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**Working Group on the Interaction
between Trade and Competition Policy**

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The Relationship between Investment and Competition Policy

I. INTRODUCTION

For some time now, it has been pointed out that discussions and debates on issues of the liberalization of trade and investment should devote more attention to competition policy. That is to say, in striving for liberalization, it is not enough to merely remove the customs-related barriers to trade that may exist at national borders or ports of entry. Countries will be able to enjoy the benefits of free trade once they establish suitable domestic climates for competition and will ensure that their distribution systems regarding imports do not pose unfair barriers to market entry after the customs clearance stage. Although the same conditions apply to investment, having a competitive market climate will be an even more important factor as investment moves the centre of business operations into a host country.

In general, the relationship between investment and competition is as follows: the promotion of investment fosters heightened competition, which in turn boosts the competitiveness of the enterprises in the host countries of such investment. Nonetheless, the lack of competition law and their differences between countries tend to undermine the predictability of the business environment for corporate investors. This state of affairs can have the effect of distorting or curbing investment activity. This is the reason why we believe it will be worthwhile for this Working Group to explore the complementary relationships between policies on investment and competition, and, in particular, the promotion of investment and the role of competition policy.

II. A POSITIVE RELATIONSHIP BETWEEN INVESTMENT AND COMPETITION

The prime benefits that investment provides in terms of competition have already been underlined in the Secretariat's paper (WT/WGTI/W/38) for the WTO Working Group on Trade and Investment: namely, that the liberalization of investment encourages market participation by new entrants, helps intensify competition in the marketplace by actively encouraging participation by domestic corporations, and ultimately contributes to the strengthened competitiveness of the market as a whole, including its domestic players. Furthermore, it has been reported that market entry by multinational corporations with advanced technologies is an effective way of boosting the efficiency of indigenous companies through technology transfers (UNCTAD World Investment Report 1997).

To give some examples relevant to recent developments in Japan, the Government approved the establishment of bank subsidiaries by foreign securities firms in 1991, relaxed restrictions on entry into the securities business by securities subsidiaries of foreign banks in 1994, and in November 1996 embarked on a series of liberalization-oriented financial reforms that would become known as the Japanese version of the Big Bang (Figure 1). These actions have facilitated entry by a series of foreign-capitalized banking and securities institutions into the Japanese market. This, in turn, has fostered heightened competition in the domestic financial market-place and, as a result, many Japanese financial service institutions have begun pursuing joint ventures and tie-ups with powerful foreign-affiliated financial institutions, particularly in the areas of asset allocation and in the development of new financial products (Figure 2). On some accounts, many domestic financial institutions have been able to effectively translate these collaborative undertakings into a more diversified and qualitatively improved set of financial products and services (Figure 3), while in the meantime they have been able to work to boost the conveniences for their clientele.

One of the notable benefits of competition policy is the promotion of new investment. Once enacted, strong competition policy can help to eliminate domestic cartels, abuses of power by market-dominant companies and other barriers that typically thwart market entry by foreign firms into the host country as regards investment. Furthermore, guaranteeing the competitive business environment for foreign entrants can also help foster heightened flows of investment from abroad.

Figure 1: Chronology of Japanese Steps in Financial Liberalization

June 1985:	Foreign banks allowed to participate in the trust banking business. Universal bank-affiliated securities houses allowed to set up branches in Japan.
June 1987:	Foreign investment advisory companies allowed to operate as investment brokerages in Japan.
Feb. 1990:	Foreign securities houses allowed to operate as securities and investment trust brokerages.
Feb. 1991:	Foreign securities houses allowed to establish subsidiary bank branches in Japan.
April 1993:	Reciprocal, subsidiary-based participation in banking, securities and investment trust industries allowed.
April 1994:	Foreign banks offered a wider range of options for participation in securities subsidiaries.
Jan. 1995:	Licensing requirements relaxed for foreign businesses striving to enter the securities, investment trust and brokerage business sectors.

(Data source: 1998 JETRO White Paper)

Figure 2: Steps to Restructure the Financial Industry in Japan

Feb. 1998:	Joint venture established by Toho Seimei and GE Capital.
May 1998:	Business tie-up by the Industrial Bank of Japan and Nomura Securities.
June 1998:	Broad-based tie-up by Nikko Securities and Travellers Group.

