not be too strong to say that the Commission colluded with the UK government to facilitate an anticompetitive merger with an incomplete remedy. At the very least, it should have required a competitively effective divestiture.”⁵¹

In the wake of the crisis, Vickers recommended far reaching structural reforms of the UK banking system. The UK Government did not fully implement his recommendations.⁵²

In Ireland, reflecting pressure from the EU Commission and the ECB,⁵³ similar solvency problems ended with the Government in effect turning the liabilities of most banking and similar intermediaries into sovereign debt, acquiring a dominant position in terms of ownership of the financial sector, and forcing through restructuring that was widely accepted would have significant negative effects in terms of competition.⁵⁴ Competition legislation was amended to transfer responsibility for decisions on bank mergers from the Competition Authority to the Minister for Finance.

The EU Commission used its state aid policing powers to compel a dramatic restructuring of the European banking system. While significant restructuring of the financial industry may have been required in order to reduce the risk of a repeat of the “too big to fail” crisis, it is far from clear that imposing such restructuring via a series of individual state aid decisions was either the most appropriate or most effective way of achieving such an outcome.

⁵¹ Lyons and Zhu (2013), *supra* note 48 p.63.

⁵² Independent Commission on Banking, (ICB) Chairperson Sir John Vickers, Final Report, September 2011. See also “Vickers says financial reforms are too soft”, *Financial Times*, 14 July 2012.

⁵³ Late in August, 2012, the Irish Government confirmed that the then head of the ECB, J.-C. Trichet, had written to the previous Irish Government in October, 2010, to the effect that unless the Irish Government agreed to a “bail out” and to accept the burden of bad bank debts in Irish based banks, further liquidity financing for the distressed banks would not be forthcoming. The Irish Government, while confirming the existence of the letter, and confirming the broad outlines of its contents, declined to publish it in full, apparently in deference to the sensitivities of the ECB: the ECB considered it a confidential communication.

⁵⁴ **Error! Main Document Only.**In addition to structural interventions such as shot-gun marriages (e.g., merging a major mortgage lender, Irish Permanent with the Trustee Savings Bank and another mortgage lender, First Active, into its parent, Ulster Bank, owned by Royal Bank of Scotland), and mergers of credit unions, Government policy and Central Bank policy was to acquiesce in the potential for reduced competition between intermediaries to help finance recapitalisation costs. The oligopolistic banking structure with the Government as a major share holder in the two largest banks saw bank profitability recover sharply after the crisis. This reflected higher margins on lending and lower losses on operating costs made possible by lower competition between intermediaries. The end result was a rapid return to a higher sectoral rate of return on assets (and profits) than comparator euro zone banks. See C. Nevin, (2018), *Irish Retail Bank Profitability 2003-2018*, Central Bank of Ireland Financial Stability Notes, 2018/10.

Extensive divestment was generally required in return for Commission approval of state aid with a 50% reduction in banks' balance sheets the norm.⁵⁵ Such divestments were frequently imposed as punishment and in the hope that they would discourage moral hazard.⁵⁶ In many cases the Commission imposed behavioural remedies which promoted collusion or price follower behaviour.⁵⁷ Lyons and Zhu argue that the reason for bailing out banks that were in difficulty was to prevent a negative externality that would affect the entire banking system. Rival banks thus benefitted from the preservation of the banking system and they question whether they required further compensation, in the form of protection from competition, at consumers' expense.⁵⁸

The question then arises as to the long-term consequences of such interventions. It now seems clear that greater financial market concentration increases the risk of global financial instability since every concentrated financial player is a counterparty to most, if not all, other major players in the same market. Should one such firm fail the financial viability of all of its counterparties is called into question. Viewed in this light, the increased concentration following the crisis has resulted in the twin ills of greater pricing power and the higher likelihood of another financial crisis. The massive support provided by various governments to troubled financial institutions has established a "*too big to fail*" doctrine which means that implicit guarantees persist indefinitely.⁵⁹

Lyons and Zhu argue that EU Commission policing almost certainly resulted in more systematic and less distortionary rescue and restructuring of the financial sector following the crash than would otherwise have been the case.⁶⁰ It is clear, however, that the Commission at least tacitly acquiesced to a number of anti-competitive mergers, even when effective competition remedies were available, while imposing anti-competitive behavioural remedies

⁵⁵ U. Soltesz and C. von Kockritz, (2010), *From State Aid Control to the Regulation of the European Banking System – DG Comp and the Restructuring of Banks*, European Competition Journal, 6(1), 285-307. They note that "sound" banks were generally treated more leniently by the Commission.

⁵⁶ Id.; Lyons and Zhu (2013), supra note 48.

⁵⁷ In *Fortis Bank*, for example, the Commission imposed a "*requirement to achieve certain margin profit levels in the private banking sector, where the bank has a strong position, to avoid that it uses the aid to undercut competitors*". See EC press release IP/11/406, dated 5th April 2011.

⁵⁸ Lyons and Zhu, (2013) supra note 48.

⁵⁹ See, for example, Kay, (2009), supra note 41; Lyons, (2009), supra note 3; and Lyons and Zhu, (2013), supra note 48.

⁶⁰ Lyons and Zhu (2013) supra note 48.

in many cases which represented unnecessary additional compensation for rivals of aid recipients and imposed unnecessary costs on consumers.

C Rolling back US Antitrust.

Various authors have highlighted how US antitrust laws have been significantly scaled back over the past 25 years by an increasingly conservative judiciary.⁶¹ This has considerably reduced the government's ability to win merger cases, a fact recognised by firms.⁶² US courts have adopted an increasingly hostile approach to monopolisation cases⁶³ and divestiture remedies.⁶⁴ and have made predatory pricing “*virtually per se legal*”.⁶⁵

*“The courts adhere to a static non-strategic view of predatory pricing, believing it to be an economic consensus. But it is an economic consensus most economists no longer accept.”*⁶⁶

Kovacic argues that the US system of treble damages also contributed to US courts steady rolling back the scope of section 2 of the Sherman Act.⁶⁷ Carlton argues that single damages provide an optimal level of deterrence for most section 2 offences.⁶⁸

The enforcement agencies have also adopted a more conservative approach.⁶⁹ Baker points out that during the Bush administration, the Justice Department “*took a narrower view of the*

⁶¹ Lande, (1994), supra note 4; D. Baker, (2009), supra note 4; Shapiro, (2019), supra note 4; Philippon, (2019), supra note 4; and S. Berry, M. Gaynor, and F.S. Morton (2019), *Do Increasing Mark-ups matter? Lessons from Empirical Industrial Organization*, Journal of Economic Perspectives, 33(3), 44-68.

