Non-standard economics and competition law: reading Michael Porter *Unique value*

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The book

Charles D. Weller (ed.), Unique Value: Competition Based on Innovation Creating Unique Value, © Charles D. Weller, 2004

Ideas

M. Porter, *Competitive strategy: techniques for analyzing Industries and competitors*, 1980

Business analysis

M. Porter, *The competitive advantage of nations*, 1990

Policy context: US/Japan rivalry

- Different set of questions from standard microeconomics/IO
- Ideas presented as relevant for antitrust (among others)

An innovative theory of innovation

- A theory of productivity
- Presented as revolutionary / "economic departments economics"

  "First, put aside any and all familiar theories of economics. The theory is as different from analysing the motion of planets from the sun, rather than from the earth; and of understanding that light is both a particle and a wave, rather than one or the other" (Ch. D. Weller, p. 4)

Key elements

- Productivity – not efficiency – is the central focus
- *Long-term* consumer welfare is the goal
- Resources (knowledge) are unlimited
- Positive-sum competition ≠ Zero-sum competition
- Implications for antitrust:
  - Profits are not an indication of likely violation of the law
  - Not useful to define *the* relevant market

What does Porter say to competition lawyers?

- **Goal** should be productivity growth
- **Tools** need to include
  - "five forces analysis" to evaluate industry competition
  - "diamond" to evaluate health of local competition
- **Justifications** of competition law enforcement: it's good for the economy *and for companies*

Goal: productivity

- Overall aim: improve standard of living
  - Proxy: GDP per capita
  - **per capita income determined by productivity**
    - Productivity= production/resources (human, capital, physical)
  - Productivity governed by innovation
  - Innovation is driven by competition
- Productivity is the "missing link" between competition and standard of living

Hierarchy of goals

Traditional view	Alternative view
Allocative efficiency	Innovation
Static efficiency	Static productivity
Innovation	Allocative efficiency

Normative propositions

- Not so much attention should be given to efficiency justifications
- More attention should be given to product or service *value*
  - Value = prices commanded in the market place
- Innovation concerns overwhelm static efficiency and allocative efficiency concerns

In plain English

- Distinctly pro-business stance
- Capacity to command high market prices should not be seen as a bad thing
  - Is "unique value" another name for market power?
  - How does one control for consumer value?
- Distinctly reminds of Bork
  - distributive issue is set aside

From Goals to Tools for competition law enforcement

- Productivity should be the core criterion in assessment of firms behaviour
  - E.g. merger enhancing productivity should be cleared
  - New legal test
- Methodological question: how should goals be translated into the law?
- Practical question: How can future productivity be assessed?

Analytical tools

- The Five Forces Model
- The Diamond framework
  - Legal sub-tests
- Typology of competition
  - Presumptions

The Five Forces Model

- Threat of entry
- Threat of substitution
- Bargaining power of buyers
- Bargaining power of suppliers
- Rivalry among current competitors

How revolutionary is this framework of analysis?

- Relevant market is not defined
  - Analysis considers the whole industry
- Concentration ratio is not central
- Prices and quantities are not the key indicators of consumer welfare
- Same factors as in the *Merger guidelines* are relevant but
  - Different weights
  - Different analytical structure

The Diamond

- Analytical tool for local competition and externality
- Relevant for assessing the link between innovation and productivity
  - Context for firm strategy and rivalry
  - Factors (input) conditions
  - Demand conditions
  - Related and supporting industries

- Again, discrete factors are familiar
- Difference with traditional analysis lies in the question orienting the analysis (productivity) and the overall structure of reasoning
- Whatever the legal test, presumptions are useful

Two types of competition

Zero-sum competition Based on imitation and price discounting	Positive sum competition Based on strategic rivalry
Homogeneous products/services at low prices	Multiple different values propositions: features, services, processes, price levels
Imitate best practices	Different approach to design, marketing, etc.
Incremental cost improvements	Potential for fundamental process improvements
Little true consumer choice	Lots of consumer choice Expanded market

What is M. Porter telling us?

- Time horizon should be long
  - Crucial in art. abuse cases (e.g. opinion of AG Jacobs in case C-7/97, Bronner)
- What matters is productivity/consumer value
- Common features with other economic discourses:
  - Points to “what really matters”: goals and relevant facts
  - (Deliberately?) confuses consumer welfare with welfare of sophisticated businesses