Figure 3: Examples of Expanded Service Offerings by Domestic Financial Institutions

- Telephone banking and Internet banking services.
- 24-hour ATM operation by banking institutions.
- Issuance of money cards that allow bank depositors overseas to withdraw funds in local currency.
- Lower fund transfer service fees as a result of steps to liberalize service fees for foreign currency transactions.

III. NEGATIVE RELATIONSHIP BETWEEN INVESTMENT AND COMPETITION

1. Market dominance by foreign corporations

Progress in the liberalization of investment and steps to encourage the participation of foreign capital in the domestic market-place can pave the way for entry by large multinational corporations that are overwhelmingly competitive. This state of affairs can deal a heavy blow to indigenous companies that are financially or technologically less competitive, leading to a dominance by multilateral corporations in the market. It is relatively easy for such conditions to materialize in industrial fields marked by high initial costs or progressive cost declines, and particularly in those fields where multinationals have a competitive advantage in terms of financial power, technology or other business resources.

However, should this occur in a country that already has an effective set of competition laws in place, the harms will be transient in nature because the liberalized investment environment and a level playing field can be expected to encourage other multinationals, as well as indigenous start-ups, to compete with the dominant multinational.

2. Anti-competitive practices by foreign corporations

Attention has also been drawn to the danger whereby multinationals with monopoly control over a given market may enlist their unique cross-border networks to exclude competitors, pursue restrictive business practices and engage in other forms of anti-competitive behaviour. Should this happen, it would conceivably give rise to a variety of monopoly-based damage, including declines in market efficiency and economic welfare. Such monopolistic abuses of power should be banned by an effective implementation of competition laws. Indeed, to maximize the benefits of investment, it seems vital that host countries have an effective set of competition laws in place (1997 UNCTAD Annual Report on Trade and Competition).

Another point that has been made (Kimura, 1997) is the prospect, particularly in host countries where the market is still relatively small, for individual companies from the industrialized world to exercise monopolistic control through cartel arrangements. This scenario can be avoided or addressed effectively through the implementation of competition laws or through collaboration with competition authorities in counterpart countries, provided the host country already has a set of competition laws.

3. Joint ventures

Additionally, in view of the potential impact on the market competition of mergers between domestic companies, as well as with foreign companies, it will be necessary to implement those competition laws that regulate mergers and acquisitions.

To give an example, the Japan Fair Trade Commission has pointed out a potential problem under the Anti-Monopoly Law in the case of a joint venture between Anheuser-Busch, the US brewer of Budweiser beer, and Kirin, a major Japanese brewer, whereby the former sought to set up in Japan through a joint-venture subsidiary arrangement with the latter. The JFTC has pointed out the problem of the strengthening of the market position of Kirin, which has already enjoyed a dominant position in the rather oligopolistic Japanese beer market. In response, Anheuser-Busch and Kirin reformed their plan significantly to make the joint-venture project temporary and limited in scope.

4. Conclusions

As indicated earlier, many host countries welcome foreign investment on the expectation that it will create more jobs, aid in the transfer of advanced technologies, foster local competition and will ultimately benefit consumers by bringing down the prices on products at the focus of such competition. However, if, as a consequence of heightened investment, giant multinationals with high levels of financial strength and technological prowess eventually gain monopoly control and abuse their monopolistic position in the local market, ultimately the economic welfare of the host country will be undermined. It is therefore essential that host countries for investment work out and enact a set of effective competition laws if they intend to curb such unfair business practices or monopolistic abuses by multinational firms. At present, however, only approximately 70 countries worldwide have laws of such kind in effect; that is to say that the vast majority have yet to complete the law-making process (1997 WTO Annual Report on Trade and Competition).

Conversely, the absence of such legal frameworks can allow domestic industries to unfairly exclude foreign-affiliated companies and other would-be market entrants. That situation would have the effect of curbing the inflow of foreign investment, thus frustrating hoped-for gains in market competition and economic welfare. Yet, the fact remains that even if a country has a set of competition laws in place, unless its laws are similar in nature to the frameworks set up by most other countries, they will undermine the ability of corporations to make reliable projections about the future business environment, thus restraining the flow of foreign investment.

Within this Working Group forum, Japan to date has emphasized the importance of adopting and implementing effective competition laws by drawing examples from its own experiences. We are hopeful that the outcome of the deliberations by this Working Group will be of help to those countries striving to adopt such legislative frameworks. Finally, we look forward to having a meaningful discussion in this Working Group on the role of and potential for international harmonization and co-operation regarding competition policy.