⁶² Shapiro (2019), supra note 4.

⁶³ D. Baker (2009), supra note 4.

⁶⁴ W. Kovacic, (1989a), *Federal Antitrust Enforcement in the Reagan Administration: Two Cheers for the Disappearance of the Large Firm Defendant in Non-merger Cases*, Research in Law & Economics, 12: 173-206 and W. Kovacic, (1989b), *Failed Expectations: The Troubled Past and Uncertain Future of the Sherman Act as a Tool for Deconcentration*, Iowa Law Review, 74: 1105-1150.

⁶⁵ A.I. Gavil, (2006), *Competition Policy, Economics, and Economists: Are We Expecting Too Much?*, in B. Hawk ed. *International Antitrust Law and Policy*, New York. Juris Publications.

⁶⁶ P. Bolton, J. Bradley and M. Riordan, *Predatory Pricing, Strategic Theory and Legal Policy*, p.3.

⁶⁷ W.E Kovacic, *Competition Policy in the European Union and the United States Convergence or Divergence?*, speech, 2 June 2008, available at <http://www.ftc.gov/speeches/kovacic/080602bateswhite.pdf>

⁶⁸ D. W. Carlton, (2007), *Does Antitrust Need to be Modernised?* Journal of Economic Perspectives, 21(3): 155-176. He argues that because cartels are covert and may therefore go undetected damages need to be a multiple of the harm inflicted in order to provide an effective deterrent. Such arguments do not apply to actions that are visible such as vertical restraints and most potential abuse of dominance strategies.

⁶⁹ Lande, (1994), supra note 4.

scope of Section 2 liability and remedies than any of its predecessors”⁷⁰ He argues that during this period the Department repeatedly urged the Supreme Court to review most Court of Appeals decisions in favour of section 2 plaintiffs, and opposed review when the defendant had prevailed in the Court of Appeals.⁷¹ He describes a Department of Justice 2009 paper on the application of Section 2 as

*“...basically an apology for not bringing the kinds of cases that the EC and Member States are regularly bringing, and a generalised amicus brief to the courts to reject most private section 2 cases.”*⁷²

Somewhat unusually the Federal Trade Commission publicly disagreed with the paper.⁷³ Shapiro argues that US merger enforcement over the previous 25 years had been too lax.⁷⁴

Wollmann identifies a significant increase in mergers between competitors following an increase in the Hart Scott Rodino merger notification thresholds, which would previously have been likely to be challenged.⁷⁵ One law firm advised clients in such cases *“it is prudent to avoid rapid and sudden price increases in the first year after closing, particularly if they are not tied to cost increases”*.⁷⁶

Some have called for an even greater curtailment of the antitrust laws arguing that merger enforcement and dominance cases produced no consumer benefits and that enforcement action should be limited to only the most egregious price fixing cases.⁷⁷ Such claims have

⁷⁰ D. Baker, *supra* note 4, p178.

⁷¹ *Id.*

⁷² *Id.*, p.147.

⁷³ *Id.*

⁷⁴ *Supra* note 4.

⁷⁵ T.G. Wollmann, (2019), *Stealth Consolidation: Evidence from an Amendment to the Hart-Scott Rodino Act*, *American Economic Review Insights*, 1(1); 77-94.

⁷⁶ R. Farrington, N. Brumfield, G. Paul, and H. Ying, (2015), *Below-threshold Transactions: Enforcement and Exposure*. Technical Report. Washington, DC: Federal Trade Commission.

⁷⁷ R.W. Crandall and C. Winston, (2003), *Does Antitrust Policy Improve Consumer Welfare? Assessing the Evidence*, *Journal of Economic Perspectives*, 17(4), 3-26.

been vigorously rejected.⁷⁸ Carstensen finds that industry performance improved following the imposition of structural remedies in a number of historic monopolisation cases.⁷⁹

There is considerable evidence that the rolling back of antitrust laws in the US has had a detrimental impact on consumers and led to increased concerns about the political influence wielded by large firms and their ability to engage in “rent seeking” behaviour.⁸⁰ In airlines⁸¹ and hospitals⁸² the failure of the antitrust agencies to challenge mergers has permitted a substantial increase in industry consolidation and led to higher prices and lower service quality. Kwoka found that most US mergers “*result in competitive harm, usually in the form of higher prices*”.⁸³ Ashenfelter et al. state “[t]he empirical evidence that mergers can cause economically significant increases in price is overwhelming.”⁸⁴

Empirical research indicates that aggregate mark-ups in the US remained fairly stable between 1955 and 1980 but increased steadily thereafter from 21% in 1980 to 61% in 2016. This increase in markups coincided with an increase in profitability indicating a rise in market power.⁸⁵ Shapiro cites increased industry concentration and rising price-cost margins

⁷⁸ See, for example, J.B. Baker (2003), *supra* note 21; J.E. Kwoka, (2003), *The Attack on Antitrust Policy and Consumer Welfare: A Response to Crandall and Winston*, mimeo.; G.J. Werden, (2004), *The Effects of Antitrust Policy on Consumer Welfare: What Crandall and Winston Overlook*, AEI Brookings Joint-Centre for Regulatory Studies.

⁷⁹ P.C. Carstensen (1999), *Remedying the Microsoft Monopoly – Monopoly Law, the Rights of Buyers, and the Enclosure Movement in Intellectual Property*, *Antitrust Bulletin*, 44(3): 577-617.

⁸⁰ Scherer and Ross point out that one of the original rationales for the US Sherman Act was to prevent the emergence of large-scale business entities because they would be able to wield undue political influence. F.M. Scherer and M. Ross, (1990), *Industrial Market Structure and Economic Performance*, 3rd ed, Houghton-Mifflin. See also Kay (2009), *supra* note 38 on the political influence of large banks. More recently see N.R. Lamoraux (2019), *The Problem of Bigness from Standard Oil to Google*, *Journal of Economic Perspectives*, 33(3): 94-117 and Phillippon (2019), *supra* note 4.

⁸¹ M.N. Cooper, (2001), *Mergers Between Major Airlines: The Anti-competition and Anti-consumer Effects of the Creation of a Private Cartel*. Statement to subcommittee on Commerce, Trade and Consumer Protection Committee on Energy and Commerce, United States House of Representatives, 21st March 2001; D.L. Moss and K. Mitchell, (2012), *The Proposed Merger of US Airways and American Airlines: The Rush to Closed Airline Systems*, American Antitrust Institute; Berry et al. (2019), *supra* note 61.

⁸² Berry et al. (2019), *supra* note 61.

⁸³ J.E. Kwoka, (2014), *Mergers, Merger Control, and Remedies: A Retrospective Analysis of U.S. Policy*. Cambridge, MA: MIT Press, p.158.

⁸⁴ O.C. Ashenfelter, C. Orley, D.S. Hosken, and M.C. Weinberg, (2014), *Did Robert Bork Understate the Competitive Impact of Mergers? Evidence from Consummated Mergers*, *Journal of Law and Economics*, 57(S3): S67–100, p.S78.

⁸⁵ J. De Loecker, J. Eeckhout and G. Unger (2020), *The Rise of Market Power and the Macroeconomic Implications*, *Quarterly Journal of Economics*, 135(2): 561-644.

and profits as evidence of the need to re-invigorate US antitrust enforcement.⁸⁶ Berry et al. suggest that the rolling back of antitrust laws may have contributed to increased mark-ups in many industries, while acknowledging further research is required. Nevertheless, they observe that “*higher mark-ups imply a world that may require increased antitrust vigilance.*”⁸⁷ Valetti and Zenger point out that merger control should not ignore structural increases in pricing power even if these were due to increased efficiency.⁸⁸ Increased industrial concentration in the US relative to the EU has resulted in increased prices and profit margins in the former along with a decline in investment and innovation.⁸⁹

D More Not Less Competition.

Our conclusion at this point is that both economic theory and historic evidence suggest that calls for a relaxation of competition policy during economic downturns is unlikely to foster recovery. The watering down of US antitrust law demonstrates that weakening competition is likely to increase market power and harm consumers. Anticompetitive behaviour and mergers cause long-term harm⁹⁰ and market power can prove durable once it has been acquired.⁹¹

It has also been suggested that, in the current crisis, competition policy should focus more on exploitative behaviour such as “excessive” pricing and pay less attention to exclusionary conduct. Such calls have been prompted partly by massive price hikes for essential medical supplies following the Covid-19 outbreak. Ignoring exclusionary conduct would, in our view, be a mistake, while actions against excessive pricing are only appropriate in extremely limited circumstances.

Turning a blind eye to exclusionary conduct will enhance the ability of dominant firms to eliminate competition. Shapiro points out that new and innovative firms may be especially

⁸⁶ Shapiro, (2019), supra note 4.

⁸⁷ Supra note 61.

⁸⁸ T. Valetti and H. Zenger, (2019), *Increasing Market Power and Merger Control*, Competition Policy Debate, 5(1): 26-35.

⁸⁹ Jean et al. (2019), supra note 23; Philippon, (2019), supra note 4.

⁹⁰ B. Lyons, (2009), supra note 3.

⁹¹ Berry et al. (2019), supra note 61.

susceptible during a recession to exclusionary behaviour by dominant firms.⁹² Similarly Berry et al. argue

*“the most useful focus for antitrust enforcers around the globe should be on conditions of entry, including acquisitions by existing firms of recent or potential entrants, along with exclusionary conduct.”*⁹³

Actions against excessive prices pose some extraordinarily complex problems and such an approach may well be the start of a slippery path.⁹⁴ Price increases provide essential signals to producers and can therefore trigger a supply side response. As Motta points out, however, supply is not equally responsive for all products. Face masks, protective garments, or certain disinfectants are relatively easy to produce, and in most countries affected by the crisis, supply of these products has increased substantially. In contrast, for technologically complex products such as ventilators, a supply side response is unlikely, at least in the short-term.⁹⁵ The need for such equipment may be declining, however: the use of High Flow Nasal Cannulae have been found to make using ventilators unnecessary.⁹⁶

Another concern that has emerged in recent years, is the potential for large firms to acquire entrants in order to eliminate potential competition, often referred to as “killer acquisitions”.⁹⁷ Potential competition is important in technology markets⁹⁸ while acquisitions of potential competitors may be particularly harmful where competition is “for the market”.⁹⁹ Such concerns, in particular, have been raised in respect of tech giants such as Google, Amazon, Facebook, Apple and Microsoft (GAFAM).

⁹² Shapiro (2019), supra note 4.

⁹³ Supra note 61, p..

⁹⁴ M. Motta, (2020, April 22), *Price Regulation in Times of Crisis Can be Tricky*, Business Maverick. Available at

<https://www.dailymaverick.co.za/opinionista/2020-04-22-price-regulation-in-times-of-crisis-can-be-tricky/>

Retrieved 25th April 2020.

⁹⁵ Id.

⁹⁶ See UchicagoMedicineNews, 22 April 2020, at www.UchicagoMedicine.org

⁹⁷ C. Cunningham, F. Ederer, and S. Ma, (2018), *Killer Acquisitions*, Available at

https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3241707 They considered several thousand pharmaceutical mergers and identified 6% of these as having enabled the acquiring firm to terminate competing drug developments.

⁹⁸ Valetti and Zenger, (2019), supra note 88.

⁹⁹ Berry et al., (2019), supra note 61.

The Furman Report commissioned by the UK Government found that these five companies between them made almost 250 acquisitions over the previous five years, none of which was subjected to an antitrust review.¹⁰⁰ As Valetti and Zenger observe while the majority of these were likely to be pro-competitive “*it would hardly be a surprise if at least some of them might raise significant potential competition concerns.*”¹⁰¹

IV INDUSTRIAL POLICY, COMPETITION POLICY AND STATE AIDS.

A “Bigger is Better”

The approach of, and implementation of, competition policy in relation to mergers during recessions may well be affected by scale and scope economies claimed to flow from mergers and acquisitions that result in larger firms. However, the question is not confined to periods of recessions. There is a tradition of using industrial policy to encourage the emergence of “national champions”, large firms seen as being better able to compete at home and abroad along the several dimensions of competition. In this respect competition policy overlaps with industrial policy and state aids. If “bigger is better” is to play a part in policy in the context of recovery from the Covid-19 recession, it must require confidence in the proposition that larger firms are in fact more efficient independently of recessions, and larger size firms do not reduce welfare.

Unfortunately, recent empirical evidence indicates that size does not confer a decisive competitive advantage and its importance has not increased over time.¹⁰² Philippon concludes that there is no reason for special competition treatment for “superstar” firms.¹⁰³ Suggestions

¹⁰⁰ J. Furman, (2019), *Unlocking Digital Competition*, Report of the Digital Competition Expert Panel. Available at

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/785547/unlocking_digital_competition_furman_review_web.pdf

Jean et al. (2019) supra note 23 report that the GAFAMs made a total of 634 acquisitions at a total cost of €142 billion between 1991 and 2018. The high prices paid in a number of instances add to concerns that the transactions may have been anti-competitive.

¹⁰¹ Supra note 88.

¹⁰² De Loecker et al. (2020), supra note 85; M. Covarrubias, G. Gutiérrez and T. Philippon (2019), *From Good to Bad Concentration?* NBER Macroeconomics Annual and University of Chicago Press, forthcoming.

¹⁰³ Supra note 4.

that increased firm size and concentration will promote greater innovation are also wide of the mark. The evidence suggests that mergers in innovation markets reduce innovation by the merging firms relative to its pre-merger level and that any response by non-merging firms is insufficient to offset such a reduction.¹⁰⁴ Increases in market power are likely to degrade investment, innovation, total output and income distribution.¹⁰⁵ This is supported by Philippon who finds evidence of increasing market power in US industry has been accompanied by declining investment, particularly in R&D.¹⁰⁶

B State aid.

State aid is likely to distort competition by enabling inefficient firms to remain in business potentially at the expense of more efficient producers. It also weakens the incentives for firms to compete. Within the EU state aid may represent a “beggar thy neighbour” policy¹⁰⁷ and result in a wasteful subsidy race between Member States resulting in a significant waste of public money. State aid controls may therefore provide useful cover for EU Member State governments.¹⁰⁸ In the EU context, state aid may create trade and competition distortions within the internal market.

*“The founders of the EU understood very clearly that the internal market should be protected from member states favouring their own companies. The Treaty introduced provisions to this effect, and awarded the European Commission the task of state aid control.”*¹⁰⁹

Hay argued that state aid should not be firm specific and should focus on activities such as R&D.¹¹⁰ The modernization of the state aid rules has established a framework for the

¹⁰⁴ B. Buehler, Coublucq, C. Heriton, G. Langus and T. Valetti, (2017), *Recent Developments at DG Competition: 2016/2017*, Review of Industrial Organization, 51(4), 397-422.

¹⁰⁵ C. Syverson, (2019), *Macroeconomics and Market Power: Context Implications, and Open Questions*, Journal of Economic Perspectives, 33(3) 23-43.

¹⁰⁶ Supra note 4.

¹⁰⁷ K. George and A. Jacquemin, (1992), *Dominant Firms and Mergers*, Economic Journal, 102: 148-157.

¹⁰⁸ B. Lyons and Zhu, (2013), supra note 48.

¹⁰⁹ M. Motta & M. Peitz, (2020, April 18), *EU State Aid Policies in the Time of Covid-19*. Available at VOX CEPR Policy Portal. <https://voxeu.org/article/eu-state-aid-policies-time-covid-19> Retrieved 24th April 2020.

¹¹⁰ D. Hay, (1987), *Competition and Industrial Policies*, Oxford Review of Economic Policy, 3(3), 27-40.

implementation of projects that are difficult to finance because of the technological or financial risks they present, even though they allow significant challenges to be met. This legal framework, known as Important Projects of Common European Interest (IPCEI), provides for significant amounts of aid to large industrial projects. The eligibility criteria require that aid targets an entire sector and not individual companies that would be chosen *ex-ante*, and that the benefits should not be limited to a single Member State. These criteria prevent the aid in question from reducing the strength of intra-European competition.¹¹¹

Even before the crisis there were questions about the effective policing of state aid within the EU. It is argued that EU rules provide an inadequate deterrent to granting illegal state aid.¹¹² Earlier we illustrated the problems with the EU Commission policing of state aid during the financial crisis. Further potential problems arise as a result of the Commission's 2012 state aid modernisation (SAM) which further decentralised the application of state aid rules to individual Member States.¹¹³ The purpose, as in the case of the 2003 reform of competition rules was to enable the Commission to focus on dealing with the most important cases. Clearly, however, there is potential for the uneven application of rules despite the Commission's efforts to ensure uniform application at the best of times.¹¹⁴

*“In its Communication on State Aid Modernisation (SAM)(12), the Commission points out that State aid policy should focus on facilitating well-designed aid targeted at market failures and objectives of common interest of the Union, and avoiding waste of public resources. State aid measures can indeed, under certain conditions, correct market failures, thereby contributing to the efficient functioning of markets and enhancing competitiveness.”*¹¹⁵

¹¹¹ See Jean et al. (2019) supra note 23.

¹¹² P. Nicolaides, (2002), *Control of State-aid in the European Union – Compliance, Sanctions and Rational Behaviour*, *World Competition*, 25(3): 249-262.

¹¹³ Commission of the European Union, *Communication on State Aid Modernisation*, COM (2012) 0209 final.

¹¹⁴ For a discussion see C.M. Colombo (2019), *State Aid Control in the Modernisation Era: Moving Toward a Differentiated Administrative Integration*, *European Law Journal*, 25: 292-316. Schaub cautioned “the entrustment of administrative state aid control to the authorities of the Member States would not be advisable.” A. Schaub, (1998) *EC Competition System: Proposals for Reform* in B. Hawk ed., *International Antitrust Law & Policy*, Juris Publications. New York.

¹¹⁵ OJ C99/03 4th April 2014, paragraph 8.

State aid should also be effective, and proportional to the aims it intends to achieve. The current crisis fits the description of market failure. As in the case of the banks during the financial crash, state aid is necessary to avoid long-run consequences for European firms, workers, and their human capital.¹¹⁶

The EU Commission adopted a “*Temporary Framework*” for state aid schemes aimed at ensuring firms’ access to liquidity and finance, and at preserving employment.¹¹⁷ The framework outlines some limiting principles, designed to establish their temporary nature and to ensure their effectiveness and their incentivising nature. For example, firms which were already in difficulty by 31 December 2019, i.e. before the crisis, cannot access most measures.

At the time of writing, the EU Commission is considering the extension of the state aid temporary framework beyond liquidity support and employment preservation, to include the recapitalisation of businesses.¹¹⁸ Such support may exceptionally be necessary in the current crisis. The problem is that if only some Member States can afford such aid, competition will, by definition, be distorted. Alternatively, States may end up in a subsidy race,

Motta and Peitz argue that the EU Commission should limit state aid schemes which go beyond liquidity and employment support as much as possible and impose stringent conditions on them. They point to the need for a credible restructuring plan to be approved before any such recapitalisation and highlight the need to avoid public money being provided to firms and industries which are unlikely to be viable in the long run.¹¹⁹ In this context it should be noted that in the background policy measures are being introduced for disease control reasons that will have significant effects on the medium to long term as well as short term prospects of certain sectors. The hospitality sector is an obvious example. Consider the impact of “social distancing” in a sector that accounts for a typical 10%-15% of GDP. If we

¹¹⁶ Motta and Peitz, (2020), supra note 119.

¹¹⁷ European Commission (2020a), *Temporary Framework for State Aid Measures to Support the Economy in the Current COVID-19 Outbreak*, Communication of 19 March 2020, C(2020)1863, OJC 091I of 20.3.2020, p.1. European Commission (2020b), *Amendment to the Temporary Framework for State Aid Measures to Support the Economy in the Current COVID-19 Outbreak*, Communication of 3.4.2020 C(2020) 2215 final.

¹¹⁸ European Commission (2020c), “*Coronavirus: Commission Statement on Consulting Member States on Proposal to Further Expand State Aid Temporary Framework to Recapitalisation Measures*”, Brussels, Statement/20/610, 9 April.

assume that social distancing implies higher operating costs and lower consumer demand simultaneously, it is logical to predict a fall in output, a fall in the number of suppliers and a fall in employment. When the economy recovers these sectors will still contract. Firms will exit the market(s). Employment will fall. In such circumstances the case for financial supports that “*keep employees linked to employers*” and reduce costs to employers and owners must be rather weak.

Several Member States are planning public recapitalisation of airlines. The news that the German government is proposing to take a 25% shareholding in Lufthansa is a case in point. Lufthansa needs the injection to survive, and clearly could not obtain that injection at a zero required rate of return based on prospects of future profits. What aspect of Lufthansa’s problems can be said to indicate a case of market failure? Over the last 20 years airlines just as big as Lufthansa disappeared in the United States...TWA, Pan Am, Continental, Northwest... In Europe, Sabena Swissair and BMI disappeared. Not surprisingly, there is a queue of candidates for state support in the sector. The exiting of airlines in the U.S. has not involved a fall in availability at cost covering prices. The fact is that there are probably too many airlines in the EU.

Motta and Peitz argue instead for a well-funded EU aid programme backed by EU money. They suggest that such a programme should pay particular attention to sectors such as energy and mobility that are of European importance and required important structural changes even before the current crisis. While acknowledging the legal constraints to raising European debt, they urge that this is the right time to push for such a proposal.¹²⁰ One key advantage of an EU programme over national ones backed by so-called Eurobonds is that it would avoid the moral hazard problems some fear in the latter case.

C Globalisation, supply chains and industrial policy.

The experience of many countries in relation to access to medical supplies has focussed the

¹¹⁹ Supra note 118.

¹²⁰ A. Benassy-Quere, R Marimon, J Pisani-Ferry, L Reichlin, D Schoenmaker and B. Weder di Mauro (2020), *COVID-19: Europe Needs a Catastrophe Relief*, VoxEU.org, 11 March.

attention of policy makers and commentators on supply chain problems. What is of immediate importance in this respect is the heightened perception that the level of dependence on uncertain availability of supplies imposed systemic risks on countries' health services. Furthermore, it has become evident that (ignoring unit cost considerations for the moment) alternative domestic production was a possibility, if only perhaps a marginal contribution to meeting demand. What has followed from this is a critical consideration of risk management, particularly for smaller countries, in an increasingly globalised world economy.

From a purely economic standpoint, this may usefully be considered under two headings. The first is the optimality of the degree of vertical dis-integration of production (the growth of vertical intra-industry trade). The second concerns what might be called a Black Swan analysis of globalisation and Covid-19, the exposure to unquantifiable risks and the mitigation of such risks.

It is an expected outcome of free trade that competitive advantage leads to countries' imports being much more heterogeneous than their exports. This is true regardless of the actual structure of production in the economy, reflecting specialisation in export production and diversification of imports to meet final demand. This tendency is further enhanced when export and import-substitute production engage in vertical disintegration (out-sourcing of inputs) in order to improve competitiveness, with cost considerations driving increased dependence on imported rather than domestically produced inputs.

Conventional economic analysis indicates that rational input supply choices will reflect more than simple unit cost considerations. It is common for a firm to organise input supply on the basis of both "in-house" production of intermediate inputs and purchases from other producers. This may reflect seasonal variability of production, with "base load" being produced in house but marginal and/or seasonal volume requirements being met from external production. In other circumstances inputs may be fully supplied by production external to the end production stage. The automobile sector is a classic example of this. The Pharma sector in Ireland is another example.

It follows that policy measures designed to reduce vertical intra-industry trade (e.g.,

Trumpian measures to “bring home” some of the out-sourced supply) as a mechanism to offset exposure to unanticipated interruptions involve non-trivial costs in terms of organisation of supply, with consequences for competitiveness.

It is reasonable to assume that in reaching decisions on location of production stages firms will be conscious of risk associated with supply chain structures. We can think of this analogously to insurance against business disruption. The firm in opting for disintegrated production accepts a risk-cost or self-insures. As with conventional insurance, the implicit cost reflects the expected cost of disruption. As a general proposition it seems reasonable to assume that the observed dependence on imported inputs reflects the “private” risk cost (the costs to the firm of some disruption affecting its activities independently of the activities of other firms). Problems arise when something happens that affects all firms, war, for example, for which no cover is available. In this respect, firms that self-insure against business disruption to supply are under-insured individually and in the aggregate. Put another way, the vertically disintegrated structure of production that sources inputs abroad may involve societal risk in excess of the perceived risk to individual firms. Consequently, firm level decisions on supply chains may be sub-optimal.

How could this under-insurance problem be solved? It is possible to think up sophisticated fiscal mechanisms. For example, a corporation tax credit related to inventories would encourage stock holding in excess of “just-in-time” supply arrangements. Alternatively (and certainly preferred by the bureaucracy for a variety of reasons) you could impose regulations setting down minimum inventory standards, thus raising costs for firms rather than reducing inflows to the Exchequer. Finally, the State can act to organise public purchase for storing.

In many cases, medical supply shortages in face of Covid-19 were due to government decisions to reduce supply stocks and ignore repeated warnings about the need to be prepared for a major pandemic. The problem therefore was one of government failure rather than market failure. Clearly, the problem would have been mitigated if governments had maintained some stocks of emergency supplies.¹²¹

This points to a strong preference for using the price mechanism (e.g., the tax credit just

mentioned) to remedy over-exposure to risk via the supply chain. Not only is the use of regulation immediately exposed to capture by political pressure groups (including bureaucratic self-interest), but regulation itself can be captured by those who are being regulated. It is inherently opaque rather than transparent, meaning that costs and benefits are difficult to measure.

Further, the potential for a domestic supply side response varies greatly between products and the appropriate response will vary accordingly. Where supply can respond quickly (as demonstrated with PPE) governments can insure against supply side disruptions through a combination of maintaining adequate stocks and contracting with domestic producers to switch to producing such equipment if required in times of crisis. Thus, it should not be assumed that the solution to supply risks involves moving to self-sufficiency in all cases.

D Collective security and strategic trade initiatives.

The experience of several countries in seeking to secure PPE and ventilator supplies in February to April 2020, has been an object lesson in terms of strategic trade policy. Problems arose first in relation to quality of supply.¹²² There also appears to have been some incidents of breaches of contracts in terms of pricing.¹²³

In this context, the behaviour of the Chinese authorities has been a textbook example of strategic trade intervention. For all practical purposes China was the only supplier available to meet increased world demand for Covid-19 related medical supplies, PPE and respirators. Production in China was characterised by numerous suppliers with little incentive to worry about product quality and faced with cut-throat competition among customers to obtain

¹²¹ Of course, by failing to maintain adequate stocks, Governments avoided the true cost of relying on distant suppliers, which distorted purchasing decisions.

¹²² See for example Minister for Finance, April 3: PPE received from China was not standard required, retrieved [irishtimes.com/breakingnews/ireland/...991987](https://www.irishtimes.com/breakingnews/ireland/...991987); also, Guardian 4 May, report 250 respirators from China dumped as dangerous to use: [theguardian.co.uk-news/2020/apr/30/entire.order](https://www.theguardian.co.uk-news/2020/apr/30/entire.order)

¹²³ See for example complaint by Northern Ireland Finance Minister on April 3 that an order, jointly with RoI, had not been completed because other larger countries had “moved in”, retrieved at [bbc.com/news/uk-northern-ireland-52091054](https://www.bbc.com/news/uk-northern-ireland-52091054)

supply. Product went to the highest bidders while quality was of secondary importance.¹²⁴

Longer term, this posed a problem for China since product quality and supply certainty are supremely important for its exports. Moreover, poor quality and high prices were inducing a switch in the US to higher cost domestic suppliers.¹²⁵ The Chinese authorities moved to intervene to ensure quality control by regulatory intervention at airports (the products were entirely dependent on air-cargo delivery). The quality control intervention increased overall transport costs, but in the circumstances, this was largely borne by the end users.¹²⁶ Combined with reserving supplies in the first place to meet domestic demand, this resulted in shifting the terms of trade strongly in China's favour as higher prices were secured for a reduced volume of exports.¹²⁷

In a sense, China was doing what has characterised coffee exports from Colombia for 60 years. Having invested heavily in branding Colombian coffee, the marketing board secured monopoly control over exporting. This was used to sustain higher prices with the surplus being returned to the growers, whose exportable output was determined by the board. This has been imitated in other coffee producing countries.

The ability to secure and maintain rents through exports depends on being a large producer relative to total demand and on a fragmented market on the demand side. It means a transfer of real income from the consumers to the producers as in any cartel. As with any cartel, the transfer is limited by two factors. The first is the potential for domestic production in importing countries. In the UK an inability of the NHS to shift its sourcing to domestic PPE producers left it to that extent exposed to problems arising from China.¹²⁸ In contrast, the

¹²⁴See Financial Times International, April 13 retrieved at [ft.com/content/22430f34-cb50-4f43-80eb-e2a28b88078e](https://www.ft.com/content/22430f34-cb50-4f43-80eb-e2a28b88078e).

¹²⁵ Id.

¹²⁶See Lodestar (cargo trade magazine) April, 2020, retrieved at [thelodestar.com/china-crackdown-on-shoddy-ppe...](https://www.thelodestar.com/china-crackdown-on-shoddy-ppe...) See also RTE, April 19, [rte.ie/news/hse-ppe-equipment-concern...](https://www.rte.ie/news/hse-ppe-equipment-concern...): RTE reported that tighter export controls in China were resulting in higher costs of PPE and delays in delivery.

¹²⁷C.P. Brown (PIIE), *China Should Export More Medical Gear to Combat COVID-19*, Peterson Institute for International Economics, May 5, 2020, retrieved at [piie.com/blogs/trade-and-investment-policy-watch/china-should-export-more](https://www.piie.com/blogs/trade-and-investment-policy-watch/china-should-export-more).

¹²⁸ For example, media reports indicate that more than 8,000 UK firms responded to UK Government appeals for medical equipment but many of them complained that the authorities failed to respond to such offers. BBC News (21st April 2020), Government: 'has 8,000 offers from PPE suppliers'. Available at <https://www.bbc.com/news/uk-politics-52369223> Retrieved 24th April 2020.

development of shale oil production in the U.S. effectively capped oil prices other than in the short term. Similarly, Jenny argues that in France the absence of a ministry for industry hampered efforts to source supplies domestically.¹²⁹

The second is the potential for countervailing power through purchaser concentration. The divided response of EU Member States rather than a common set of measures across them left individual countries with limited bargaining power and capability to retaliate against discrimination. As a bloc, however, the EU accounts for at least 60% of the effective demand for PPE etc. from China. It is in the EU's interest at a time like this to try to harness the purchasing power of its Member States to set the terms for price and quality for these imports, just as it is in their interest to support EU solidarity in obtaining markets for their exports in a world that pays lip service to free trade, but little else.

E Avoiding protectionism

The current US administration has tapped into a significant and deeply rooted isolationist and unilateralist attitude to all the dimensions of foreign policy. It would be unwise to assume that there would be a qualitatively different approach to trade policy in the U.S. if there were a change at the White House in 2021. The tone would certainly change, but it is not at all clear that there would be a full-scale reversal of policy stance.

It is understandable that the EU could consider reacting to this trend in American policy on trade relations by countering it with a retaliatory shift towards a protectionist regime affecting the EU. It is what you would expect in the prisoner's dilemma model of a non-cooperative game in such circumstances. It is also supported by considerations of strategic trade policy, since US protectionism would not simply be isolationist in aim, but also would aim at improving the terms of trade from an American perspective.

Allied to this are concerns about "unfair" competition because other countries do not apply similar rules with respect to competition, environmental standards and so on. Jean et al argue that greater insistence by the EU on reciprocal market access provides a more effective way

¹²⁹ Jenny, (2020) supra note 1.

of addressing such problems than protectionist measures.¹³⁰

A further source of protectionist pressure is the “prisoners’ dilemma” identified by Krugman whereby expansionary fiscal measures by individual countries to kick-start their economies benefit other countries by increasing the expanding country’s demand for imports.¹³¹ He acknowledges that such difficulties could be overcome if all countries adopted a similar fiscal stance. While such a solution may not be feasible worldwide, a coordinated EU fiscal response could at least mitigate this “prisoners’ dilemma” as import leakages for the EU would be lower than for individual Member States.

F Immediate initiatives.

If, however, we are facing into a permanent change in social distancing in employment and provision of services we have to accept that previous levels of employment in a variety of occupations will not be restored. The same applies to changes in the distribution and communications sectors.

The implication of this is that scarce fiscal resources should not be spread thinly everywhere but targeted on sectors that are more likely to expand. Statements that SMEs are the backbone of the economy, and consequently resources should be allocated to supporting employment in such enterprises should not be made or accepted unquestioningly. In an open economy it is production of tradable goods and services and of inputs to these that in the long run determines total output and employment. Size is not relevant unless smaller firms are somehow more productive or more flexible.

We have already drawn attention to the question of providing support to a flag carrier airline. The EU Commission view is that there are too many airports (a surplus capacity based

¹³⁰ Jean et al., (2019) supra note 23 note that, in a limited number of sectors where sunk costs are very high and/or network or scale effects are particularly important, firms may benefit from lax competition policies but as such policies are likely to result in higher prices in such markets requiring reciprocal access represents an effective remedy for EU firms.

¹³¹ P. Krugman, (2009) *Protectionism and Stimulus*, blog dated 1 February 2009: <http://krugman.blogs.nytimes.com/2009/02/01/protectionism-and-stimulus-wonkish/>

on regional pressure).¹³² Moreover, over much of Europe road and rail transport, even with tolls and high fuel taxes, is faster and more comfortable point to point than air transport. The 2014 guidelines on state aids in the air transport sector make clear the basic principles underlying aids. As previously noted, the Commission in its *Communication on State Aid Modernisation* points out that State aid policy should focus on facilitating well-designed aid targeted at market failures and objectives of common interest of the Union and avoiding waste of public resources.¹³³

However, state aids to airlines as affected by treaty obligations were subject to a Commission decision in 2004. This provided a let-out where airlines were concerned on the principles involved as just described: further aid was not permitted *unless under exceptional circumstances, unforeseeable and external to the company*.¹³⁴ It would be hard to describe Covid-19 as not covered. However, whether permitted or not, it is a matter for concern that once again “flag carriers” are being singled out for special treatment under cover of “too big to fail” arguments that are patently spurious, and are simply masking political pressure. In relation to airlines and air transport infrastructure the continuation of the 2004 let-out constitutes a major failure on the part of the EU Commission.

The issue of state aids also raises “level playing field” issues as between member states of the EU.¹³⁵ These are at the micro-economic and macro-economic levels. At the micro economic level, it is obviously possible for Member State governments to design the structure of intervention supports for businesses and the labour market to offset Covid-19 difficulties in such a way as to affect competitiveness relative to other member states. At the macroeconomic level there is reason to think that countries’ financial requirements to offset the impact of Covid-19 on economic activity will be found to be inversely related to countries’ financial solvency position (debt to GDP ratio). The proposal for “Corona bonds” can be seen as a mechanism to deal with this problem. However, by creating a Euro zone

¹³² Communication from the Commission:: *Guidelines on State Aid to Airports and Airlines* (2014/c99/03): In paragraphs 6 and 7 the Commission argues that competition between these airports for traffic has resulted in subsidy incentives to airlines that are distorting transport markets.

¹³³ Supra note 113.

¹³⁴ OJ C350/7, 2004.

¹³⁵ The EU is currently insisting on the need for a level playing field in its discussions with the UK Government

liability instrument that can make it easier for badly affected countries to meet the cost of suppressing Covid-19, you also create the possibility of tackling longer term structural factors affecting relative competitiveness: comparative advantage is not entirely (or even mainly) exogenous. Hence, it is not surprising to see that opposition to “Corona bonds” is mainly from Germany and associated states. This has been explained away as regrettably reflecting a reluctance to share costs on the basis of solidarity. Viewed from this perspective, however, it is an issue of aids to industry on a national level scale. This is the moral hazard risk referred to by Motta and Peitz. It is obvious that not all Member States have the same financial capacity to provide the level of support to their firms, creating the risk of market distortions.¹³⁶ While “Corona bonds” would go some way to solving this, the moral hazard remains: floating off “Corona bonds” involves the potential to export risk. Motta and Peitz, argue that it would have been much better if such liquidity interventions had been offered by an EU-wide fund, in order to maintain the level playing field among EU companies.¹³⁷

The rhetoric as regards recovery is concentrated on employment restoration. This is what lies behind the widely supported mechanism of maintaining the links between employees and their firms even after being laid off. The logic behind this is partly political, partly economic. Politically it maintains confidence in the return to employment after the pandemic subsides. Economically, it makes sense in that it reduces prospective hiring and training costs for firms that are coming out of suspension or returning to pre-Covid output levels.

Direct support for employment is agreed to be necessary, but only as a short-term measure. This is not just because of a hope that they would not be necessary as recovery from the lock-down commenced, but because the fiscal consequences of the intervention were simply unsustainable in the longer term. In Ireland the major component was originally introduced for a three-month period up to 12 June, 2020, but in the last couple of weeks, and against the background of strident demands from leftist groupings in the Dail (Parliament), the Government has effectively abandoned the deadline.

in relation to future trading arrangements post-Brexit.

¹³⁶ *Financial Times*, (2020, May 1), *EU Countries Clash Over State Aid as Rich Inject More Cash*. Germany reportedly accounted for 50% of all state aid granted by EU Member States up to that point and the German government reportedly expects hundreds of companies to seek support.

¹³⁷ *Supra* note 119.

The original justification for the income maintenance element in this package was to maintain links between firms and employees who would otherwise be simply laid off as a consequence of the lock-down. From a competition perspective this is interesting. Any mechanism that ties employees to existing employers is of benefit to employers in that it protects access to investment in human capital among employees. In the case of temporary reductions in labour demand it reduces hiring costs when demand picks up (this is expressly part of the justification of the arrangements in Ireland). From existing employees' perspective the ties make them more attractive to their employers, which gives them a competitive advantage over other potential employees, which restricts competition in the same manner as traditional guild type labour market restrictions (preference to families of existing workers, for example). It is an unavoidable conclusion that in so far as this is effective it works by reducing competition in the labour market on both sides. The implication is that if the objective is to reduce hiring costs to employers when demand picks up it would be preferable to subsidise hiring costs (and, perhaps, reduce firing costs!) rather than reduce competition in the labour market.

V SOME CONCLUSIONS.

Our starting point was that the economic crisis might be seen by some as justifying the need for a less stringent application of competition law, coupled with more interventionist industrial policies and increased trade protectionism. Economics tells us that such views are mistaken and indicates that competition policy can assist with economic recovery as it is anti-cyclical in downturns. This is supported by historical experience, particularly US experience of the Great Depression, the experience of Japan in the 1990s and the financial crash. The steady rolling back of US antitrust over the past 25 years has resulted in an increase in market power with rising mark-ups and profitability. Reduced competition also leads to lower investment and a decline in R&D activity.

Support for “national champions” ignores evidence that in most industry sectors, size does not confer any significant advantage and historical evidence that politicians and bureaucrats

have a poor track record at picking winners. There is an EU mechanism, IPCEI, which provides for significant amounts of aid to large industrial projects but does so in way that eliminates competitive distortions by requiring that aid be provided to an entire sector and not individual companies, and that the benefits should not be limited to a single Member State..

Experience in recent months has exposed weaknesses in global supply chains. Firms and Governments underestimated such risks and chose not to bear the cost of insuring against them, e.g. by holding stocks of PPE having been warned of the risk of a potential pandemic. Purchase decisions may have been distorted because price did not accurately reflect the true costs of reliance on distant suppliers. Nevertheless, in many countries domestic suppliers were able to respond quickly to supply shortages. In the case of some, perhaps many products, the supply chain risk may be managed by a combination of holding sufficient stocks and having contractual arrangements with domestic suppliers for them to switch to producing emergency equipment during a crisis.

Calls for the EU to adopt a more protectionist approach on trade are perhaps an understandable response to unfair international competition, protectionism, and strategic trade policy elsewhere. Collective action by EU Member States using their collective buyer power and insistence on reciprocal market access for EU exports as suggested by Jean et al may represent a better strategy.¹³⁸

The Covid-19 induced economic crisis has severely affected businesses in all EU Member States and will leave many dependent on government support for their survival. There are serious risks, however, this will result in very serious distortions as some Member States are in a better position to provide state aid than others. Motta and Peitz warn that if such *“developments are not discouraged, we shall see an unprecedented volume of state aid which is likely to disrupt the internal market with dramatic long-run consequences.”*¹³⁹ This requires strong and effective preventative action by the EU Commission. The crisis requires a collective EU response, which would require that State Aid funding should be provided at EU rather than individual Member State level, as advocated by Motta and Peitz.¹⁴⁰

¹³⁸ Jean et al., (2019) supra note 23.

¹³⁹ Supra note 119.

¹⁴⁰ Id.

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